# What Every Landman Should

# Know About The Railroad Commission Of Texas

## TEXAS LAND INSTITUTE

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## About the Speaker

**Jack Wilhelm is an oil and gas lawyer located in Austin, Texas. Mr. Wilhelm began his career as a staff attorney for Amoco Production Company in New Orleans. Following eight years in New Orleans, Mr. Wilhelm was transferred to Amoco's corporate office in Chicago, where his practice focused on natural gas sales and regulation, and where he served as general counsel of Amoco Oil Pipeline Company, then one of the largest oil pipeline systems in North America. Following his career with Amoco, Mr. Wilhelm became Associate General Counsel of United Gas Pipe Line Company in Houston, Texas. In his position as General Counsel, Mr. Wilhelm oversaw United's state and federal regulatory activities and negotiated the sale of United Gas to Koch Industries (a multi-billion dollar transaction). In 1993, Mr. Wilhelm joined Mobil Oil Corporation as its general counsel in Midland, Texas. In 1996, he opened Mobil's State Public Affairs Office and, after the merger of Exxon and Mobil, in 1999, managed the combined ExxonMobil government affairs office in Austin. In 2001, Mr. Wilhelm accepted an appointment from Texas Comptroller Carole Keeton Strayhorn to become a State Tax Judge. In 2002, he joined the McCall & Ritchie law firm and a year later opened his own offices in downtown Austin.**

**Mr. Wilhelm holds a law degree from the University of Arkansas and a Masters in Energy and Environmental Law from Tulane University; he is licensed to practice in Texas, Louisiana, Illinois, and Arkansas; he maintains a civil law practice that focuses in oil and gas law, environmental law, and state tax laws.**

**In addition to practicing law, Mr. Wilhelm serves as the Parliamentarian of the Travis County Republican Party, a director of the Lost Creek Municipal Utility District, and a member of the Interstate Oil and Gas Compact Commission. He is a frequent speaker on a variety of legal issues, and a complete listing of these speeches and publications can be obtained on-line at www.wilhelmlaw.net.**

## What Every Landman Should Know About The Railroad Commission Of Texas

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# What Every Landman Should Know About The Railroad Commission Of Texas[1]

The Railroad Commission of Texas was established in 1891 under a constitutional and legislative mandate to prevent discrimination in railroad charges and establish reasonable tariffs. It is the oldest regulatory agency in the state and one of the oldest of its kind in the nation. A pioneer in rail regulation, the Railroad Commission has four regulatory divisions that oversee the following:

1. Texas oil and gas industry,
2. gas utilities, pipeline and rail safety,
3. safety in the liquefied petroleum gas industry, and
4. the surface mining of coal and uranium.[2]

There are two other agencies in Texas with which the Texas oil and gas landman will have regular dealings: The Texas General Land Office and the Texas Comptroller. The Texas General Land Office administers the leasing of state owned lands for oil and gas exploration. The Texas Comptroller is the state's treasurer, administering and collecting severance taxes[3] and sales and use taxes, among other things.

This paper will focus on the ***Oil & Gas Division,*** the division that oversees the Texas oil and gas industry.

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[2] Railroad Commission Homepage, www.rrc.state.tx.us. The Railroad Commission's Mission Statement is as follows:

**MISSION STATEMENT**

**We serve Texas by:**

§ Our stewardship of natural resources and the environment
§ Our concern for personal and community safety
§ Our support of enhanced development and economic vitality for the benefit of Texans

[3] 7.5% on gas; 4.6% on oil.

## Summary

## Ten Things the Railroad Commission Does that You Need to Know

**10 things the Railroad Commission does:**

**Drilling and Production**

1. Spacing and density of drilling are regulated, including horizontal drainholes, affecting the placement and number of wells on a tract;
2. Production is regulated to prevent waste, protect correlative rights, and must be lawful to gain the protection of non-liability for capture;
3. Waterflooding and waterflood units may be approved, insulating the operator from liability for trespass and confiscation;
4. Location exceptions for oil and gas wells (referred to as Rule 37 Applications);

**Gathering and Pipelines**

5. The regulation of intrastate crude oil and gas pipelines as common carriers and common purchasers;
6. Classification of a pipeline as a utility or common carrier vests it, among other things, with the power of eminent domain;

**Environmental and Safety Regulation**

7. The Commission regulates the environmental and safety aspects of oil and gas production, including well plugging. The RRC regulations are broad and flexible;
8. Regulation of the disposal of oil-field waste, including the permitting of commercial landfarm operations and disposal wells;
9. Regulation of the injection of Carbon Dioxide into producing reservoirs; and

**Information**

10. The Commission maintains some important information, such as well logs, field and pipeline maps, and production reporting numbers.

## Statutory Authority

The Legislature has delegated the following authority to the Railroad Commission:

> § 81.051. JURISDICTION OF COMMISSION. (a) The commission has jurisdiction over all:
> (1) common carrier pipelines defined in Section 111.002 of this code in Texas;
> (2) oil and gas wells in Texas;
> (3) persons owning or operating pipelines in Texas; and
> (4) persons owning or engaged in drilling or operating oil or gas wells in Texas.
>
> (b) Persons listed in Subsection (a) of this section and their pipelines and oil and gas wells are subject to the jurisdiction conferred by law on the commission.[4]

***Presentation focuses on Spacing/Density, Production Rates, Field Designations, Units, and Spacing/Density Exceptions***

## I. Spacing and Density Regulation – Rules 37, 38, and 11.

Rule 37 was first adopted in 1919.[5] The rule establishes minimum well spacing requirements for fields without special field rules. Many, if not most, fields have their own special field rules, so always be sure to check for those specific, special field rules.

Absent special field rules, the statewide spacing rules are as follows:

1. No well may be drilled closer than 467 feet to the nearest property, lease, or subdivision line, and
2. No well may be drilled closer than 1200 feet to the nearest well on the same tract which is completed in or drilling to the same reservoir.

Rule 38[6] establishes the minimum number of acres that must be assigned to each well in order to obtain a drilling permit for fields without special field rules. Again, many, if not most, fields have their own special field rules, so always be sure to check for those specific, special field rules.

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[4] The statutes governing the Railroad Commission can be found beginning at Title 3 of the Texas Natural Resources Code, Section 81.001 et seq. The Commission's Oil and Gas Division rules and regulations appear at Title 16 Texas Administrative Code, Part 1, Chapter 3, Section 3.1 et seq. Additionally, these rules can be found on the Commission's web-page: www.rrc.state.tx.us.

[5] 16 Tex. Admin. Code § 3.37. See Appendix D for a complete copy of Rule 37.

[6] 16 Tex. Admin. Code § 3.38. See Appendix D for a complete copy of Rule 38.

Absent special field rules, the statewide density rule is as follows:

1. The minimum requirement is 40 acres per well.

*Tolerance Acreage:* Rule 38(c) allows the drilling of an additional well if the remaining (tolerance) acreage is greater than or equal to half the standard proration unit size.

An exception to Rule 37 exists if the applicant will suffer a net uncompensated drainage from his tract. However, it is easy to run afoul of *The Voluntary Subdivision Rule*. The rule provides that a voluntary subdivision made after the attachment of Rule 37 will not be considered for purposes of determining whether an application to drill must be granted in order to prevent confiscation.

Rule 11[7] requires that "all wells shall be drilled as nearly as vertical as possible by normal, prudent, practical drilling operations." The Rule specifically addresses two classes of wells (1) wells that are intentionally deviated, and (2) wells that are not intentionally deviated but where the cumulative displacement is such that the well bore could have crossed the lease or property line.

An open issue is the Commission's interest in regulating a well drilled from a Rule 37 legal surface location but that is bottom-holed nearer than the otherwise allowable legal location (e.g., deviation, intentional or not).

## II. Production Rates.

It is well established that the Railroad Commission, like its counterparts in other states, has the constitutional authority to regulate the production of oil and natural gas. That authority was restated by the United States Supreme Court as recently as 1989. *Northwest Cent. Pipeline v. Kan. Corp. Comm'n,* 489 U.S. 493 (1989). The Commission's rules concerning pro-ration and allowables are set forth in Rules 31, 42, and 45.

Because overall Texas production rates no longer have a direct impact on the worldwide price of oil, production rates are not as controversial as in the distant past. Most disputes center on correlative production rights of competing operators within a field.

## III. Fields and Field Rules

Field rules establish the parameters for the development and operation of a field. These rules typically cover the following:

a. Well Spacing;
b. Well Density;

[7] 16 Tex. Admin. Code § 3.11. See Appendix D for a complete copy of Rule 11.

c. Production allowable allocation formula for the field; and
d. Surface casing requirements.

Since field rules are on a reservoir basis, and multiple reservoirs may be covered by a given lease, careful analysis should be given to the interaction between field rules and a lease.

Field is synonymous with "common reservoir." A common reservoir consists of a common accumulation of hydrocarbons …." *Railroad Commission v. Graford Oil Corp.,* 557 S.W.2d 946 (Tex. 1977).[8]

## IV. Pooling and Unitization

Unlike Louisiana, the vast number of units are voluntary pooled units, which will be discussed in greater detail below.

