

# COOPERATIVE MINERAL INTEREST DEVELOPMENT IN THE LONE STAR STATE: IT'S TIME TO MESS WITH TEXAS

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INTRODUCTION .....	385
I. HISTORY OF OIL AND GAS PRODUCTION IN TEXAS .....	388
A. <i>The Pre-MIPA World</i> .....	389
B. <i>The Small Tract Advantage</i> .....	391
II. THE <i>Normanna</i> DECISION .....	392
A. <i>Reaction to Normanna</i> .....	394
B. <i>The Passage of MIPA</i> .....	396
1. MIPA's Requirements .....	397
2. Imprint of Independent Producers on MIPA .....	397
III. UNITIZATION .....	398
A. <i>History of Unitization in Texas</i> .....	399
B. <i>Empirical Studies</i> .....	400
C. <i>Efforts to Pass a Compulsory Unitization Statute</i> .....	401
IV. THE COSTS OF COMBATTING THE ENVIRONMENTAL CONSEQUENCES OF OVER-DRILLING .....	404
CONCLUSION .....	406

## INTRODUCTION

Since the early discoveries of the Spindletop, King Ranch, and East Texas oil fields, the oil and gas industry has dominated the Texas economy. The industry has also played an important role in shaping state politics and culture. The oil boom of the early 1900s created thousands of jobs for ordinary workers and immense wealth for a select few. Early Texas oil barons made headlines because of their lavish lifestyles and often extreme political beliefs.<sup>1</sup> Legendary wildcatter H.L. Hunt typified this oil-fueled exuber-

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1. For an excellent study of the early days of the Texas oil industry and four of the most prominent wildcatters of the time, H. Roy Cullen, Sid Richardson, Clint Murchison,

ance. Hunt became one of the eight richest individuals in the United States after securing mineral rights to the East Texas oil field (the largest oil field in the contiguous United States) from an unscrupulous land man at a poker game. Hunt used his tremendous resources to support conservative politicians (including Joseph McCarthy) and to promote a conservative political agenda.<sup>2</sup> Hunt's politics, particularly his focus on the primacy of individualism and his belief that government intervention posed the greatest single threat to individual liberty, helped to shape the broader neoconservative movement. His political influence continues to resonate throughout the modern political dialogue in Texas.<sup>3</sup>

Before Hunt became a billionaire, he was a wildcatter—an independent oil producer who bought up mineral rights and drilled exploratory wells in the hopes of striking it rich. Hunt, along with other independents,<sup>4</sup> played a large role in the development of Texas oil fields. Independents competed with major oil companies and used their influence in the Texas legislature to maintain a regulatory environment that gave small producers a competitive advantage over large producers.<sup>5</sup> The political sway of independent producers has resulted in Texas' failure to implement an efficient oil and gas regulatory system, and has contributed to unnecessary waste, wells, drilling expense, and environmental harm to the state.

Texas was among the last of the oil producing states to pass a compulsory pooling statute. Compulsory pooling statutes allow state agencies to compel mineral rights owners to combine their acreage to form a spacing unit of sufficient size to prevent waste.<sup>6</sup> Most compulsory pooling statutes require landowners to make good faith efforts to reach private agreement

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and H.L. Hunt, see BRYAN BURROUGH, *THE BIG RICH: THE RISE AND FALL OF THE GREATEST TEXAS OIL FORTUNES* (2009). These men and their fortunes played a large role in shaping state and national politics, and their influence shaped Texas' political landscape that made it so difficult to pass pooling and unitization statutes.

2. Jerrell Dean Palmer, *Hunt, Haroldson Lafayette*, HANDBOOK OF TEXAS ONLINE (June 15, 2010), <https://www.tshaonline.org/handbook/online/articles/fhu59>. In addition to bankrolling two conservative talk radio programs from 1951-63, Hunt published a utopian novel in which he suggested that more votes should be given to the oldest and wealthiest members of society, and that political speech should be limited to print media.

3. See, e.g., Paul D. Carrington, *Big Money in Texas Judicial Elections: The Sickness and its Remedies*, 53 SMU L. REV. 263, 268 (2000).

4. "Independent" simply indicates an individual not affiliated with a major oil company.

5. See Jacqueline Lang Weaver, *The Politics of Oil and Gas Jurisprudence: The Eighty-Six Percent Factor*, 33 WASHBURN L.J. 492 (1994). Part II of the Article is titled "The Texas Legislature and the Conservation Laws: Worshiping the Independent."

6. See *infra* Section I.B, *The Small Tract Advantage*.

regarding royalty allocation before the state will compel pooling.<sup>7</sup> If private agreement is not reached, the state will designate the boundaries of the spacing unit and the well site and allocate royalties on a per-acre basis.<sup>8</sup>

The legislative hesitation was primarily due to compulsory pooling's unpopularity among politically powerful independent producers who benefitted from Texas Railroad Commission (Commission) field rules that gave independent producers a disproportionate advantage. Texas' compulsory pooling statute only gained enough political support after the Texas Supreme Court invalidated the Commission's unfair rules in a landmark case and required the Commission to promulgate new rules that reduced the independents' advantage.<sup>9</sup> The court's willingness to act in promotion of wise resource use, combined with newly aggressive Commission field rules that promoted pooling to increase efficiency spurred the Texas Legislature (Legislature) to act. However, despite the success of the mandatory pooling legislation in combatting waste, there remains little political support for a compulsory unitization statute that would allow producers to maximize secondary recovery efforts in Texas' oil and gas fields.

Today, Texas remains the only oil producing state without a compulsory unitization statute. Whereas pooling allows the operation of a spacing unit overlying a reservoir without regard to the property boundaries that cross the spacing unit, unitization allows the operation of the entire oil field as a single unit. Because unitized fields operate without regard to spacing units that would otherwise overlay the field, unitized field operators are able to place the minimum number of wells needed to recover the resource and, thus, take steps to efficiently manage field pressure. Generally, unitization is more common in secondary recovery efforts, in which producers re-pressurize a depleted field using salt water or carbon dioxide gas to aid in the movement of fluid hydrocarbons through porous geological formations.<sup>10</sup> Part I of this Note examines the court decisions and regulatory context that led to the passage of Texas' compulsory pooling statute, the Mineral Interest Pooling Act (MIPA), in 1965. Part II examines the landmark Texas Supreme Court case that precipitated MIPA, and the administration of the modern version of this statute. Part III of this Note examines Texas legisla-

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7. See, e.g., OHIO REV. CODE ANN. § 1509.27 (West 2014) (requiring that landowners attempt to reach a voluntary pooling agreement before the Division of Oil and Gas Resources Management will issue a mandatory pooling order).

8. See *id.* at § 1509.27.

9. See *Atlantic Refining Co. v. R.R. Comm'n of Tex.*, 346 S.W.2d 801 (Tex. 1961).

10. For a general description of primary and secondary recovery methods, as well as a game-theoretic examination of when and under what conditions rational individual owners will cooperate, see Paula Murray & Frank Cross, *The Case for a Texas Compulsory Unitization Statute*, 23 ST. MARY'S L. J. 1099 (1992).

tors' efforts to pass a compulsory unitization statute, and Part IV discusses the consequences of failing to do so.

