

APPEARANCES: **Ron M. Barnes**, attorney, appeared on behalf of applicant, RDT Properties, Inc. ("RDT"); **William H. Huffman**, attorney, appeared on behalf of Carnes Petroleum Corporation and Dwain C. and Carl S. Carnes ("Carnes"); **Gregory L. Mahaffey**, attorney, appeared on behalf of Toklan Oil and gas Corporation ("Toklan"); and **Jim Hamilton**, Assistant General Counsel for the Conservation Division, filed notice of appearance.

The Administrative Law Judge ("ALJ") filed her Report of the Administrative Law Judge on the 2nd day of September, 2011, to which Exceptions were timely filed and proper notice given of the setting of the Exceptions.

The Appellate argument concerning the Oral Exceptions were referred to **Patricia D. MacGuigan**, Oil and Gas Appellate Referee ("Referee"), on the 14th day of October, 2011. After considering the arguments of counsel and the record contained within this Cause, the Referee finds as follows:

STATEMENT OF THE CASE

CARNES APPEALS the ALJ's recommendation that the subject application should be granted with RDT named as operator of the Cleveland Field Unit and the plan of unitization should be adopted.

RDT seeks to unitize the subject lands for the purpose of developing and managing a geological interval from the top of the Cottage Grove (Peoples) Sand to the base of the Arbuckle, including but not limited to the Cottage Grove (Peoples), Layton, Cleveland, Big Lime, Oswego, Prue, Skinner, Red Fork, Bartlesville, Simpson and Arbuckle formations as one unit and increase recovery of reserves for the owners in the proposed unit. Carnes opposes the creation of the unit because it will interfere with their current production income. Additionally, to participate in the unit an initial investment of over \$1 million would be Carnes' proportionate share or, in the alternative, participation as a non-consenting party would result in the Carnes' interest being subject to the statutorily imposed 300% penalty before any unit proceeds would be distributed to the Carnes. The Cleveland Field Unit unitization would contain 1,760 acres more or less.

CARNES TAKES THE POSITION:

- (1) The ALJ Report is contrary to the evidence and to the law.

(2) The ALJ's Report fails to protect the owners in the common sources of supply.

(3) The ALJ's Report fails to meet the statutory requirements set forth in Title 52 O.S. Section 281.1 et seq.

(4) RDT proposes the addition of \$4 million of expense incurred in the operation of the waterflood unit and enhanced recovery project authorized by Order No. 28979 and Order No. 328676. RDT requests retroactive operation of the plan of unitization and requires all owners to pay expenses incurred in the operation of an enhanced recovery project that they had no interest in and received no benefit from such enhanced recovery project.

(5) The method to allocate production does not comply with the statutory requirements. The order shall be under terms and conditions, as may be shown by the evidence to be fair, reasonable, equitable and which are necessary or proper to protect, safeguard, and adjust the respective rights and obligations of the several persons affected, including royalty interest owners, Owners of overriding royalties, oil and gas payments, carried interests, mortgagees, lien claimants and others, as well as lessees. The plan of unitization is designed to solely favor RDT and does not protect Carnes.

(6) The allocation factor is based solely on surface acreage, number of wells and current production. A separately owned tract's fair, equitable and reasonable share of the unit production shall be measured by the value of each such tract for oil and gas purposes and its contributing value to the unit in relation to like values of other tracts in the unit, taking into account acreage, the quantity of oil and gas recoverable therefrom, location on structure, its probable productivity of oil and gas in the absence of unit operations, the burden of operation to which the tract will or is likely to be subjected, or so many of said factors, or such other pertinent engineering, geological, or operating factors, as may be reasonably susceptible of determination. RDT admitted that original recoverable reserves, remaining primary reserves and recoverable secondary reserves were not utilized to determine allocation factors. The method utilized does not conform to statutory requirements and fails to take into account any engineering, geological or operating factors in determining the allocation factor. The allocation factor used does not determine the quantity of oil and gas recoverable therefrom or location on structure.

(7) RDT admitted that the Cleveland formation contained approximately 50% of the ultimate recoverable reserves, however, the Cleveland reserves were not considered in the preparation of the allocation. RDT exhibits reflect substantial recoverable reserves under the Carnes tract and no consideration is given by the RDT allocation factors.