In Texas, there are five (5) types of units:

1. Drilling Unit: The acreage area shown on the Form W-1 application for the permit to drill. It is the area shown to establish that the applicant has sufficient unassigned acreage to satisfy the density requirement. The designation of a drilling unit has not title significance;
2. Proration Unit: The acreage designated on a Form P-15 and the attached plat to show the acreage assigned to the well for proration purposes where field rules provide for the setting of allowables on an acreage basis, in whole or in part. The proration unit is designated after the well is drilled and completed, and only productive acreage can be assigned to a proration unit. The designation of a proration unit can be changed at any time. A proration unit has not title significance.
3. Voluntary Pooled Unit: The most common unit in Texas, is a unit formed by the voluntary joinder of separate ownership interests. A voluntary pooled unit is created by one of three mechanisms:
   - The community lease;
   - Pooling under a lease pooling clause;
   - Pooling by agreement of the interest owners in the property to be pooled. Any amount of acreage can be pooled by such agreement.
4. Pooling and Cooperative Agreements:[9] These are Commission approved units necessary to effect secondary recovery operations for oil or gas including recycling, repressuring, water flooding, and gas repressurizing. These pooled units do not bind a landowner, royalty owner, lessor, lessee, overriding royalty owner, or any other person who does not execute the cooperative agreement. The purpose of these units is largely to protect the operator from claims for violating correlative rights and anti-trust claims (most often called a fieldwide unit). Normally the RRC requires that at least 65% of the royalty interest and

[8] For purposes of the common purchaser laws, a field may be defined as a geographic area.
[9] TEX. NAT. RES. CODE §101.001 et seq.

85% of the working interest commit to the unit agreement before a hearing on approval will be granted.

Importantly, subsurface movement of hydrocarbons and water pursuant to a Commission approved secondary recovery operation does NOT result in a trespass. Thus, Commission approval is an important protection for the Operator from lawsuits by arguably adversely affected nearby landowners. *Railroad Commission v. Manziel,* 361 S.W.2d 560 (Tex. 1962).

5. Forced Pooling under the Mineral Interest Pooling Act (MIPA). Under limited circumstances, the Railroad Commission may force pool certain tracts under limited circumstances. The circumstances are as follows:
   - The field must have been discovered after March 8, 1961;
   - No wildcats;
   - There must be special field rules;
   - The must be two or more separately owned tracts. It cannot be used merely to pool separate interests in the same tract;
   - One of the interest owners with the right to drill must have drilled or proposed to drill a well on the existing or proposed proration unit;
   - Units are limited to 160 acres for oil; 640 acres for gas, plus a 10% tolerance;
   - Cannot force pool State owned lands;
   - The pooling must result in the avoidance of the drilling of unnecessary wells, the protection of correlative rights, or the prevention of waste;
   - As a prerequisite, there must have been a fair and reasonable offer to pool. The Commission determines whether the offer was fair and reasonable. *Railroad Commission v. Pend Oreille Oil & Gas Co., Inc.,* 817 S.W.2d 36 (Tex. 1991).

## V. Well Bonding (Plugging or Performance Bonds)

Plugging bonds are relatively new to Texas. Texas now requires bonds in the following amounts:

a. For 10 or fewer wells, $25,000;
b. For 11 to 100 wells, $50,000; and
c. For over 100, $100,000.[10]

Not surprisingly, there are additional bonding requirements pertaining to offshore wells. Furthermore, operators can elect to post letters of credit of cash deposits in lieu of performance bonds.[11]

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[10] 16 Tex. Admin. Code § 3.78.

[11] HB 380 by West (79th Leg. Sess., 2005) authorizes the Railroad Commission to also accept a pre-paid well-specific plugging insurance policy (in lieu of bond, letter of credit, or cash deposit).

## VI. Horizontal Drainholes

This technology has presented challenges to the Railroad Commission in administering spacing rules and the assignment of allowables. That said, the Commission has had guidelines for horizontal drilling since 1987.

Statewide Rule 86 (16 TAC § 3.86) governs the drilling of horizontal drainhole wells. Rule 86 requires the following:

- All portions of the horizontal drainhole must comply with the applicable lease-line and between well spacing requirements for the field. Otherwise, a Rule 37 exception application is required;
- Operators may obtain an acreage bonus (and, usually an allowable bonus), roughly keyed to the length of the horizontal drainhole;[12] and
- The Operator must conduct a directional survey on every horizontal drainhole well; and
- Optional special field rules for horizontal drilling in individual fields.

And yes, the surface location of the horizontal drainhole may be outside the geographic boundaries of the unit.

## VII. Emerging Issues

***Authority of a City to Assess Pipeline Fees and Recover Damages***

For a number of years, a number of cities on the Gulf Coast have imposed and attempted to impose fees on pipelines that traverse public roads. Fearing this authority would be abused if left unregulated, the Legislature imposed some limitations in the last session.[13]

Now, by statute, a municipality may impose the following charges (but no more):

- Assess a reasonable annual charge, not to exceed the cost of the city of administering, supervising, inspecting, and otherwise regulating the location of the pipeline facility, including maintaining records and maps of the location of the pipeline facility); and
- Recover the reasonable cost of repairing damage to a public road that is caused by the placement, construction, maintenance, repair, replacement, operation, or use of a pipeline.

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[12] For fields with a density requirement of 40 acres or less, the operator may assign an additional 20 acres to the proration unit; for fields with a density requirement greater than 40 acres, the general rule is that for every 827 feet of horizontal drainhole, the operator may assign an additional 40 acres to the proration unit.

[13] HB 951 by West (79$^{th}$ Leg. Sess., 2005).

### *Increased Regulation of Natural Gas Gathering Systems*[14]

At least one industry trade association[15] has expressed a concern that gas gathering systems are taking advantage of natural gas producers. The Alliance argues that pipelines that have a monopoly have taken advantage of their overwhelming market power and forced producers to accept contracts that are undesirable. Producers are told to "take it, or leave it" and shut in their wells.

In response, legislation was introduced in the last legislative session that would have required a gas utility (e.g., gas pipeline or gathering system) to transport gas for fair and reasonable fees.[16] The gas utility would have been required to post a tariff that is available for public inspection[17] that includes geographical identity of receipt and delivery points, the identity of the shipper, and the nature of type of service. If the gas utility elected not to post a tariff, the pipeline would have had to transport gas at the lowest rate charged by the utility to any person. If the producer disagreed with the tariff, he could file a complaint with the RRC, which would then establish a just and reasonable rate.

There were a series of compromise legislative proposals and, ultimately, nothing passed. However, you can expect this issue, the severity of regulation of gas gathers and transporters, to be before the public, and our industry, for several years to come.

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[14] This is not a new issue. See for instance, Jack M. Wilhelm, States Considering the Regulation of Natural Gas Gathering Systems, Nat. Gas Mag. (Apr. 1996).
[15] The Texas Alliance.
[16] HB 821 by Keffer (79th Leg. Sess., 2005).
[17] Currently, tariffs are not available for public inspection.

## Appendices

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## Appendix A

**Railroad Commissioners are elected to six-year terms with one Commissioner seeking election every two years. When a Commissioner is appointed by the Governor to fill an unexpired term, the appointee serves until the next General Election at which time the appointee may run for the remainder of the unexpired term.**

Chairman **Victor Carrillo** joined the Texas Railroad Commission in February 2003 when Governor Rick Perry appointed him to fill the unexpired term of Tony Garza who became U.S. Ambassador to Mexico. He is also Chairman of the newly created Texas Energy Planning Council whose mission is to create a comprehensive energy plan for the State of Texas.

A native Texan, Commissioner **Elizabeth Ames Jones** is the newest member of the Commission, having been appointed earlier this year upon the resignation of Commissioner Charles Matthews. Prior to her appointment, Commissioner Jones served as a State Representative out of the San Antonio area. Her family has been in the oil and gas business for several generations. She is a graduate of the University of Texas.

**Michael L. Williams** was initially appointed to the Texas Railroad Commission by former Governor George W. Bush in December 1998 to serve the unexpired term of Carole Keeton Rylander. Williams was elected by his fellow commissioners in September 1999 to chair the Commission. In November 2000, the people of Texas elected him to complete the term expiring in the year 2002, and in November 2002, they reaffirmed their support by electing him to a term expiring in 2008. He is the first African American in Texas history to hold a statewide executive post and is the highest ranking African American in Texas state government.