## I. HISTORY OF OIL AND GAS PRODUCTION IN TEXAS

The efficiency of Texas' oil and gas production has national and global significance. Roughly thirty percent of the oil produced in the United States comes from Texas, and the proportion is similar for natural gas.<sup>11</sup> If Texas were a stand-alone country, it would be the fourteenth largest oil producing and the third largest natural gas producing country in the world. Energy forecasters project that the United States will become the largest producer of oil and gas in the near future, largely due to the development of Texas shale plays including the Eagle Ford, Haynesville, and Barnett formations.<sup>12</sup> Unconventional development of oil and natural gas reserves will play a critical role in increasing U.S. energy independence from countries like Venezuela, Iraq, and Saudi Arabia, which, in turn, could advance American national security interests.<sup>13</sup> While some of the advantages of increased energy production seem obvious, the specter of H.L. Hunt's individualist political views has hindered efficient production in Texas' oil fields.

Despite Texas' importance as the dominant domestic oil and gas producer, its regulatory system has lagged behind other states. The Lone Star State has a long history of favoring strong private property rights and Texas legislatures have been criticized for resisting policies that would sacrifice individual rights for the sake of the common good.<sup>14</sup> As the history of Texas oil and gas development reveals, an unyielding preference for individual rights can lead to unreasonable results. To avoid severe negative economic consequences, Texas courts have acted in equity to prohibit policies that favored independent producers.

The Texas Legislature responded to the court's decision by passing MIPA, a statute designed to promote cooperative and efficient development

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11. David Blackmon, *The Texas Shale Oil & Gas Revolution – Leading the Way to Enhanced Energy Security*, FORBES.COM, (March 19, 2013, 10:13 A.M.), <http://www.forbes.com/sites/davidblackmon/2013/03/19/the-texas-shale-oil-gas-revolution-leading-the-way-to-enhanced-energy-security/>.

12. U.S. ENERGY INFORMATION ADMINISTRATION, U.S. EXPECTED TO BE LARGEST PRODUCER OF PETROLEUM AND NATURAL GAS HYDROCARBONS IN 2013, (Oct. 4, 2013), <http://www.eia.gov/todayinenergy/detail.cfm?id=13251>; see also U.S. ENERGY INFORMATION ADMINISTRATION, GROWTH IN U.S. HYDROCARBON PRODUCTION FROM SHALE RESOURCES DRIVEN BY DRILLING EFFICIENCY, (March 11, 2014), <http://www.eia.gov/todayinenergy/detail.cfm?id=15351>.

13. See Luis E. Cuervo, *OPEC From Myth to Reality*, 30 HOUS. J. INT'L L. 433 (2008).

14. *Texas Political Culture*, TEXAS POLITICS (2009), [http://www.laits.utexas.edu/txp\\_media/html/cult/](http://www.laits.utexas.edu/txp_media/html/cult/) (describing the three major pillars of Texas' political culture and political ideology as classical liberalism, social conservatism, and populism).

of oil and gas resources. This victory for efficiency is substantial and can serve as a model for how courts and administrative agencies can work in tandem to shape public policy, even in the face of political gridlock. However, the Texas Legislature has not gone far enough. Lawmakers have repeatedly refused to pass a compulsory unitization statute, likely due to reluctance to burden politically persuasive individual operators. In response to the Legislature's failure to act, the Texas Railroad Commission and the Texas Supreme Court have again issued rulings that rely on equitable principles to eliminate some of the advantages of refusing to unitize. The Legislature should follow the lead of the court and pass a compulsory unitization statute, ensuring efficient production, reducing environmental harm, and eliminating waste.

### A. *The Pre-MIPA World*

Professor Weaver describes the United States as “a nation of marginal, idle, and orphaned wells.”<sup>15</sup> Under the common law *ad coelum* doctrine, the ownership of a piece of land extends from the center of the earth up into the heavens. Rights to oil and gas have been primarily based on two theories of property: ownership in place and the exclusive right to drill. Ownership in place is based on the fee simple determinable and gives the property owner an interest in the oil. The exclusive right to drill, by contrast, is a nonownership theory based on a *profit-à-prendre*, the right to enter land and take a part of the natural resources of the land. Under this nonownership theory, a property interest vests in only the person that removes the oil from the ground, however removal of the oil is still limited by the owner's right to exclude others from his property.<sup>16</sup>

The first legal question addressed by the courts was who held title to the extracted oil or gas. In the beginning, there was the rule of capture. This rule holds that “the person who reaches [oil] by means of a well, and severs it from the realty, and converts it into personality” holds title to the oil.<sup>17</sup> Under the rule of capture, a mineral rights owner was entitled to drill a well and produce as much oil as he could without liability for drainage of his neighbor's property. His neighbors were powerless to enjoin his production or to share in its proceeds. Instead, courts held that the best defense against

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15. Jacqueline Lang Weaver, *The Tragedy of the Commons from Spindletop to Enron*, 24 J. LAND RESOURCES & ENVIL. L. 187, 190 (2004).

16. See Colleen Lamarre, Note, *Owning the Center of the Earth: Hydraulic Fracturing and Subsurface Trespass in the Marcellus Shale Region*, 21 CORNELL J.L. & PUB. POL'Y 457, 468-70 (2011).

17. *Kelly v. Ohio Oil Co.*, 49 N.E. 399, 401 (Ohio 1897).

drainage was to “go and do likewise.”<sup>18</sup> Because there may be (and usually are) several owners of surface tracts overlying an oil field, the rule of capture enabled a producer to gain the full benefit of his production while sharing the negative externalities of overproduction (e.g., prematurely lost field pressure) with the other owners. This rule created an incentive to maximize individual production without regard for the negative field-wide consequences of overproduction.<sup>19</sup> This classic tragedy of the commons resulted in “a system that compels [an operator] to increase his [production] without limit in a world that is limited.”<sup>20</sup>

As surely as the nascent oil and gas law encouraged haste, it also created incentive for strategic behavior. Savvy producers acted quickly to strategically place wells to preemptively drain their neighbors’ property. Early producers drilled far more wells than necessary to efficiently recover oil and gas from fields. Images of the Spindletop oil field near Beaumont, Texas in 1903 show oil derricks situated side-by-side as producers scrambled to sink as many wells as possible. These wells pumped at rates far exceeding the maximum efficient rate of recovery, quickly depleting the reservoir’s natural pressure and leaving a substantial amount of oil underground and irretrievable.

Owners seeking to protect themselves from the economic consequences of drainage found no recourse in the courts. A case typifying Texas courts’ approach to oil production and royalty allocation under the rule of capture was *Japhet v. McRae*.<sup>21</sup> In *Japhet*, the owner of a fifteen-acre tract of land, Fischer, leased the mineral rights of the tract to a production company. Shortly after, Fisher conveyed the north five acres to Keeble, who sold three of those acres to McRae. Eighteen months later, Fisher conveyed his remaining ten acres to Keeble, who sold them to Japhet. All of the conveyances mentioned the production lease and each deed provided that the owner should have all rights of the original lessor (including production royalties). Japhet convinced the production company to drill a well on his ten acres, and upon discovery of a large quantity of oil, received a one-

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18. *Barnard v. Monongahela Natural Gas Co.*, 65 A. 801, 802 (Pa. 1907).

19. Oil production exploits natural pressure to force crude oil up the well bore from the reservoir. The efficiency of production depends on two major factors: well spacing and rate of production. Overproduction results in a loss of this natural pressure, which, in the absence of secondary recovery efforts, causes waste by leaving oil underground.

20. Garrett Hardin, *The Tragedy of the Commons*, 168 *SCIENCE* 1243, 1244 (1968).

21. 276 S.W. 669 (Tex. Comm’n App. 1925). Though this case was heard by the Commission of Appeals, the judgment was entered as the judgment of the Texas Supreme Court. *Id.* at 672; *see also* *Kelly v. Ohio Oil Co.*, 49 N.E. at 401, *supra* note 17 (holding that the rule of capture allowed the defendant to drill a series of wells along the lease property line in an intentional effort to drain oil from adjacent tracts; plaintiff could protect his interests by drilling his own series of wells on his side of the property line).

eighth share in production, per the terms of the production company's original lease with Fisher. McRae and Keeble sued, collectively seeking a third of the royalties paid to Japhet. The court, citing a corollary to the rule of capture that "oil is a part of the realty until brought to the surface," held that apportionment of the royalty was unwarranted.<sup>22</sup> Japhet was solely entitled to the royalties produced from his land and his neighbors' only defense was to seek a spacing exception to drill his own well. Clearly, while the holding of *Japhet* may have fit within the bounds of the law of the day, the decision presented an unsustainable solution to the problems created by the rule of capture.

### B. *The Small Tract Advantage*

To combat waste caused by the free-for-all created by the rule of capture, the Commission first implemented spacing rules to regulate the physical location of the wells and later issued prorationing rules (allowables) to control the rate of production. Spacing rules take into account the drainage radius of the particular kind of well—typically, oil wells drain from an area with a radius of roughly forty acres and gas wells from roughly 650 acres, though each field varies based on actual geologic conditions. Prorationing orders "cartelized" Texas oil production: the orders characterized price-reducing overproduction as economic waste and then reduced each well's allowable to prevent that waste, creating artificial scarcity to artificially inflate the price of oil.<sup>23</sup>

While prorationing orders were intended to prevent waste resulting from the rule of capture, their implementation created an incentive for small tract drilling. Allowables set by these orders were determined on a per-well and per-acre basis. For oil wells, the typical formula set total allowables based on a one-half per well, one-half per acre proration formula. For gas wells, the formula set allowables based on a one-third per well and two-thirds per acre proration formula. In either case, the minimum allowable provided for a "living allowable," a condition that ensured operation of the well would still be profitable. This gave small tract owners the ability to

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22. The court's opinion reflected the general lack of understanding of oilfield geology available to experts at the time. Citing the fact that productive wells were often located "side by side" with dry wells, the court noted that the mystifying nature of oil as a fugitive, migratory resource prevented a legal presumption that Japhet's well drained from Keeble and McRae's land. *Id.* at 671. It seems as though a showing that Japhet's well did in fact drain Keeble and McRae's land may have changed the court's opinion in this case.

23. Weaver, *supra* note 15, at 190. Juan Pablo Pérez Alfonso, the Venezuelan politician primarily responsible for the creation of OPEC, used the Texas Railroad Commission as a model for a regulatory entity that used its police power to influence oil prices to reduce economic waste. Cuervo, *supra* note 13, at 572-81.

drain from neighbors' land with impunity. Originally, Texas courts did nothing to stop this practice.

In *Halbouty v. Darsey*,<sup>24</sup> plaintiffs challenged a decision by the Commission to issue a permit for a well on a 0.48-acre site overlying reserves valued at an estimated \$20,000 when the cost of drilling and extraction would be at least \$250,000. To achieve a living allowable, the well would necessarily have to drain a substantial amount of gas from reserves underlying neighboring properties. The owners of the surrounding tracts offered to pool the 0.48 acre tract, but the small tract owner refused, and the appellate court was bound by precedent to approve the unfair allowable: "The unconditional offer to pool the 0.48 acre tract with surrounding tracts in the field can in no event defeat the permit under the facts here. This is not a matter over which the Commission had been given jurisdiction to require, but is a subject for voluntary agreement."<sup>25</sup> The only factors the court considered relevant were the vested right of property owners to recover oil and gas from beneath their land and whether or not the land had been properly subdivided.<sup>26</sup> Independent producers, who were more likely to be small tract owners, fought early efforts to pass a compulsory statute that would reduce the frequency of arguably unfair results such as the *Halbouty* case.

The Texas Supreme Court, however, was not bound by the same constraints that kept the appeals court from changing the status quo and was soon confronted with a case that "presented a clear choice . . . to encourage efficiency and greater ultimate recover in the gas fields, or to allow the old order to reign even in new fields."<sup>27</sup>

## II. THE *Normanna* DECISION

In *Atlantic Refining Company v. Railroad Commission of Texas (Normanna)*,<sup>28</sup> the Atlantic Refining Company, along with another oil company and five individuals (collectively referred to as Atlantic), brought suit

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24. 326 S.W.2d 528, 529-30 (Tex. Civ. App. 1959) (writ ref'd n.r.e.). In Texas, n.r.e. means no reversible error: the lower court opinion may not be entirely correct, but the petition presents no error that is reversible. See THE GREENBOOK: TEXAS RULES OF FORM, Appendix E (Texas Law Review Ass'n ed., 12th ed. 2010).

25. *Halbouty*, 326 S.W.2d at 532 (citing *Dailey v. R.R. Comm'n*, 133 S.W.2d 219 (Tex. Civ. App. 1939)).

26. Shockingly, the court even disregarded the fact that the location of the drill site might create "hazard to life and to property" because those considerations were not grounds on which the Commission could deny a Rule 37 spacing exception. *Id.* at 532-33.

27. JACQUELINE LANG WEAVER, UNITIZATION OF OIL AND GAS FIELDS IN TEXAS (1986) (hereinafter WEAVER, UNITIZATION).

28. 346 S.W.2d 801 (Tex. 1961). This case is commonly referred to as the *Normanna* case because it dealt with allowables on tracts overlying the Normanna Gas field in Bee County, Texas.

to annul a Commission order which set allowables based on the standard one-third per well, two-thirds per acre proration formula for the newly-discovered Normanna gas field. Such a rule “means that 1/3 of the total field allowable must be divided equally among all the wells in the field and that 2/3 of the total field allowable will be divided among all the wells on a per acreage basis.”<sup>29</sup> The appellee, a partnership called Bright & Schiff, owned a 0.3-acre lot<sup>30</sup> adjacent to Atlantic’s tract on the Normanna Field. Although the Commission had established a 320-acre spacing pattern for the Normanna Field, Bright & Schiff applied for and received a Rule 37 spacing exception,<sup>31</sup> which allowed them to place a well on their small tract. Under the Commission’s production proration rule, Bright & Schiff would be allowed to produce over two hundred times more gas per-acre than a well spaced at 320 acres. Expert testimony produced by Atlantic estimated that the total value of the gas underlying Bright & Schiff’s tract was roughly \$7000. However, under the Commission’s rule, Bright & Schiff would be allowed to produce an estimated \$2.5 million worth of gas over the twenty-year life of the well. In addition, if the court approved the Commission’s order, Atlantic would be unable to recover damages for drainage of its field due to the rule of capture.