## Appendix B

## OIL AND GAS DIVISION DISTRICT OFFICES

| DIST | DIRECTOR | PHONE# | FAX# | ADDRESS | CITY, ZIP |
|---|---|---|---|---|---|
| **01 & 02** | Tom Melville | 210-227-1313 | 210-227-4822 | 115 E Travis St Ste 1610 | San Antonio 78205-1689 |
| **03** | Guy Grossman | 713-869-5001 | 713-869-9621 | 1706 Seamist Dr Ste 501 | Houston 77008-3135 |
| **04** | Fermin Munoz, Jr. | 361-242-3113 | 361-242-9613 | P O Box 10307 | Corpus Christi 78460-0307 |
| **05 & 06** | Randy Earley | 903-984-3026 | 903-983-3413 | 619 Henderson Blvd | Kilgore 75662-5998 |
| **7B** | Joe Cress | 325-677-3545 | 325-677-7122 | 3444 N. First St., Ste. 600 | Abilene 79603 |
| **7C** | Don Horner | 325-657-7450 | 325-657-7455 | 622 S. Oakes St., Ste. J | San Angelo 76903 |
| **08 & 8A** | Mark Henkhaus | 432-684-5581 | 432-684-6005 | Conoco Towers 10 Desta Dr. Suite 500E | Midland 79705 |
| **09** | Walter Gwyn | 940-723-2153 | 940-723-5088 | 901 Indiana Ave, Ste 600 | Wichita Falls 76301-6798 |
| **10** | Lindsay Patterson | 806-665-1653 | 806-665-4217 | P O Box 941 | Pampa 79066-0941 |

## OIL AND GAS DIVISION AUSTIN OFFICE

**1701 North Congress Avenue**
**Austin , Texas 78701**

**P.O. Box 12967**
**Austin , Texas 78711-2967**

**(512) 463-7288**
**(TDD) (800) 735-2989**

| TITLE | NAME | PHONE# | FAX# |
|---|---|---|---|
| Director | Richard A. Varela | (512) 463-6810 | (512) 463-6780 |
| Deputy Director | Tommie Seitz | (512) 463-6810 | (512) 463-6780 |
| General Counsel | Lindil Fowler | (512) 463-6848 | (512) 463-6684 |

| | | | |
|---|---|---|---|
| Assistant Director<br>Environmental Services | Steve Seni | (512) 475-4439 | (512) 463-6780 |
| Assistant Director<br>Permitting/Product.Services | Deborah LaHood | (512) 463-6838 | (512) 463-6955 |
| Assistant Director<br>Site Remediation | John Tintera | (512) 463-6765 | 512) 463-2388 |
| Deputy Director<br>Field Operations | Charles C. Ross | (512) 463-6830 | (512) 463-7328 |
| Publication/Oil and Gas Forms | | (512) 463-7255 | |
| 24 Hour Emergency | | (512) 463-6788 | |

## Appendix C
## Select Texas Statutes

### NATURAL RESOURCES CODE
### SUBCHAPTER J. PAYMENT FOR PROCEEDS OF SALE
### (Royalty Payment Obligations: $100 minimum, division orders, etc.)

§ 91.401. DEFINITIONS. In this subchapter:

(1) "Payee" means any person or persons legally entitled to payment from the proceeds derived from the sale of oil or gas from an oil or gas well located in this state.

(2) "Payor" means the party who undertakes to distribute oil and gas proceeds to the payee, whether as the purchaser of the production of oil or gas generating such proceeds or as operator of the well from which such production was obtained or as lessee under the lease on which royalty is due. The payor is the first purchaser of such production of oil or gas from an oil or gas well, unless the owner of the right to produce under an oil or gas lease or pooling order and the first purchaser have entered into arrangements providing that the proceeds derived from the sale of oil or gas are to be paid by the first purchaser to the owner of the right to produce who is thereby deemed to be the payor having the responsibility of paying those proceeds received from the first purchaser to the payee.

(3) "Division order" means an agreement signed by the payee directing the distribution of proceeds from the sale of oil, gas, casinghead gas, or other related hydrocarbons. The order directs and authorizes the payor to make payment for the products taken in accordance with the division order. When used herein "division order" shall also include "transfer order".

(4) "Transfer order" means an agreement signed by a payee and his transferee (new payee) directing the payor under the division order to pay another person a share in the oil or gas produced

§ 91.402. TIME FOR PAYMENT OF PROCEEDS. (a) The proceeds derived from the sale of oil or gas production from an oil or gas well located in this state must be paid to each payee by payor on or before 120 days after the end of the month of first sale of production from the well. After that time, payments must be made to each payee on a timely basis according to the frequency of payment specified in a lease or other written agreement between payee and payor. If the lease or other agreement does not specify the time for payment, subsequent proceeds must be paid no later than:

(1) 60 days after the end of the calendar month in which subsequent oil production is sold; or

(2) 90 days after the end of the calendar month in which subsequent gas production is sold.

(b) Payments may be withheld without interest beyond the time limits set out in Subsection (a) of this section when there is:

(1) a dispute concerning title that would affect distribution of payments;

(2) a reasonable doubt that the payee:

(A) has sold or authorized the sale of its share of the oil or gas to the purchaser of such production; or

(B) has clear title to the interest in the proceeds of production;

(3) a requirement in a title opinion that places in issue the title, identity, or whereabouts of the payee and that has not been satisfied by the payee after a reasonable request for curative information has been made by the payor.

(c) (1) As a condition for the payment of proceeds from the sale of oil and gas production to payee, a payor shall be entitled to receive a signed division order from payee containing only the following provisions:

(A) the effective date of the division order, transfer order, or other instrument;

(B) a description of the property from which the oil or gas is being produced and the type of production;

(C) the fractional and/or decimal interest in production claimed by payee, the type of interest, the certification of title to the share of production claimed, and, unless otherwise agreed to by the parties, an agreement to notify payor at least one month in advance of the effective date of any change in the interest in production owned by payee and an agreement to indemnify the payor and reimburse the payor for payments made if the payee does not have merchantable title to the production sold;

(D) the authorization to suspend payment to payee for production until the resolution of any title dispute or adverse claim asserted regarding the interest in production claimed by payee;

(E) the name, address, and taxpayer identification number of payee;

(F) provisions for the valuation and timing of settlements of oil and gas production to the payee; and

(G) a notification to the payee that other statutory rights may be available to a payee with regard to payments.

(2) Such a division order does not amend any lease or operating agreement between the interest owner and the lessee or operator or any other contracts for the purchase of oil or gas.

(d) In the alternative, the provisions of Subsection (c) of this section may be satisfied by a division order for oil payments in substantially the following form and content:

**DIVISION ORDER**

TO:
(Payor) Property No.

Effective (Date)

The undersigned severally and not jointly certifies it is the legal owner of the interest set out below of all the oil and related liquid hydrocarbons produced from the property described below:

OPERATOR:

Property name:

County:
State:

Legal Description:

OWNER NO.
TAX I.D./SOC. SEC. NO. PAYEE

DIVISION OF INTEREST

THIS AGREEMENT DOES NOT AMEND ANY LEASE OR OPERATING AGREEMENT BETWEEN THE INTEREST OWNERS AND THE LESSEE OR OPERATOR OR ANY OTHER CONTRACTS FOR THE PURCHASE OF OIL OR GAS.

The following provisions apply to each interest owner ("owner") who executes this agreement:

TERMS OF SALE: The undersigned will be paid in accordance with the division of interests set out above. The payor shall pay all parties at the price agreed to by the operator for oil to be sold pursuant to this division order. Purchaser shall compute quantity and make corrections for gravity and temperature and make deductions for impurities.

PAYMENT: From the effective date, payment is to be made monthly by payor's check, based on this division of interest, for oil run during the preceding calendar month from the property listed above, less taxes required by law to be deducted and remitted by payor as purchaser. Payments of less than $100 may be accrued before disbursement until the total amount equals $100 or more, or until 12 months' proceeds accumulate, whichever occurs first. However, the payor may hold accumulated proceeds of less than $10 until production ceases or the payor's responsibility for making payment for production ceases, whichever occurs first. Payee agrees to refund to payor any amounts attributable to an interest or part of an interest that payee does not own.

INDEMNITY: The owner agrees to indemnify and hold payor harmless from all liability resulting from payments made to the owner in accordance with such division of interest, including but not limited to attorney fees or judgments in connection with any suit that affects the owner's interest to which payor is made a party.

DISPUTE; WITHHOLDING OF FUNDS: If a suit is filed that affects the interest of the owner, written notice shall be given to payor by the owner together with a copy of the complaint or petition filed.

In the event of a claim or dispute that affects title to the division of interest credited herein, payor is authorized to withhold payments accruing to such interest, without interest unless otherwise required by applicable statute, until the claim or dispute is settled.

TERMINATION: Termination of this agreement is effective on the first day of the month that begins after the 30th day after the date written notice of termination is received by either party.

NOTICES: The owner agrees to notify payor in writing of any change in the division of interest, including changes of interest contingent on payment of money or expiration of time.

No change of interest is binding on payor until the recorded copy of the instrument of change or documents satisfactorily evidencing such change are furnished to payor at the time the change occurs.

Any change of interest shall be made effective on the first day of the month following receipt of such notice by payor.

Any correspondence regarding this agreement shall be furnished to the addresses listed unless otherwise advised by either party.

In addition to the legal rights provided by the terms and provisions of this division order, an owner may have certain statutory rights under the laws of this state.

Signature of
Social Security/
Witness
Interest Owner
Tax I.D. No.
Address
____________

Failure to furnish your Social Security/Tax I.D. number will result in withholding tax in accordance with federal law, and any tax withheld will not be refundable by payor.

(e) If an owner in a producing property will not sign a division order because it contains provisions in addition to those provisions provided for in this section, payor shall not withhold payment solely because of such refusal. If an owner in a producing property refuses to sign a division order which includes only the provisions specified in

Subsection (c) of this section, payor may withhold payment without interest until such division order is signed.