The trial court, relying primarily on *Ryan Consolidated Petroleum Corp. v. Pickens*,<sup>32</sup> determined that the Commission’s order was valid. In *Pickens*, both Ryan and Pickens applied for permits to drill on recently subdivided lots. Pickens’ permit was approved by the Commission, and Ryan’s was denied. After litigation determined that the permitting process was valid, Ryan sued for an equitable share of the oil produced from Pickens’ well based on Ryan’s proportionate ownership of the tract. Citing the rule of capture, the *Pickens* court refused to grant Ryan’s requested relief. The Texas Supreme Court distinguished *Normanna* from *Pickens*, holding that the rule of capture did not have any bearing on the evaluation of the validity of an order from the Commission. After citing several cases that overturned Commission orders that resulted in disproportionate recovery

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29. *Id.* at 803.

30. The lot was 79 feet wide and 130 feet long, actually slightly less than 0.3 acres. *Id.* at 802.

31. 16 Tex. Admin. Code § 3.37(h). Such exceptions may be granted upon the applicant establishing that a spacing exception “is necessary either to prevent waste or to prevent the confiscation of property.” 16 Tex. Admin. Code § 3.37(a)(3). “Confiscation” refers principally to drainage. *See Gulf Land Co. v. Atlantic Refining Co.*, 131 S.W.2d 73, 80 (Tex. 1939) (defining confiscation as “depriving the owner or lessee of a fair chance to recover the oil and gas under his land, or the equivalent in kind.”).

32. 285 S.W.2d 201 (Tex. 1955). Pickens was famed corporate raider T. Boone Pickens. A year after this case, he founded the company that would eventually become Mesa Petroleum, which he grew to one of the largest independent petroleum companies in the world.

amounts for small tract owners,<sup>33</sup> the court invalidated the Commission's order:

Viewing all the facts in the light of the substantial evidence rule, we think the 1/3-2/3 proration formula is an unreasonable basis upon which to prorate the gas production from this reservoir. It does not come close to compelling ratable production; neither does it afford each producer in the field an opportunity to produce his fair share of the gas from the reservoir.<sup>34</sup>

The *Normanna* court did not offer a rule or standard to guide the Commission other than to say that, "[t]he responsibility rests with the Commission to devise some rule of proration which will conserve the gas in the field in question and at the same time be fair and just to all parties without depriving any of them of his property."<sup>35</sup> However, even in the absence of a clear standard, *Normanna* became precedent for overruling Commission proration orders that were "arbitrary, unreasonable and confiscatory of [operators'] property."<sup>36</sup>

### A. Reaction to Normanna

The *Normanna* decision, handed down on March 8, 1961, caused administrative headaches at the Commission, as well as a flurry of commentary among those interested in Texas oil and gas law. An essay published shortly after the decision catalogued responses from the Commission and various commentators.<sup>37</sup> *Normanna* effectively eliminated the Commission's ability to favor small tract owners over large. In a later order, the Commission outlined its struggle to strike a fair balance between the rights of small and large tract owners in the absence of statutory authority to compel pooling:

[B]ecause of the additional responsibility placed upon the Commission [as a result of the *Normanna* decision], as knotty a problem as has ever been placed before the Commission must be solved, that in

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33. *E.g.*, *Corzelius v. Harrell*, 179 S.W.2d 419 (Tex. Civ. App. 1944) (writ granted, subsequently dismissed as moot) (holding that the Commission was under the duty prorate gas production such that owners of two adjacent tracts would not drain from each others holdings); *Marrs v. R.R. Comm'n*, 177 S.W.2d 941 (Tex. 1944) (invalidating a Commission order because the allowable was "entirely out of proportion" to the oil under each tract).

34. *Atlantic Refining Co. v. R.R. Comm'n of Tex.*, 346 S.W. 2d at 812.

35. *Id.*

36. *Halbouty v. R.R. Comm'n*, 357 S.W.2d 364, 369 (Tex. 1962) (explicitly following *Normanna* in invalidating a 1/3 - 2/3 proration order). This case is commonly referred to as the *Port Acres* decision.

37. Clyde Brown, *Does the Normanna Decision Herald a New Trend in Texas Oil and Gas Regulatory Practices*, 6 S. TEX. L.J. 32 (1961-62).

all probability is best resolved through the use of a special allowable that would encourage a small tract owner to negotiate with his neighbors for fair and just treatment, but would also provide a sufficient allowable to such small tract to encourage a reasonable attitude in such neighbors so that they would endeavor to work out this common problem . . .<sup>38</sup>

The Commission proceeded to establish a default allocation formula based solely on acreage. However, in the same order (in Rule 3(b)), the Commission created an exception for gas wells on tracts fewer than one hundred acres. If an applicant could show that (1) he could not economically operate a well on his small tract based on a per-acre allowable, and (2) that owners of adjacent tracts had refused to pool with the applicant, the Commission would grant the small tract the same allowable that would be available to a one hundred-acre tract. This rule required owners of small tracts to attempt to reach voluntary pooling agreements with their neighbors, but gave them greater bargaining power in the process.

While *Normanna* did not affect the rules in place in the East Texas fields,<sup>39</sup> relatively new field orders subjected to a timely challenge were struck down under the *Normanna* precedent.<sup>40</sup> The combined actions of the court and the Commission, resulted in a de facto compulsory pooling regime. Commentators began seriously discussing the increasing appropriateness of a compulsory pooling statute, and independent producers, who had previously fought tooth and nail to prevent such legislation, hastily composed a bill to present to the legislature.<sup>41</sup>

A fundamental question is why the Texas Supreme Court decided to abruptly engage in such a clear example of judicial activism and overturn over thirty years of precedent. The dissent in *Normanna* argued that the court was “creating compulsory pooling, directly contrary to the legislative declaration of intent that the Commission was not authorized to require that separately owned tracts be unitized.”<sup>42</sup> Of course, while the court never explicitly *required* pooling, its order, combined with the Commission’s new allowable formula resulted in a de facto compulsory regime. Professor

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38. *Id.* at 36 (citing Tex. R.R. Comm’n, O. & G. Docket No. 129, no. 2-46,673).

39. Citing the doctrine of laches, the Texas Supreme Court refused to overturn field rules that producers had acquiesced to in the Hawkins and Yates fields, and the 50-50 proration orders in those fields stood. *See* R.R. Comm’n of Tex. v. Aluminum Co. of America, 380 S.W.2d 599 (Tex. 1964).

40. *See, e.g.*, R.R. Comm’n of Tex. v. Shell Oil Co., 380 S.W.2d 556 (Tex. 1964).

41. *See, e.g.*, Ernest E. Smith, *The Texas Compulsory Pooling Act*, 43 TEX. L. REV. 1003 (1965).

42. WEAVER, UNITIZATION at 127.

Weaver attributes the court's change in opinion to economic pressures caused by excess production and falling prices, combined with the rising price of drilling wells. In addition, newly producing fields, like the one at Port Acres,<sup>43</sup> required more sophisticated management techniques like gas cycling to recover gas condensate that would otherwise be lost if the field were not operated as a single unit. Compulsory pooling had become an economic necessity, and not even the powerful independents could delay the inevitable.

### B. *The Passage of MIPA*

Less than five years after *Normanna*, the Texas Legislature passed the statute that became MIPA.<sup>44</sup> This statute gave the Commission the authority to compel pooling of separately owned mineral interests in the same field upon application by a qualified interest owner and "for the purpose of avoiding the drilling of unnecessary wells, protecting correlative rights, or preventing waste."<sup>45</sup> Pooled units are usually, though not exclusively, formed for primary recovery of oil and gas resources. As stated in the Texas Practice Series,

The purpose of the Mineral Interest Pooling Act . . . is to permit the owner of a tract embracing only a small part of an oil and gas reservoir to participate fairly in the production from the reservoir and, conversely, to protect the owner of a larger portion of a reservoir from unfair drainage from a tract embracing only a small portion of a reservoir.<sup>46</sup>

In order to achieve these goals, MIPA requires that private parties demonstrate that they have exhausted attempts to reach a private agreement to pool, and then gives the Commission the authority to compel pooling. While MIPA was based on other states' compulsory pooling statutes, it is complicated and contains provisions not analogous to those other statutes.<sup>47</sup> Most commentators agree that the purpose of MIPA is primarily to encourage voluntary pooling rather than for the Commission to actually issue pooling orders.

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43. See Halbouty, *supra* note 36.

44. TEX. NAT. RES. CODE ANN. §§ 102.001-102.112 (West).

45. TEX. NAT. RES. CODE ANN. § 102.011 (West).

46. 4 ALOYSIUS A. LEOPOLD, TEX. PRACTICE SERIES - LAND TITLES AND TITLE EXAMINATION § 23.38 490 (3rd ed. 2013).

47. See, e.g., OHIO REV. CODE ANN. § 1509.27 (West 2014).

## 1. MIPA's Requirements

MIPA § 102.011 specifies the elements that must be present before the Commission can exercise authority to force pooling. Courts and commentators have interpreted this section to require: (1) two or more separately owned tracts, (2) lying within a common reservoir, (3) for which field rules have been established, (4) where separately owned interests in oil and gas are within an existing or proposed proration unit, (5) the interest owners have not agreed to voluntarily pool their interests, and (6) at least one interest owner has drilled or proposes to drill a well within the proration unit.<sup>48</sup> In addition, before an applicant receives a pooling order under MIPA, the applicant must first show that she has made a “fair and reasonable offer” to pool.<sup>49</sup>

Certain categories of fields are excluded from the operation of the statute. Reservoirs that were discovered and produced before March 8, 1961 (the date of the *Normanna* decision) may not be pooled under MIPA,<sup>50</sup> nor may lands owned by the State of Texas.<sup>51</sup> Units pooled under MIPA may not exceed 160 acres for oil wells (or 640 acres for gas wells) regardless of the size of the standard spacing unit in the applicable field,<sup>52</sup> and MIPA may not be invoked to pool two tracts that each separately have sufficient acreage to create a spacing unit under the applicable field rule.<sup>53</sup> Finally, an applicant must show that the acreage that she seeks to pool “reasonably appears to lie within the productive limits of the reservoir.”<sup>54</sup>

## 2. Imprint of Independent Producers on MIPA

As might be predicted, a bill drafted by independent producers tended to favor independent producers. For example, MIPA only applies to fields discovered after the *Normanna* decision and does not apply to exploratory drilling. The Commission cannot initiate pooling; so in the absence of an application to pool, operators are still granted spacing exceptions and allowed to drain from neighboring tracts. The pooled unit sizing limit precludes use of MIPA to accomplish field-wide unitization, and the requirement of a fair and reasonable offer forces applicants to negotiate with small tract owners before going through the hassle of an administrative

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48. TEX. NAT. RES. CODE ANN. § 102.011 (West); see also Ronnie Blackwell, *Forced Pooling within the Barnett Shale: How Should The Texas Mineral Interest Pooling Act Apply to Units with Horizontal Wells?*, 17 TEX. WESLEYAN L. REV. 1, 7 (2010).

49. TEX. NAT. RES. CODE ANN. § 102.013 (West).

50. TEX. NAT. RES. CODE ANN. § 102.003 (West).

51. TEX. NAT. RES. CODE ANN. § 102.004 (West).

52. TEX. NAT. RES. CODE ANN. § 102.011 (West).

53. TEX. NAT. RES. CODE ANN. § 102.014 (West).

54. TEX. NAT. RES. CODE ANN. § 102.018 (West).

proceeding. Small tract owners are also allowed to apply for pooling, which enables them to muscle into larger tracts. Finally, small tract owners can elect to pay drilling expenses out of their royalties, allowing them to avoid the front-end financial risk of drilling a dry well.

It is important to note that the appropriate state policy when it comes to forcing pooling may vary according to a number of factors. For example, Ohio and New York require that operators pool tracts *before* they start drilling. This may be because the relatively high degree of spacing unit fragmentation in those states creates a greater interest in up-front authorization (because drilling a well will affect more neighbors). This may slow the development of oil and gas resources, but it preemptively protects the rights of many who may suffer from collective action problems (e.g. high transaction costs) to combat unwanted production if the default right allows drilling. Texas, by contrast, presumptively allows drilling in the absence of pooling. This may be because the relatively light fragmentation of Texas' spacing units means that fewer neighbors will be affected by the drilling of a well.<sup>55</sup> Further, if neighbors do not want the well, there are fewer to organize, which reduces the transaction costs involved in asserting their own property rights.<sup>56</sup> In this sense, Texas sticks to its strong tradition of protecting the property rights of the individual by requiring the affirmative assertion of rights by a wronged neighbor. This balance is part of the reason that MIPA is so effective. This policy, which threatens compulsory action to favor voluntary agreements, should serve as a model for Texas legislators to pass a compulsory unitization statute.

### III. UNITIZATION

Unitization is "the operation of separately owned tracts of land for oil and gas as if they are one tract under one ownership and with disregard to property lines or interests, except for the apportionment of the costs and proceeds . . . whether the aggregate of the area developed is large or small."<sup>57</sup> In the absence of compulsory unitization statutes, the many owners of a field's mineral interests must unanimously agree to operate as a unit. Despite the advantages that unitization may provide for all parties, unanimous approval of a field-wide unitization plan is rare. Absent statutory au-

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55. Texas has an average of about seven leases per field, whereas Oklahoma has an average of over thirteen. Stuart T. MacDonald, *Land Tenure Patterns and Unitization Legislation: Evidence from Texas and Oklahoma*, 12 SW. BUS. & ECON. J. 1, 5 (2003-04).

56. Lindsey Trachtenberg, Note, *Reconsidering the Use of Forced Pooling for Shale Gas Development*, 19 BUFF. ENVTL. L.J. 179, 200-01 (2012). Pooling has also been suggested as a remedy against drainage caused by hydraulic fracturing that crosses lease lines. See *Costal Oil & Gas Co. v. Garza Energy Trust*, 263 S.W.3d 1 (Tex. 2008).