(f) Payment may be remitted to a payee annually for the aggregate of up to 12 months' accumulation of proceeds if the payor owes the payee a total amount of $100 or less for production from all oil or gas wells for which the payor must pay the payee. However, the payor may hold accumulated proceeds of less than $10 until production ceases or the payor's responsibility for making payment for production ceases, whichever occurs first. On the written request of the payee, the payor shall remit payment of accumulated proceeds to the payee annually if the payor owes the payee less than $10. On the written request of the payee, the payor shall remit payment of proceeds to the payee monthly if the payor owes the payee more than $25 but less than $100.

(g) Division orders are binding for the time and to the extent that they have been acted on and made the basis of settlements and payments, and, from the time that notice is given that settlements will not be made on the basis provided in them, they cease to be binding. Division orders are terminable by either party on 30 days written notice.

(h) The execution of a division order between a royalty owner and lessee or between a royalty owner and a party other than lessee shall not change or relieve the lessee's specific, expressed or implied obligations under an oil and gas lease, including any obligation to market production as a reasonably prudent lessee. Any provision of a division order between payee and its lessee which is in contradiction with any provision of an oil and gas lease is invalid to the extent of the contradiction.

(i) A division order may be used to clarify royalty settlement terms in the oil and gas lease. With respect to oil and/or gas sold in the field where produced or at a gathering point in the immediate vicinity, the terms "market value," "market price," "prevailing price in the field," or other such language, when used as a basis of valuation in the oil and gas lease, shall be defined as the amount realized at the mouth of the well by the seller of such production in an arm's-length transaction.

§ 91.403. PAYMENT OF INTEREST ON LATE PAYMENTS. (a) If payment has not been made for any reason in the time limits specified in Section 91.402 of this code, the payor must pay interest to a payee beginning at the expiration of those time limits at two percentage points above the percentage rate charged on loans to depository institutions by the New York Federal Reserve Bank, unless a different rate of interest is specified in a written agreement between payor and payee.

(b) Subsection (a) of this section does not apply where payments are withheld or suspended by a payor beyond the time limits specified in Section 91.402 of this code because of the conditions enumerated in Section 91.402 of this code.

(c) The payor's obligation to pay interest and the payee's right to receive interest under Subsection (a) of this section terminate on delivery of the proceeds and accumulated interest to the comptroller as provided by Title 6, Property Code.

§ 91.404. NONPAYMENT OF OIL AND GAS PROCEEDS OR INTEREST. (a) If a payee seeks relief for the failure of a payor to make timely payment of proceeds from the sale of oil or gas or an interest in oil or gas as required under Section 91.402 or 91.403 of this code, the payee must give the payor written notice by mail of that failure as a prerequisite to beginning judicial action against the payor for nonpayment.

(b) The payor has 30 days after receipt of the required notice from the payee in which to pay the proceeds due, or to respond by stating in writing a reasonable cause for nonpayment.

(c) A payee has a cause of action for nonpayment of oil or gas proceeds or interest on those proceeds as required in Section 91.402 or 91.403 of this code in any court of competent jurisdiction in the county in which the oil or gas well is located.

§ 91.405. EXEMPTIONS. This subchapter does not apply to any royalties that are payable to:

(1) the board of regents of The University of Texas System under a lease of land dedicated to the permanent university fund; or

(2) the General Land Office as provided by Subchapter D, Chapter 52, of this code.

§ 91.406. ATTORNEY'S FEES AND MINIMUM AWARD. If a suit is filed to collect proceeds and interest under this subchapter, the court shall include in any final judgment in favor of the plaintiff an award of:

(1) reasonable attorney's fees; and

(2) if the actual damages to the plaintiff are less than $200, an additional amount so that the total amount of damages equals $200.

§ 91.407. NOTICE OF CHANGE OF PAYOR. (a) Following a change in payor, the new payor shall give written notice to each payee to whom the payor is responsible for distributing oil or gas proceeds. The notice must be given to the payee or the payee's designee at the payee's or designee's most recent known address.

(b) Upon receipt of payee's address from the operator or lessee, the payor must provide the notice within the time permitted for payment of proceeds and in accordance with the conditions for payment provided by Section 91.402. The notice must include:

(1) the information required by Sections 91.502(1), (2), and (12) and Section 91.503; and

(2) the payor's telephone number.

c) The notice may be given by any writing, including a division order, check stub, or attachment to a payment form.

(d) A payor that is obligated to pay interest to a payee under Section 91.403 and that does not give the payee a notice required by this section is liable to the payee for interest under that section at a rate that is two percent more than the rate provided by that section.

§ 91.408. INFORMATION FOR PAYEES OF PROCEEDS OF PRODUCTION FROM CERTAIN GAS WELLS. (a) A payor of proceeds from the sale of gas produced from a tight formation as defined by Section 29(c)(2)(B), Internal Revenue Code of 1986, annually shall furnish the payee a statement providing the information necessary to compute the federal income tax credit provided by that section for the gas for which payment was made in the preceding year, including:

(1) information as described in Section 91.502(1) of this code; and

(2) the volume of the gas, measured in:

(A) thousands of cubic feet and heating value; or

(B) millions of British thermal units for each thousand cubic feet.

(b) A payor shall furnish a statement required by Subsection (a) not later than March 15 each year.

## Limitations on the Ability to Seek indemnification from Oil and Gas Drillers (Oil-Field Anti-Indemnity Statute)

**CIVIL PRACTICE & REMEDIES CODE**

CHAPTER 127. INDEMNITY PROVISIONS IN CERTAIN MINERAL AGREEMENTS

Sec. 127.001. DEFINITIONS. In this chapter:

(1) 'Agreement pertaining to a well for oil, gas, or water or to a mine for a mineral':

(A) means:

(i) a written or oral agreement or understanding concerning the rendering of well or mine services; or

(ii) an agreement to perform a part of those services or an act collateral to those services, including furnishing or renting equipment, incidental transportation, or other goods and services furnished in connection with the services; but

(B) does not include a joint operating agreement.

(2) 'Joint operating agreement' means an agreement between or among holders of working interests or operating rights for the joint exploration, development, operation, or production of minerals.

(3) 'Mutual indemnity obligation' means an indemnity obligation in an agreement pertaining to a well for oil, gas, or water or to a mine for a mineral in which the parties agree to indemnify each other and each other's contractors and their employees against loss, liability, or damages arising in connection with bodily injury, death, and damage to property of the respective employees, contractors or their employees, and invitees of each party arising out of or resulting from the performance of the agreement.

(4) 'Well or mine service':

(A) includes:

(i) drilling, deepening, reworking, repairing, improving, testing, treating, perforating, acidizing, logging, conditioning, purchasing, gathering, storing, or transporting oil, brine water, fresh water, produced water, condensate, petroleum products, or other liquid commodities, or otherwise rendering services in connection with a well drilled to produce or dispose of oil, gas, other minerals or water; and

(ii) designing, excavating, constructing, improving, or otherwise rendering services in connection with a mine shaft, drift, or other structure intended for use in exploring for or producing a mineral; but

(B) does not include:

(i) purchasing, selling, gathering, storing, or transporting gas or natural gas liquids by pipeline or fixed associated facilities; or

(ii) construction, maintenance, or repair of oil, natural gas liquids, or gas pipelines or fixed associated facilities.

(5) 'Wild well' means a well from which the escape of oil or gas is not intended and cannot be controlled by equipment used in normal drilling practice.

(6) 'Unilateral indemnity obligation' means an indemnity obligation in an agreement pertaining to a well for oil, gas, or water or to a mine for a mineral in which one of the parties as indemnitor agrees to indemnify the other party as indemnitee with respect to claims for personal injury or death to the indemnitor's employees or agents or to the employees or agents of the indemnitor's contractors but in which the indemnitee does not make a reciprocal indemnity to the indemnitor.

Sec. 127.002. FINDINGS; CERTAIN AGREEMENTS AGAINST PUBLIC POLICY. (a) The legislature finds that an inequity is fostered on certain contractors by the indemnity provisions in certain agreements pertaining to wells for oil, gas, or water or to mines for other minerals.

(b) Certain agreements that provide for indemnification of a negligent indemnitee are against the public policy of this state.

(c) The legislature finds that joint operating agreement provisions for the sharing of costs or losses arising from joint activities, including costs or losses attributable to the negligent acts or omissions of any party conducting the joint activity:

(1) are commonly understood, accepted, and desired by the parties to joint operating agreements;

(2) encourage mineral development;

(3) are not against the public policy of this state; and

(4) are enforceable unless those costs or losses are expressly excluded by written agreement.

Acts 1985, 69th Leg., ch. 959, Sec. 1, eff. Sept. 1, 1985. Amended by Acts 1991, 72nd Leg., ch. 36, Sec. 2, eff. April 19, 1991.

Sec. 127.003. AGREEMENT VOID AND UNENFORCEABLE. (a) Except as otherwise provided by this chapter, a covenant, promise, agreement, or understanding contained in, collateral to, or affecting an agreement pertaining to a well for oil, gas, or water or to a mine for a mineral

is void if it purports to indemnify a person against loss or liability for damage that:

(1) is caused by or results from the sole or concurrent negligence of the indemnitee, his agent or employee, or an individual contractor directly responsible to the indemnitee; and

(2) arises from:

(A) personal injury or death;

(B) property injury; or

(C) any other loss, damage, or expense that arises from personal injury, death, or property injury.

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Sec. 127.004. EXCLUSIONS. This chapter does not apply to loss or liability for damages or an expense arising from:

(1) personal injury, death, or property injury that results from radioactivity;

(2) property injury that results from pollution, including cleanup and control of the pollutant;

(3) property injury that results from reservoir or underground damage, including loss of oil, gas, other mineral substance, or water or the well bore itself;

(4) personal injury, death, or property injury that results from the performance of services to control a wild well to protect the safety of the general public or to prevent depletion of vital natural resources; or

(5) cost of control of a wild well, underground or above the surface.

Sec. 127.005. INSURANCE COVERAGE. (a) This chapter does not apply to an agreement that provides for indemnity if the parties agree in writing that the indemnity obligation will be supported by liability insurance coverage to be furnished by the indemnitor subject to the limitations specified in Subsection (b) or (c).

(b) With respect to a mutual indemnity obligation, the indemnity obligation is limited to the extent of the coverage and dollar limits of insurance or qualified self-insurance each party as indemnitor has agreed to obtain for the benefit of the other party as indemnitee.

(c) With respect to a unilateral indemnity obligation, the amount of insurance required may not exceed $500,000.

Sec. 127.006. INSURANCE CONTRACT; WORKERS' COMPENSATION. This chapter does not affect:

(1) the validity of an insurance contract; or

(2) a benefit conferred by the workers' compensation statutes of this state.

Sec. 127.007. OWNER OF SURFACE ESTATE. This chapter does not deprive an owner of the surface estate of the right to secure indemnity from a lessee, an operator, a contractor, or other person conducting operations for the exploration or production of minerals of the owner's land.

## Limitation on Purchasing Mineral Interests by Mail

### PROPERTY CODE

§ 5.151. DISCLOSURE IN OFFER TO PURCHASE MINERAL INTEREST.

(a) A person who mails to the owner of a mineral or royalty interest an offer to purchase only the mineral or royalty interest, it being understood that for the purpose of this section the taking of an oil, gas, or mineral lease shall not be deemed a purchase of a mineral or royalty interest, and encloses an instrument of conveyance of only the mineral or royalty interest and a draft or other instrument, as defined in Section 3.104, Business & Commerce Code, providing for payment for that interest shall include in the offer a conspicuous statement printed in a type style that is approximately the same size as 14-point type style or larger and is in substantially the following form:

BY EXECUTING AND DELIVERING THIS INSTRUMENT YOU ARE SELLING ALL OR A PORTION OF YOUR MINERAL OR ROYALTY INTEREST IN (DESCRIPTION OF PROPERTY BEING CONVEYED).

(b) A person who conveys a mineral or royalty interest as provided by Subsection (a) may bring suit against the purchaser of the interest if:

(1) the purchaser did not give the notice required by Subsection (a); and

(2) the person has given 30 days' written notice to the purchaser that a suit will be filed unless the matter is otherwise resolved.

(c) A plaintiff who prevails in a suit under Subsection (b) may recover from the initial purchaser of the mineral or royalty interest the greater of:

(1) $100; or

(2) an amount up to the difference between the amount paid by the purchaser for the mineral or royalty interest and the fair market value of the mineral or royalty interest at the time of the sale.

(d) The prevailing party in a suit under Subsection (b) may recover:

(1) court costs; and

(2) reasonable attorney's fees.

(e) A person must bring a suit under Subsection (b) not later than the second anniversary of the date the person executed the conveyance.

(f) The remedy provided under this section shall be in addition to any other remedies existing under law, excluding rescission or other remedies that would make the conveyance of the mineral or royalty interest void or of no force and effect.

## Appendix D

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| **TITLE 16** | ECONOMIC REGULATION |
| **PART 1** | RAILROAD COMMISSION OF TEXAS |
| **CHAPTER 3** | OIL AND GAS DIVISION |
| **RULE §3.37** | Statewide Spacing Rule |

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(a) Distance requirements.

(1) No well for oil, gas, or geothermal resource shall hereafter be drilled nearer than 1,200 feet to any well completed in or drilling to the same horizon on the same tract or farm, and no well shall be drilled nearer than 467 feet to any property line, lease line, or subdivision line; provided the commission, in order to prevent waste or to prevent the confiscation of property, may grant exceptions to permit drilling within shorter distances than prescribed in this paragraph when the commission shall determine that such exceptions are necessary either to prevent waste or to prevent the confiscation of property.

(2) When an exception to this section is desired, application shall be made by filing the proper fee as provided in §3.78 of this title (relating to Fees and Financial Security Requirements) and the appropriate form according to the instructions on the form, accompanied by a plat as described in subsection (c) of this section. A person acquainted with the facts pertinent to the application shall certify that all facts stated in it are true and within the knowledge of that person.

(A) When an exception to only the minimum lease-line spacing requirement is desired, the applicant shall file a list of the mailing addresses of all affected persons, who, for tracts closer to the well than the greater of one-half of the prescribed minimum between-well spacing distance or the minimum lease-line spacing distance, include:

(i) the designated operator;

(ii) all lessees of record for tracts that have no designated operator; and

(iii) all owners of record of unleased mineral interests.

(B) When an exception to the minimum between-well spacing requirement of this section is desired, the applicant is required to file the mailing addresses of those persons identified in subparagraph (A)(i)-(iii) of this paragraph for each adjacent tract and each tract nearer to the well than the greater of one-half the prescribed minimum between-well spacing distance or the minimum lease-line spacing.

(3) An exception may be granted pursuant to subsection (h)(2) of this section, or after a public hearing held after at least 10 days notice to all persons described in paragraph (2) of this subsection. At any such hearing, the burden shall be on the applicant to establish that an exception to this section is necessary either to prevent waste or to prevent the confiscation of property. For purposes of giving notice of an application for an exception, the commission will presume that every person described in paragraph (2) of this subsection will be affected by the application, unless the Oil and Gas Division director or the director's delegate determines they are unaffected. Such determination will be made only upon written request and a showing by the applicant that:

(A) competent, conclusive geological or engineering data indicate that no drainage of hydrocarbons from the particular tract(s) subject to the request will occur due to production from the applicant's proposed well; and

(B) notice to the particular operator(s), lessee(s) of record, or owner(s) of record of unleased mineral interest would be unduly burdensome or expensive.

(b) The distances mentioned in subsection (a) of this section are minimum distances to provide standard development on a pattern of one well to each 40 acres in areas where proration units

have not been established.
(c) In filing an application for an exception to the distance requirements of this section, in addition to the plat requirements in §3.5 of this title (relating to Application to Drill, Deepen, Reenter, or Plug Back) (Statewide Rule 5), the applicant shall attach to each copy of the form a plat that:
(1) shows to scale the property on which the exception is sought; all other applied for, permitted, and completed oil, gas, or oil and gas wells in the same field and reservoir on said property; and all adjoining surrounding properties and completed wells in the same field and reservoir within the prescribed minimum between-well spacing distance of the applicant's well;
(2) shows the entire lease, pooled unit, or unitized tract indicating the names and offsetting properties of all affected offset operators;
(3) corresponds to the listing required under subsection (a)(2) of this section;
(4) is certified by a person acquainted with the facts pertinent to the application that the plat is accurately drawn to scale and correctly reflects all pertinent and required data.
(d) In the interest of protecting life and for the purpose of preventing waste and preventing the confiscation of property, the commission reserves the right in particular oil, gas, and geothermal resource fields to enter special orders increasing or decreasing the minimum distances provided by this section.
(e) No well drilled in violation of this section without special permit obtained, issued, or granted in the manner prescribed in said section, and no well drilled under such special permit or on the commission's own order which does not conform in all respects to the terms of such permit shall be permitted to produce either oil, gas, or geothermal resources and any such well so drilled in violation of said section or on the commission's own order shall be plugged.
(f) No operator shall commence the drilling of a well, either on a regular location or on a Rule 37 exception location, until first having been notified by the commission that the regular location has been approved, or that the Rule 37 exception location has been approved. Failure of an operator to comply with this subsection will cause such well to be closed in and the holding up of the allowable of such well.
(g) Subdivision of property.
(1) In applying Rule 37 (Statewide Spacing Rule) of statewide application and in applying every special rule with relation to spacing in every field in this state, no subdivision of property made subsequent to the adoption of the original spacing rule will be considered in determining whether or not any property is being confiscated within the terms of such spacing rule, and no subdivision of property will be regarded in applying such spacing rule or in determining the matter of confiscation if such subdivision took place subsequent to the promulgation and adoption of the original spacing rule.
(2) Any subdivision of property creating a tract of such size and shape that it is necessary to obtain an exception to the spacing rule before a well can be drilled thereon is a voluntary subdivision and not entitled to a permit to prevent confiscation of property if it were either:
(A) segregated from a larger tract in contemplation of oil, gas, or geothermal resource development; or
(B) segregated by fee title conveyance from a larger tract after the spacing rule became effective and the voluntary subdivision rule attached.
(3) The date of attachment of the voluntary subdivision rule is the date of discovery of oil, gas, or geothermal resource production in a certain continuous reservoir, regardless of the subsequent lateral extensions of such reservoir, provided that such rule does not attach in the case of a segregation of a small tract by fee title conveyance which is not located in an oil, gas, or geothermal resource field having a discovery date prior to the date of such segregation.
(4) The date of attachment of the voluntary subdivision rule for multiple reservoir fields located in the same structural feature and separated vertically but not laterally (i.e., the multiple reservoirs

overlap geographically at least in part), shall be the same date as that assigned to the earliest discovery well for such multiple reservoir structure.