57. 1 W. L. SUMMERS, *THE LAW OF OIL AND GAS* § 5.49 (3d ed. 2004).

thority, courts have refused to compel unitization, even in the face of tremendous waste. For example, in *Western Gulf Oil Co. v. Superior Oil Co.*,<sup>58</sup> the California Court of Appeals approved the decision of owners of tracts overlying the Paloma Oil Field not to operate the field as a single unit, despite plaintiff's allegations (taken as true) that unitizing would enable the production of an additional \$166 million worth of oil, gas, and condensate.

### A. History of Unitization in Texas

Texas remains the only state in the nation without a compulsory unitization statute, despite the fact that “[s]uch a statute is universally recognized as necessary to assure the maximum efficient recovery of oil and gas while also allocating fair shares of a field’s bounty to the different operators of leases overlying a common reservoir.”<sup>59</sup> Because of the difficulties associated with voluntary unitization, all states producing oil and gas in any serious capacity (Texas excluded) have enacted a compulsory unitization statute.<sup>60</sup> While the majority of states allow for compulsory unitization to prevent waste, improve overall recovery, reduce the number of unnecessary wells, or protect correlative rights, some states have provided for limited compulsory unitization to bolster secondary recovery efforts.<sup>61</sup>

Hostility toward unitizing oil fields has a long history in Texas. In 1931, legislators passed a bill that strengthened the ability of the Commission to combat wasteful practices. But in outlining the scope of the term “waste,” the legislators ensured that the law would not be used to require unitization. The definition of waste, which has survived from 1931 to the present day, includes,

[W]aste or loss incident to or resulting from the unnecessary, inefficient, excessive, or improper use of the reservoir energy, including the gas energy or water drive, in any well or pool; however, it is not the intent of this section or the provisions of this chapter . . . to require repressuring of an oil pool or to require that the separately owned properties in any pool be unitized under one management, control, or ownership.<sup>62</sup>

At the time of this law’s passage, the hostility toward unitization was understandable. Independent producers and legislators wanted to avoid the

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58. 206 P.2d 944 (Cal. App. 1949).

59. Weaver, *supra* note 15, at 187.

60. See, e.g., ALASKA STAT. ANN. § 31.05.110 (West); N.D. CENT. CODE § 38-08-09.1; CAL. PUB. RES. CODE § 3320.2; OKLA. STAT. tit. 52 § 287.4.

61. See, e.g., CAL. PUB. RES. CODE § 3643(c).

62. TEX. NAT. RES. CODE ANN. § 85.046(a)(7).

evils of monopoly threatened by the vertically integrated major oil companies that controlled the vast majority of U.S. pipelines. During testimony leading to the passage of the 1931 statute, the party that spoke most forcefully in favor of unitization of the East Texas field was William Farish, president of Humble Oil (which later became Exxon). Humble, as the largest producer in the area, controller of the pipelines, and owner of the refineries, sought to operate the field, and independent producers were unwilling to relinquish their claims for fear of being excluded by the widely maligned corporate giant.<sup>63</sup>

A second concern that caused legislators to balk at compulsory unitization was the perceived lack of institutional competence of the Railroad Commission. The "mysterious, fugitive nature" of oil resources made it difficult for the Commission to understand oil and gas production and even more difficult to promulgate and enforce regulations.<sup>64</sup> Uncertainty surrounding the physical nature of the oil and gas in a reserve also led to problems related to royalty allocation. There were nearly six hundred small operators on the East Texas field. They were not producing in equal amounts nor were their leases of uniform size. In fact, data from the period show that these independent operators had conjured forty-nine percent of the field's total production from only twenty percent of the acreage of the field. If the field were to be unitized, the Commission would need to determine the "fair shares" of each of the producers. The difficulty in determining fair share would be a daunting task in a political vacuum but was nearly impossible when "no independent would willingly settle for a fair share when he had gained an unfair share from the unregulated commons."<sup>65</sup>

### B. *Empirical Studies*

Professor Weaver argues that despite Texas' lack of a compulsory unitization statute, the Railroad Commission has nevertheless been able to encourage unitization of many Texas oil and gas fields through field orders amounting to "not-so-subtle coercion." By examining data from the late seventies and early eighties, she determined that at least forty-eight percent of Texas' total oil production in that era came from voluntarily unitized fields. By contrast, in Oklahoma, a maximum of thirty-nine percent of its oil production came from unitized fields. It may seem surprising that Texas produces a larger proportion of its oil from unitized areas, particularly

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63. Weaver, *supra* note 15, at 189. Humble, in these days before common carrier legislation, had gained a reputation for using its pipeline power to coerce small operators into selling their leases at discounted prices.

64. See Japhet, *supra* note 16.

65. Weaver, *supra* note 15, at 189.

considering that Oklahoma has had a compulsory unitization statute since 1945.<sup>66</sup>

A more recent study also compared unitization in Texas and Oklahoma.<sup>67</sup> Professor MacDonald found that while less than four percent of Texas fields sampled were officially unitized, over sixty-five percent of the fields sampled were operated by a single producer. If a single operator has the rights to an entire field, that field is unified de facto. By contrast, during the same time frame, MacDonald found that twenty-five percent of Oklahoma's fields were officially unitized but only eighteen percent were operated by a single operator, resulting in a lower de facto proportion of unitization. Further, Professor MacDonald pointed out that pressure-maintenance secondary recovery operations occurred in eighty-five percent of Texas' largest fields, a fact which suggests that such operations can and do occur in the absence of a compulsory unitization statute.

These studies suggest that Texas has had some success in cooperative secondary recovery efforts. However, "the real question is not how much unitization has occurred. . .but how much more is needed."<sup>68</sup> The answer to this question depends on whom you ask. Predictably, major oil producers want unitization, while the independents do not. Texas produced 769,501,187 barrels of crude oil in 2013 and over 814,537,759 barrels of crude oil in 2014.<sup>69</sup> While there is wide variation among fields, on average, unitization agreements increase oil recovery by nearly seventeen million barrels over the life of the field.<sup>70</sup>

### C. *Efforts to Pass a Compulsory Unitization Statute*

Texas' current unitization agreements are not achieved through Commission orders. Instead, the Commission merely authorizes agreements for the "cooperative development"<sup>71</sup> of separately owned properties for secondary recovery efforts, including gas cycling, repressuring, and water flooding.<sup>72</sup> No person may be compelled to join these agreements and those who

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66. WEAVER, UNITIZATION at 316 ("This percentage is a minimum because it does not include production from fields that are completely owned by one landowner and leased to one operator, which therefore can be produced as a unit . . .").

67. MacDonald, *supra* note 55.

68. WEAVER, UNITIZATION at 323.

69. Railroad Commission of Texas, Texas Monthly Oil and Gas Production (2008-2014), *available at* <http://www.rrc.state.tx.us/oil-gas/research-and-statistics/production-data/texas-monthly-oil-gas-production/>.