(5) If a newly discovered reservoir is located outside the then productive limits of any previously discovered reservoirs and is classified by the commission as a newly discovered field, then the date of discovery of such newly found reservoir remains the date of attachment for the voluntary subdivision rule, even though subsequent development may result in the extension of such newly discovered reservoir until it overlies or underlies older reservoirs with prior discovery dates.

(6) The date of attachment of the voluntary subdivision rule for a reservoir that has been developed through expansion of separately recognized fields into a recognized single reservoir and is merged by commission order is the earliest discovery date of production from such merged reservoir, and that date will be used subsequent to the date of merger of the fields into a single field.

(7) The date of attachment of the voluntary subdivision rule for a reservoir under any special circumstance which the commission deems sufficient to provide for an exception may be established other than as prescribed in this section, so that innocent parties may have their rights protected.

(h) Exceptions to Rule 37.

(1) An order granting exception to Rule 37 wherein protest is had shall carry as its last paragraph the following language: It is further ordered by the commission that this order shall not be final until 20 days after it is actually mailed to the parties by the commission; provided that if a motion for rehearing of the application is filed by any party at interest within such 20-day period, this order shall not become final until such motion is overruled, or if such motion is granted, this order shall be subject to further action by the commission. Permits issued pursuant to paragraph (2) of this subsection shall be issued without the 20-day waiting period.

(2) The director of the Oil and Gas Division or a delegate of the director may issue an exception permit for drilling, deepening, or additional completion, recompletion, or reentry in an existing well bore if:

(A) a notice of at least 10 days has been given, and no protest has been made to the application; or

(B) written waivers of objection are received from all persons to whom notice would be given pursuant to subsection (a)(2) of this section.

(3) Applications filed for drilling, deepening, or additional completion, recompletion, or reentry will be processed and permit issued in accordance with this regulation, subject to the commission's discretion to set any application for hearing. If the director or a delegate of the director declines to grant an application, the operator may request a hearing.

(i) Rule 37 permits.

(1) Unless otherwise specified in a permit or in a final order granting an exception to this section, permits issued by the commission for completions requiring an exception to this section shall expire two years from the effective date of the permit unless drilling operations are commenced in good faith within the two-year permit period. The permit period will not be extended.

(2) So long as a Rule 37 exception is in litigation, the two-year permit period will not commence. On final adjudication and decree from the last court of appeal the two-year permit period will commence, beginning on the date of final decree.

(j) Once an application for a spacing exception has been denied, no new application shall be entertained except on changed conditions. Changed conditions in the commission's administration of its Spacing Rule 37 and amendments thereto applicable to the various special fields and reservoirs of Texas and in passing upon applications for permits under said rule and amendments shall include, among other things, the following.

(1) Any material changes in the physical conditions of the producing reservoir under the tract under consideration or under the area surrounding said tract which would materially affect the recovery of oil, gas, or geothermal resource from the given tract.

(2) Any material changes in the distribution or allocation of allowable production in the area surrounding the tract under consideration which would materially affect or tend to affect the recovery of oil, gas, or geothermal resource from the given tract.

(3) Any additional permits granted by the commission for wells drilled in the area surrounding or on offset tracts to the tract under consideration which would materially affect or tend to affect the recovery of oil, gas, or geothermal resource from the given tract.

(4) Any additional facts or evidence thereof materially affecting or tending to affect the recovery of oil, gas, or geothermal resource from the applicant's tract, or the property rights of applicant, which were not known of and considered by the commission at any previous hearing or application thereon.

(k) Exceptions to Statewide Rule 37 apply to the total depth for which the permit is granted or if special field rules are applicable, an exception to the spacing rule shall be granted only for the reservoir or reservoirs or applicable depth to which the well is projected. Subsequent recompletion of the well to reservoirs other than that covered by the permit issued would be granted only after the filing and processing of a new application.

(l) Salt dome oil or gas fields.

(1) The provisions of this section shall not apply to certain approved salt dome oil or gas fields. An application for classification as a salt dome oil or gas field shall include the following:

(A) geological evidence proving that an oil or gas field is a piercement-type salt dome, that faulting has caused the producing formation to be at a 45 angle or greater, and that each well is likely to be completed in a separate reservoir;

(B) establishment, by plat or otherwise, of the probable productive limits of the salt dome area;

(C) certification that notice of the application for salt dome classification with evidence included has been given to all operators in the field or, if a new field, in accordance with subsection (a)(2) of this section; and

(D) a list of persons notified and the date notice was mailed.

(2) The director of the Oil and Gas Division, or the director's delegate, may administratively grant an application for salt dome classification if the evidence proves that the oil or gas field is a salt dome.

(3) The operator may request a hearing if the director of the Oil and Gas Division, or the director's delegate, declines to approve an application. If an application is protested within 10 days of notice, it will be set for hearing. After hearing, the examiner shall recommend final commission action.

(4) The amendment providing for administrative approval of salt dome oil and gas fields does not alter the status of those fields previously approved and listed in this section.

(m) Wells that were deviated, whether intentionally or otherwise, prior to April 1, 1949, and are bottomed on the lease where permitted, are legal wells. The Rule 37 department will develop the record in each reapplication for such deviated wells so that the commission can determine the condition of each such well. The following will be adduced from sworn testimony and authenticated data at each such hearing.

(1) That such well was deviated before April 1, 1949. Proof of completion of the well prior to that date and its subsequent producing status is not adequate proof of deviation.

(2) That such well was completed on the lease where the surface location was permitted. Such bottom hole location must be proven by the submission of an acceptable authenticated directional survey.

(3) That such bottom hole location is one that either is not in direct violation of a condition or limitation placed in the permit to drill, or is not in violation of a specific commission order. Example: Denial order for a Rule 37 application for a comparable location.

(4) That the present operator of such well or his predecessor has not filed either a false inclination or a false directional survey with the commission.

(5) A well that is either bottomed off the lease, deviated after April 1, 1949, drilled in direct violation of a specific condition or limitation placed in the Rule 37 permit, or is in violation of a specific commission order, is an illegal well and it shall not be permitted, and such well where permit is refused shall not be considered a replaceable well under commission replacement-well regulation.

(6) The provisions of this section do not preclude an operator from applying for approval of the bottom hole location of a deviated well as a reasonable location under the rules and regulations now applicable, provided, that such bottom hole location shall not be approved unless the applicant proves that a vertical projection of the permitted surface location for such well is within the productive limits of the reservoir.

# Texas Administrative Code

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|---|---|
| **TITLE 16** | ECONOMIC REGULATION |
| **PART 1** | RAILROAD COMMISSION OF TEXAS |
| **CHAPTER 3** | OIL AND GAS DIVISION |
| **RULE §3.38** | Well Densities |

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(a) Definitions. The following words and terms, when used in this section, shall have the following meanings, unless the context clearly indicates otherwise.

(1) Commission designee--Director of the Oil and Gas Division or any Commission employee designated in writing by the director or the Commission.

(2) Drilling unit--The acreage assigned to a well for drilling purposes.

(3) Proration unit--The acreage assigned to a well for the purpose of assigning allowables and allocating allowable production to the well.

(4) Substandard acreage--Less acreage than the smallest amount established for standard or optional drilling units.

(5) Surplus acreage--Substandard acreage within a lease, pooled unit, or unitized tract that remains unassigned after the assignment of acreage to each applied for, permitted, or completed well in a field, in an amount equaling or exceeding the amount established for standard or optional drilling units. Surplus acreage is distinguished from the term "tolerance acreage,"in that tolerance acreage is defined in context with proration regulation, while surplus acreage is defined by this rule only in context with well density regulation.

(6) Tolerance acreage--Acreage within a lease, pooled unit, or unitized tract that may be assigned to a well for proration purposes pursuant to special field rules in addition to the amount established for a prescribed or optional proration unit.

(b) Density requirements.

(1) General prohibition. No well shall be drilled on substandard acreage except as hereinafter provided.

(2) Standard units.

(A) The standard drilling unit for all oil, gas, and geothermal resource fields wherein only spacing rules, either special, country regular, or statewide, are applicable is hereby prescribed to be the following.

(B) The spacing rules listed in subparagraph (A) of this paragraph are not exclusive. If any spacing rule not listed in subparagraph (A) of this subsection is brought to the attention of the commission, it will be given an appropriate acreage assignment.

(c) Development to final density. An application to drill a well for oil, gas, or geothermal resource on a drilling unit composed of surplus acreage, commonly referred to as the "tolerance well," may be granted as regular when the operator seeking such permit certifies to the commission in a prescribed form the necessary data to show that such permit is needed to develop a lease, pooled unit, or unitized tract to final density, and only in the following circumstances:

(1) when the amount of surplus acreage equals or exceeds the maximum amount provided for tolerance acreage by special or county regular rules for the field, provided that this paragraph does not apply for a lease, pooled unit, or unitized tract that is completely developed with optional units and the special or county regular rules for the field do not have a tolerance provisions expressly made applicable to optional proration units;

(2) if the special or county regular rules for the field do not have a tolerance provision expressly made applicable to optional proration units, when the amount of surplus acreage equals or

exceeds one-half of the smallest amount established for an optional drilling unit; or
(3) if the applicable rules for the field do not have a tolerance provision for the standard drilling or proration unit, when the amount of surplus acreage equals or exceeds one-half the amount prescribed for the standard unit.
(d) Applications involving the voluntary subdivision rule.
(1) Density exception not required. An exception to the minimum density provision is not required for the first well in a field on a lease, pooled unit, or unitized tract composed of substandard acreage, when the leases, or the drillsite tract of a pooled unit or unitized tract:
(A) took its present size and shape prior to the date of attachment of the voluntary subdivision rule (§3.37(g) of this title (relating to Statewide Spacing Rule)); or
(B) took its present size and shape after the date of attachment of the voluntary subdivision rule (§3.37(g) of this title (relating to Statewide Spacing Rule)) and was not composed of substandard acreage in the field according to the density rules in effect at the time it took its present size and shape.
(2) Density exception required. An exception to the density provision is required, and may be granted only to prevent waste, for a well on a lease, pooled unit, or unitized tract that is composed of substandard acreage and that:
(A) took its present size and shape after the date of attachment of the voluntary subdivision rule (§3.37(g) of this title (relating to the Statewide Spacing Rule)); and
(B) was composed of substandard acreage in the field according to the density rules in effect at the time it took its present size and shape.
(3) Unit dissolution.
(A) If two or more separate tracts are joined to form a unit for oil or gas development, the unit is accepted by the Commission, and the unit has produced hydrocarbons in the preceding twenty (20) years, the unit may not thereafter be dissolved into the separate tracts with the rules of the commission applicable to each separate tract if the dissolution results in any tract composed of substandard acreage for the field from which the unit produced, unless the Commission approves such dissolution.
(B) The Commission shall grant approval only after application, notice, and an opportunity for hearing. The applicant seeking the unit dissolution shall provide a list of the names and addresses of all current lessees and unleased mineral interest owners of each tract within the joined or unitized tract at the time the application is filed. The Commission shall give notice of the application to all current lessees and unleased mineral interest owners of each tract within the joined or unitized tract. Additionally, if one or more wells on the unitized tract has produced from the field within the 12-month period prior to the application, the applicant shall include on the list all affected persons described in subsection (h)(1)(A) of this section, and the Commission shall give notice of the application to these affected persons.
(C) A Commission designee may grant administrative approval if the Commission designee determines that granting the application will not result in the circumvention of the density restrictions of this section or other Commission rules, and if either:
(i) written waivers are filed by all affected persons; or
(ii) no protest is filed within the time set forth in the notice of application.
(e) Application involving unitized areas with entity for density orders. An exception to the minimum density provision is not required for a well in a unitized area for which the commission has granted an entity for density order, if the sum of all applied for, permitted, or completed producing wells in the field within the unitized area, multiplied by the applicable density provision, does not exceed the total number of acres in the unitized area. The operator must indicate the docket number of the entity for density order on the application form.
(f) Exceptions to density provisions authorized. The Commission, or Commission designee, in order to prevent waste or, except as provided in subsection (d)(2) of this section, to prevent the

confiscation of property, may grant exceptions to the density provisions set forth in this section. Such an exception may be granted only after notice and an opportunity for hearing.

(g) Filing requirements.

(1) Application. An application for permit to drill shall include the fees required in §3.78 of this title (relating to Fees and Financial Security Requirements) and shall be certified by a person acquainted with the facts, stating that all information in the application is true and complete to the best of that person's knowledge.

(2) Plat. When filing an application for an exception to the density requirements of this section, in addition to the plat requirements in §3.5 of this title (relating to Application to Drill, Deepen, Reenter, or Plug Back) (Statewide Rule 5), the applicant shall attach to each copy of the application a plat that:

(A) depicts the lease, pooled unit, or unitized tract, showing thereon the acreage assigned to the drilling unit for the proposed well and the acreage assigned to all current applied for, permitted, or completed oil, gas, or oil and gas wells in the same field or reservoir which are located within the lease, pooled unit, or unitized tract;

(B) on large leases, pooled units, or unitized tracts, if the established density is not exceeded as shown on the face of the application, outlines the acreage assigned to the well for which the permit is sought and the immediately adjacent wells on the lease, pooled unit, or unitized tract;

(C) on leases, pooled units, or unitized tracts from which production is secured from more than one field, outlines the acreage assigned to the wells in each field that is the subject of the current application;

(D) corresponds to the listing required under subsection (g)(1)(A) of this section.

(E) is certified by a person acquainted with the facts pertinent to the application that the plat is accurately drawn to scale and correctly reflects all pertinent and required data.

(3) Substandard acreage. An application for a permit to drill on a lease, pooled unit, or unitized tract composed of substandard acreage must include a certification in a prescribed form indicating the date the lease, or the drillsite tract of a pooled unit or unitized tract, took its present size and shape.

(4) Surplus acreage. An application for permit to drill on surplus acreage pursuant to subsection (c) of this section must include a certification in a prescribed form indicating the date the lease, pooled unit, or unitized tract took its present size and shape.

(5) Certifications. Certifications required under paragraphs (3) and (4) of this subsection shall be filed on Form W-1A, Substandard Acreage Certification.

(A) The operator shall file the Form W-1A with the drilling permit application and shall indicate the purpose of filing. The operator shall accurately complete all information required on the form in accordance with instructions on the form.

(B) The operator shall list the field or fields for which the substandard acreage certification applies in the designated area on the form. If there are more than three fields for which the certification applies, the operator shall attach additional Forms W-1A and shall number the additional pages in sequence.

(C) The operator shall file the original Form W-1A with the Commission's Austin office and a copy with the appropriate district office, unless the operator files electronically through the Commission's Electronic Compliance and Approval Process (ECAP) system.

(D) The operator or the operator's agent shall certify the information provided on the Form W-1A is true, complete, and correct by signing and dating the form, and listing the requested identification and contact information.

(E) Failure to timely file the required information on the appropriate form may result in the dismissal of the application.

(h) Procedure for obtaining exceptions to the density provisions.

(1) Filing requirements. If a permit to drill requires an exception to the applicable density

provision, the operator must file, in addition to the items required by subsection (g) of this section:

(A) a list of the names and addresses of all affected persons. For the purpose of giving notice of application, the Commission presumes that affected persons include the operators and unleased mineral interest owners of all adjacent offset tracts, and the operators and unleased mineral interest owners of all tracts nearer to the proposed well than the prescribed minimum lease-line spacing distance. The Commission designee may determine that such a person is not affected only upon written request and a showing by the applicant that:

(i) competent, convincing geological or engineering data indicate that drainage of hydrocarbons from the particular tracts subject to the request will not occur due to production from the proposed well; and

(ii) notice to the particular operators and unleased mineral interest owners would be unduly burdensome or expensive;

(B) engineering and/or geological data, including a written explanation of each exhibit, showing that the drilling of a well on substandard acreage is necessary to prevent waste or to prevent the confiscation of property;

(C) additional data requested by the Commission designee.

(2) Notice of application. Upon receipt of a complete application, the Commission will give notice of the application by mail to all affected persons for whom signed waivers have not been submitted.

(3) Approval without hearing. If the Commission designee determines, based on the data submitted, that a permit requiring an exception to the applicable density provision is justified according to subsection (f) of this section, then the Commission designee may issue the exception permit administratively if:

(A) signed waivers from all affected persons were submitted with the application; or

(B) notice of application was given in accordance with paragraph (2) of this subsection and no protest was filed within 21 days of the notice; or

(C) no person appeared to protest the application at a hearing scheduled pursuant to paragraph (4)(A) of this subsection.

(4) Hearing on the application.

(A) If a written protest is filed within 21 days after the notice of application is given in accordance with paragraph (2) of this subsection, the application will be set for hearing.

(B) If the application is not protested and the Commission designee determines that a permit requiring an exception to the applicable density provision is not justified according to subsection (f) of this section, the operator may request a hearing to consider the application.

(i) Duration. A permit is issued as an exception to the applicable density provision shall expire two years from the effective date of the permit; unless drilling operations are commenced in good faith within the two year period.

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## Texas Administrative Code

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| **TITLE 16** | ECONOMIC REGULATION |
| **PART 1** | RAILROAD COMMISSION OF TEXAS |
| **CHAPTER 3** | OIL AND GAS DIVISION |
| **RULE §3.11** | Inclination and Directional Surveys Required |

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(a) General. All wells shall be drilled as nearly vertical as possible by normal, prudent, practical drilling operations. Nothing in this section shall be construed to permit the drilling of any well in

such a manner that the wellbore crosses lease and/or property lines (or unit lines in cases of pooling) without special permission.

(b) Inclination surveys.

(1) Requirements.

(A) An inclination survey made by persons or concerns approved by the commission shall be filed on a form prescribed by the commission for each well drilled or deepened with rotary tools, except as hereinafter provided, or when, as a result of any operation, the course of the well is changed. The first shot point of such inclination survey shall be made at a depth not greater than 500 feet below the surface of the ground, and succeeding shot points shall be made either at 500-foot intervals or at the nearest drill bit change thereto, but not to exceed 1,000 feet apart.