70. WEAVER, UNITIZATION at 317.

71. TEX. NAT. RES. CODE ANN. § 101 (West).

72. TEX. NAT. RES. CODE ANN. § 101.011 (West).

choose not to join are not bound by the agreement's terms.<sup>73</sup> The Commission will only approve cooperative development agreements if they find, after providing the statutorily required notice and hearings, that such an agreement promotes the public welfare, does not infringe on rights of persons not party to the agreement, that the costs of secondary recovery do not exceed the value of additional oil and gas recovered, and that the agreement does not cover more acreage than reasonably necessary to effectuate the secondary recovery effort.<sup>74</sup> These agreements usually happen late in the life of an oil field, long after production has fallen below peak levels, and still allow for strategic holding out by owners in position to benefit from the secondary recovery efforts of others.<sup>75</sup>

In 2013, Texas State Representative Van Taylor introduced Texas House Bill 100, The Oil and Gas Majority Rights Protection Act (MRPA). This bill would enable the Commission to compel unitization if approved by seventy percent of the working interest holders.<sup>76</sup> Similar bills had been introduced in previous legislative sessions. These bills were brought forth mostly by conservative Republicans.<sup>77</sup> Such proposals have caused heated, even vitriolic debate among producers, interest holders, commentators, and legislators.<sup>78</sup> For example, in 1999, a compulsory unitization bill was introduced in the Texas House that would allow the Commission to order unitization if eighty percent of the property and mineral rights owners agreed. During testimony at the Texas Capital, opponents of the bill characterized it as confiscatory and a threat to private property rights. Professor Weaver testified that the Commission and the courts had already agreed that the prevention of waste takes precedent over private property rights. Representative Joe Crabb replied that her argument that the public interest should supersede private property rights "sounds like something Hitler said."<sup>79</sup>

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73. TEX. NAT. RES. CODE ANN. § 101.012 (West).

74. See TEX. NAT. RES. CODE ANN. § 101.013 *et seq.* (West).

75. See generally Murray & Cross, *supra* note 10, at 1125 (describing an attempted unitization effort).

76. H.B. 100, §§ 104.001, 104.056, 83rd Leg. (Tex. 2013).

77. *E.g.*, H.B. 1624, 76th Leg. (Tex. 1999).

78. See Associated Press, *Oilmen Claim Divisive Action*, THE VICTORIA ADVOCATE, Oct. 17, 1974, available at <https://news.google.com/newspapers?id=6gpaAAAAIbAJ&sjid=bEsNAAAAlbAJ&pg=5214%2C2915049>; see also Charles Sartain, *Compulsory Unitization Undermines Texas Values*, ENERGY AND THE LAW (March 12, 2013), available at <http://www.energyandthelaw.com/2013/03/12/compulsor-unitization-undermines-texas-values-rhetorically-speaking/>.

79. Philip Parker, *Oil Families Tell House Panel Unitization Bill Is Unnecessary*, LUBBOCK AVALANCHE-JOURNAL, March 31, 1999, [http://lubbockonline.com/stories/033199/bus\\_033199011.shtml](http://lubbockonline.com/stories/033199/bus_033199011.shtml). On his 1999 election finance filing report, Crabb disclosed that he and his wife owned 5,100-13,998 shares of Exxon Mobil, then valued at \$188,343-\$516,946 (author's calculations). Crabb continued to represent Texas House District 127 until his retirement in 2010. See Joe F. Crabb, *Personal Financial Statement*, THE TEXAS TRIBUNE RECORDS

Proponents of the most recent legislation argue that compulsory unitization increases efficiency and conservation; fewer wells with better management should be utilized to prevent waste by permitting recovery of a greater percentage of the oil and gas in the field. Of course, this result would lead to greater overall royalties. As a related matter, unitization protects surface owners and reduces environmental impact. Fewer wells mean fewer of the physical impacts that are concurrent with well development: surface facilities, trucks, lights, noise, etc. Fewer wells managed by a single, large unit operator are also more likely to be carefully maintained, resulting in fewer accidents and spills. Finally, proponents argue that unitization creates jobs.

Opponents of compulsory unitization legislation characterize such laws as infringing on individual property rights and argue that compulsory unitization threatens their liberty. Unitization eliminates their freedom to contract with producers and the MRPA would also authorize the Commission to amend or abrogate surface use protections that conflict with unit operations. From a financial perspective, small operations may suffer under risk penalties, which allow for a lien on "proceeds of production due to any working interest owner who is not paying the owner's share of the costs of unit operation as compensation to the paying owner or owners."<sup>80</sup> Small operators argue that they will not be able to pay their proportion of upfront costs for multimillion dollar carbon dioxide advanced recovery projects, subjecting them to a possible penalty of up to three hundred percent of the cost and eliminating current income from their small producing wells.<sup>81</sup>

According to the modern debate, whether compulsory unitization is a good idea depends on whether one thinks private property rights should be limited to maximize public welfare. Texas legislators seem to have made up their minds: Representative Taylor's bill never left committee review. But they should reconsider their opposition to a compulsory unitization statute. The debate over the proposed law has focused primarily on the competition between private property and the benefits of increased recovery. Legislators have conspicuously neglected to discuss the negative externalities imposed on the State caused by inefficient practices. When the costs of abandoned wells and contaminated site remediation are considered, the scales tip firmly in favor of passing a compulsory unitization statute designed to increase recovery and minimize the number of wells used to effectuate recovery.

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(Feb. 14, 2000), <http://records.texastribune.org/personal-finance/joe-crabb-1999-financials-00020049-135859.pdf>.

80. *Supra*, note 71, at § 104.108.

81. *Id.*

#### IV. THE COSTS OF COMBATTING THE ENVIRONMENTAL CONSEQUENCES OF OVER-DRILLING

The unfortunate (yet predictable) result of the refusal to pass a compulsory unitization statute is that Texas leads the nation in the number of marginally producing, idle, and orphan wells.<sup>82</sup> In order for inactive wells to stay compliant with state regulations, the operators must provide financial assurance and qualify for a plugging extension. The Commission will declare a well orphaned if the operator fails to keep up with required paperwork. As of August 2013, the Commission recognized 8644 wells as orphans.<sup>83</sup> These abandoned wells, when not properly plugged, pose environmental threats because they create a physical nexus between deep hydrocarbon reserves, super-salty brines, and shallow underground freshwater aquifers. To combat the potential harms threatened by such a large number of abandoned wells, the Texas legislature has designed two programs to reduce the number of orphans.

The first program, the Oil Field Cleanup Fund (OFCF), created a thirty-million-dollar fund for use by the Commission “for any purpose related to the regulation of oil and gas development, including . . . oil and gas well plugging.”<sup>84</sup> Under the OFCF, the Commission uses fund money to cap eligible orphaned wells. After the orphan well is capped, the Office of the Attorney General may bring suit against the responsible operator to recover costs of capping, as well as civil penalties. The Commission prioritizes which wells to cap by examining several factors, including the stage of well completion, wellbore condition, proximity to environmentally sensitive areas, and other unique environmental, safety, or economic concerns.<sup>85</sup> The money in the OFCF comes from several sources including production taxes, hazardous waste generation fees, and enforcement penalties paid by oil and gas companies. The Commission is required to issue an annual progress report detailing the program’s activities and finances.<sup>86</sup> Since 1992, the OFCF has been used to plug 29,782 orphaned wells at a total cost of over \$209 million.<sup>87</sup>

The second program designed to combat the number of abandoned wells is the Orphan Well Reduction Program (OWRP), which is designed

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82. Weaver, *supra* note 15, at 190. Of course, it might be predicted that Texas would have the most orphaned wells simply because Texas has the most wells period.