(B) Inclination surveys conforming to these requirements may be made either during the normal course of drilling or after the well has reached total depth. Acceptable directional surveys may be filed in lieu of inclination surveys.

(C) Copies of all directional or inclination surveys, regardless of the reason for which they are run, shall be filed as a part of or in addition to the inclination surveys otherwise required by this section. If computations are made from dipmeter surveys to determine the course of the wellbore in any portion of the surveyed interval, a report of such computations shall be required.

(D) Inclination surveys shall not be required in any well drilled to a total depth of 2,000 feet or less on a regular location at least 150 feet from the nearest lease line, provided the well is not intentionally deviated from the vertical in any manner whatsoever.

(E) Inclination surveys shall not be required on wells deepened with rotary tools if the well is deepened no more than 300 feet or the distance from the surface location to the nearest lease or boundary line, whichever is the lesser, and provided that the well was not intentionally deviated from the vertical at any time before or after the beginning of deepening operations.

(F) Inclination surveys will not be required on wells that are drilled and completed as dry holes and are permanently plugged and abandoned. If such wells are reentered at a later date and completed as producers or injection or disposal wells, inclination reports will be required and must be filed with the appropriate completion form for the well.

(G) Inclination survey filings will not be required on wells that are reentries within casing of previously producing wells if inclination data are already on file with the Railroad Commission of Texas (commission). If such data are not on file with the commission, the results of an inclination survey must be reported on the appropriate form and filed with the completion form, except as provided by subparagraph (D) of this paragraph.

(2) Reports.

(A) The report form shall be signed and certified by a party having personal knowledge of the facts therein contained. The report shall include a tabulation of the maximum drifts which could occur between the surface and the first shot point, and each two successive shot points, assuming that all of the unsurveyed hole between any two shot points has the same inclination as that measured at the lowest shot point, and the total possible accumulative drift, assuming that all measured angles of inclination are in the same direction.

(B) In addition, the report shall be accompanied by a certified statement of the operator, or of someone acting at his direction on his behalf, either:

(i) that the well was not intentionally deviated from vertical; or

(ii) that the well was deviated at random, with an explanation of the circumstances.

(C) The report shall be filed in the district office by attaching one copy to each appropriate completion form for the well.

(D) The commission may require the submittal of the original charts, graphs, or discs resulting from the surveys.

(c) Directional surveys.

(1) When required.

(A) When the maximum displacement indicated by an inclination survey is greater than the actual distance from the surface location to the nearest lease line or pooled unit boundary, it will be considered to be a violating well subject to plugging and to penalty action. However, an operator may submit a directional survey, run at his own expense by a commission approved surveying company, to show the true bottom hole location of the well to be within the prescribed limits. When such directional survey shows the well to be bottomed within the confines of the lease, but nearer to a well or lease line or pooled unit boundary than allowed by applicable rules, or by the permit for the well if the well has been granted an exception to §3.37 of this title (relating to Statewide Spacing Rule), a new permit will be required if it is established that the bottom hole location or completion location is not a reasonable location.

(B) Directional surveys shall be required on each well drilled under the directional deviation provisions of this section.

(C) No oil, gas, or geothermal resource allowable shall be assigned any well on which a directional survey is required under any provision of this section until a directional survey has been filed with and accepted by the commission.

(2) Filing and type of survey.

(A) Directional surveys required under this section must be run by competent surveying companies, approved by the commission, signed and certified by a person having actual knowledge of the facts, in the manner prescribed by the commission in accordance with §3.12 of this title (relating to Directional Survey Company Report).

(B) All directional surveys, unless otherwise specified by the commission, shall be either single shot surveys or multi-shot surveys with the shot points not more than 200 feet apart, beginning within 200 feet of the surface, and the bottom hole location must be oriented both to the surface location and to the lease lines (or unit lines in cases of pooling).

(C) If more than 200 feet of surface casing has been run, the operator may begin the directional survey immediately below the surface casing depth. However, if such method is used, the inclination drifts from the surface of the ground to the surface casing depth must be added cumulatively and reported on the appropriate form. This total shall be assumed to be in the direction least favorable to the operator, and such point shall be considered the starting point of the directional survey.

(d) Intentional deviation of wells.

(1) Definitions.

(A) Directional deviation--The intentional deviation of a well from vertical in a predetermined compass direction.

(B) Random deviation--The intentional deviation of a well without regard to compass direction for one of the following reasons:

(i) to straighten a hole which has become crooked in the normal course of drilling;

(ii) to sidetrack a portion of a hole because of mechanical difficulty in drilling.

(2) When permitted.

(A) Directional deviation. A permit for directionally deviating a well may be granted by the commission:

(i) for the purpose of seeking to reach and control another well which is out of control or threatens to evade control;

(ii) where conditions on the surface of the ground prevent or unduly complicate the drilling of a well at a regular location;

(iii) where conditions are encountered underground which prevent or unduly hinder the normal completion of the well;

(iv) where it can be shown to be advantageous from the standpoint of mechanical operation to drill more than one well from the same surface location to reach the productive horizon at essentially the same positions as would be reached if the several wells were normally drilled from

regular locations prescribed by the well spacing rules in effect;

(v) for the purpose of drilling a horizontal drainhole; or

(vi) for other reasons found by the commission to be sufficient after notice and hearing.

(B) Random deviation. Permission for the random deviation of a well may be granted by the commission whenever the necessity for such deviation is shown, as prescribed in paragraph (3)(C) of this subsection.

(3) Applications for deviation.

(A) Applications for wells to be directionally deviated must specify on the application to drill both the surface location of the well and the projected bottom hole location of the well. On the plat, in addition to the plat requirements provided for in §3.5 of this title (relating to Application to Drill, Deepen, Reenter, or Plug Back) (Statewide Rule 5), the following shall be included:

(i) two perpendicular lines providing the distance in feet from the projected bottomhole location, rather than the surface location, to the nearest points on the lease, pooled unit, or unitized tract line. If there is an unleased interest in a tract of the pooled unit or unitized tract that is nearer than the pooled unit or unitized tract line, the nearest point on that unleased tract boundary shall be used;

(ii) a line providing the distance in feet from the projected bottomhole location to the nearest point on the lease line, pooled unit line, or unitized tract line. If there is an unleased interest in a tract of the pooled unit that is nearer than the pooled unit line, the nearest point on that unleased tract boundary shall be used;

(iii) a line providing the distance in feet from the projected bottomhole location, rather than the surface location, to the nearest oil, gas, or oil and gas well, identified by number, applied for, permitted, or completed in the same lease, pooled unit, or unitized tract and in the same field and reservoir; and

(iv) perpendicular lines providing the distance in feet from the two nearest non-parallel survey/section lines to the projected bottomhole location.

(B) If the necessity for directional deviation arises unexpectedly after drilling has begun, the operator shall give written notice by letter or telegram of such necessity to the appropriate district office and to the commission office in Austin, and upon giving such notice, the operator may proceed with the directional deviation. The commission may, at its discretion, accept written notice electronically transmitted. If the operator proceeds with the drilling of a deviated well under such circumstances, he proceeds at his own risk. Before any allowable shall be assigned to such well, a permit for the subsurface location of each completion interval shall be obtained from the commission under the provisions set out in the commission rules. However, should the operator fail to show good and sufficient cause for such deviation, no permit will be granted for the well.

(C) If the necessity for random deviation arises unexpectedly after the drilling has begun, the operator shall give written notice by letter or telegram of such necessity to the appropriate district office and to the commission office in Austin, and, upon giving such notice, the operator may proceed with the random deviation, subject to compliance with the provisions of this section on inclination surveys. The commission may, at its discretion, accept written notice electronically transmitted.

(e) Surveys on request of other operators. The commission, at the written request of any operator in a field, shall determine whether a directional survey, an inclination survey, or any other type of survey approved by the commission for the purpose of determining bottom hole location of wells, shall be made in regard to a well complained of in the same field.

(1) The complaining party must show probable cause to suspect that the well complained of is not bottomed within its own lease lines.

(2) The complaining party must agree to pay all costs and expenses of such survey, shall assume all liability, and shall be required to post bond in a sufficient sum as determined by the

commission as security against all costs and risks associated with the survey.

(3) The complaining party and the commission shall agree upon the selection of the well surveying company to conduct the survey, which shall be a surveying company on the commission's approved list.

(4) The survey shall be witnessed by the commission, and may be witnessed by any party, or his agent, who has an interest in the field.

(5) Nothing in these rules shall be construed to prevent or limit the commission, acting on its own authority, from conducting spot checks and surveys at any time and place for the purpose of determining compliance with the commission rules and regulations.

(f) Penalties.

(1) False reports. The filing of a false or incorrect directional survey shall be grounds for cancellation of the well permit, for pipeline severance of the lease on which the well is located, for penalty action under the applicable statutes, and/or for such other and further action as may be appropriate.

(2) Other. The same penalties and actions as set forth in paragraph (1) of this subsection shall be assessable against any operator who refuses to comply with a commission order which issues under subsection (e) of this section.

## Appendix E

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