83. R.R. COMM’N OF TEXAS, OIL AND GAS REGULATION AND CLEANUP PROGRAM ANNUAL REPORT – FY 2013, available at <http://www.rrc.state.tx.us/environmental/ofcfund/expenditures/OFCU2013.pdf> (hereinafter OFCF Report 2013).

84. TEX. NAT. RES. CODE ANN. § 81.067-69 (West).

85. OFCF REPORT 2013, *supra* note 83, at 16.

86. TEX. NAT. RES. CODE ANN. § 81.069 (West).

87. OFCF REPORT 2013, *supra* note 83, at 1.

to encourage “operators in good standing” to assume operation and regulatory responsibility for orphaned wells. After identifying an orphaned well and filing notice with the Commission, an operator may conduct a limited visual inspection of the well and elect to petition to be designated as the well’s operator after proving a possessory interest in the mineral estate (e.g., by executing a lease with the mineral rights owner). To encourage participation in this program, during the first two years of its existence, the Commission waived certain taxes and fees and reimbursed the operator “50 cents for each foot of well depth if . . . the person [brought] the well back into continuous active operation or [plugged] the well.”<sup>88</sup> Under this two-year program, the Commission paid \$107,000 to operators who plugged thirteen wells and returned forty-one wells to active production.<sup>89</sup>

Both the OFCF and OWRP programs have largely been recognized as successful and have plugged virtually all orphaned wells categorized as highest priority. Though there are currently over 8000 orphan wells remaining, this is a substantial reduction in the number of orphan wells that would exist in the absence of such a program.<sup>90</sup>

In addition to reducing the number of orphan wells, the Commission engages in contaminated site remediation. In 2013, it conducted 280 cleanup activities, including twenty-seven emergency operations, at a total cost of \$7,596,106.<sup>91</sup> The Commission has also established programs to encourage private parties to incur their own expenses in remediating contaminated sites. For parties that *did not contribute* to the contamination of the site, the Voluntary Cleanup Program (VCP) seeks to “provide an incentive to remediate property by removing the liability to the state of lenders, developers, owners, and operators who did not cause or contribute to contamination.”<sup>92</sup> As part of the VCP, a non-contributing person may remediate a site (with Commission oversight), and upon completion, will be absolved of “all liability to the State for cleanup costs” not caused by that person.<sup>93</sup> This program “expedites the return of contaminated properties into productive use,” and has resulted in the cleanup of sixty-five sites since 1992.<sup>94</sup>

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88. TEX. NAT. RES. CODE ANN. §§ 89.047-48 (West).

89. Clint Shields, *Wells They Leave Behind*, FISCAL NOTES (Aug. 2010) at 4, 5, <http://www.window.state.tx.us/comptrol/fnotes/pdf/fn1008.pdf>.

90. *Id.* at 5. The Commission recognized 16,770 orphan wells in 2003. Interestingly, while the vast majority of orphaned wells are inland wells, the Commission lists 70 offshore wells as orphans.

91. OFCF REPORT 2013 *supra* note 83, at 12, 14.

92. TEX. NAT. RES. CODE ANN. § 91.652 (West).

93. TEX. NAT. RES. CODE ANN. § 91.660 (West).

94. OFCF REPORT 2013, *supra* note 83, at 21.

A second program, the Operator Cleanup Program (OCP), allows owners and operators who *did contribute* to the contamination of a site to conduct their own site cleanups. These actions, usually in environmentally sensitive areas, are completely operator funded but overseen by the Commission. OCP allows owners and operators to avoid the additional liability that would be imposed on them by the Attorney General if the Commission used money from the OFCF to remediate the site. At the same time, OCP allows the Commission to ensure that the site is remediated to specific standards. Commission oversight of remediation efforts includes frequent sampling, reporting, and evaluation “to ensure final cleanup is protective of the public health, safety and the environment.” As of August 2013, there were close to six hundred OCP cleanups conducted under Commission oversight.<sup>95</sup>

While neither the VCP nor the OCP require the direct expenditure of cleanup funds from the OFCF, the administration costs involved in overseeing these programs are substantial and require “considerable staff resources of employees who are paid out of the fund.”<sup>96</sup> The Commission did not provide detailed financial information for administrative expenses allocated by program but reported that over twenty-four million dollars was spent in administrative costs for fiscal year 2013.<sup>97</sup> All costs considered, the amount that Texas has spent on plugging orphan wells and remediating sites exceeds a quarter-billion dollars. This number is staggering and provides yet another example of how drilling of unnecessary wells leads to inefficiency.

## CONCLUSION

These costs—financial, environmental, and administrative—combined with the millions of barrels of oil foregone due to the lack of enhanced recovery efforts that would result from compulsory unitization, highlight the need for Texas to modernize its laws to ease the burden on its courts and agencies. In *Normanna*, the Texas Supreme Court recognized that current policies were close to sending the state over an economic precipice and boldly acted to create new policy despite Texas’ traditional disdain for judicial activism. Following the court’s lead, the Commission implemented policies that limited and penalized selfish behavior. In the years following the passage of MIPA, the Commission ordered the pooling of hundreds of tracts that would have otherwise led to the drilling of unnecessary wells. It

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95. *Id.* at 22.

96. *Id.*

97. *Id.* at 14. This was over twice the amount originally budgeted for administrative costs, and approaches the total expenditures for well-plugging operations.

is doubtless that the mere *threat* of compulsory pooling facilitated thousands more voluntary pooling agreements, all with the same effect of eliminating unnecessary wells.

The economic consequences of the absence of a compulsory unitization statute are less dire, or at least less obvious. The Commission, having learned from its experience in creating policies that promote voluntary pooling, has been able to promote voluntary unitization with a surprisingly high success rate. Unfortunately, this has given some politicians the impression that Texas has no need for a compulsory unitization statute. After all, if it ain't broke, don't fix it. But it is broke, or at least the regulatory system does not work as well as it could. A compulsory unitization statute that requires a high percentage of operating and royalty interest owners to approve an agreement before it takes field-wide effect would give ample protection to private property rights. If an owner does not like the unitization agreement, he only needs to convince twenty or thirty percent of the other interest holders (minus whatever percentage the non-consenting owner holds) that they should not agree to unitize. What a compulsory unitization statute fails to protect is an individual owner's ability to hold out on a unitization agreement in order to take advantage of the secondary recovery operations of his neighbors. The neighbors will then be hesitant to unitize in the presence of a holdout for fear of getting a bad deal. The hold-out that is protected in the absence of a compulsory unitization statute may prevent some fields from ever becoming unitized, and may delay the process for those that do eventually become unitized, resulting in more wells, more pollution, and more costs for Texans to bear. The failure to pass a compulsory unitization statute is bad for oil recovery, bad for the environment, and bad for Texas.