(8) The Bartlesville formation contains a substantial amount of the recoverable reserves. The area owned by RDT has been subject to waterflooding operations for 64 years and RDT has represented the waterflooded area has an oil cut of less than 1%. The Carnes tract exhibits a 15% oil cut. RDT further admitted the majority of the recoverable Bartlesville reserves are on the periphery of the unit, favoring the Carnes tract but no consideration is given to the Carnes tract for the recoverable reserves in the Bartlesville.

(9) The parties disputed the exact amount of remaining recoverable reserves under the Carnes tract and RDT admitted there are at least 57,946 bbls of remaining primary reserves. RDT did not present a witness to testify as to the remaining primary recoverable reserves and only set the figures on an exhibit exchanged. Carnes calculated 134,171 barrels of remaining primary recoverable reserves. Carnes will incur no additional capital expense to recover those remaining reserves, however, the RDT plan requires Carnes to pay approximately \$1,700,000 in order to recover those remaining primary reserves. The plan does not protect Carnes' interest in the remaining primary reserves.

(10) Reasonable provision shall be made in the plan of unitization for carrying or otherwise financing lessees who are unable to promptly meet their financial obligations in connection with the unit by establishing a fair rate of interest to all concerned based upon the terms and conditions as to time. The plan of unitization does not provide for a method to finance the Carnes' interest but requires the prepayment by Carnes of the estimated costs. The ALJ based her decision to grant the application on Carnes failure to inquire or seek financing. The ability or not of Carnes to obtain financing does not relieve RDT from meeting the statutory requirements.

(11) The exhibits of RDT and Carnes indicated the Carnes property is fault separated from the main unit and will not and has not benefitted from the waterflooding operation that has been conducted on the existing waterflood/enhanced recovery unit. RDT did not dispute or contest the testimony and existence of the fault as opined by the Carnes witness. The ALJ concludes the evidence does not show separation, however the only expert witness testimony concluded the Carnes property is in fact fault separated. There is no evidence to support the finding of the ALJ.

(12) RDT proposes to unitize the Cottage Grove (Peoples) Sand, Layton, Cleveland, Big Lime, Oswego, Prue, Skinner, Red Fork, Bartlesville, Simpson and Arbuckle formations. The evidence was devoid of any contribution by any formation except the Bartlesville and Prue formations. In fact there is no Simpson or Arbuckle production shown on any exhibits. The statute requires

the boundaries of the common sources of supply be defined by actual drilling operations. No such definition was presented for the Big Lime, Oswego, Red Fork, Simpson or Arbuckle formations. The evidence fails to meet the statutory burden for those formations.

(13) Carnes requests that the Oklahoma Corporation Commission reverse the recommendations of the ALJ and deny the Application of RDT for a unitization enhanced recovery unit described as the Cleveland Field Unit.

THE ALJ FOUND:

(1) The ALJ recommended that the RDT application should be granted with RDT named as operator of the Cleveland Field Unit and that the plan of unitization should be adopted.

(2) RDT presented evidence and testimony regarding extensive studies and tests that have been conducted in the proposed unit area all of which indicate that the unitization plan set forth in the subject application will ultimately increase production and benefit the owners involved. The statutory majorities of approval from the working interest owners and the royalty interest owners have been met/exceeded as to the unitization plan. RDT has expended considerable time and money to determine the extent of reserves remaining in the subject formations underlying the proposed unit area as well as the structural characteristics and areas that will be affected by waterflooding these zones. While the potential of faulting that may result in some separation of the Carnes tracts was indicated using cross-sections and by highlighting some of the RDT exhibit maps, the geological evidence presented by the protestants did not convince the ALJ that the proposed unit operations would be precluded (by the referenced faulting potential) from affecting the Carnes properties. Therefore, the Carnes tracts should not be deleted from the proposed unit area as it appears that the tracts will be affected and should participate as one of the contributing properties. Thus, the ALJ finds that the RDT evidence met the statutory and Commission requirements for unitization as to the proposed area.

(3) There was a large discrepancy in the remaining primary reserve figures (specifically for the Carnes fee tract) presented by the parties. It appears that this discrepancy can be directly attributed, at least in part, to Carnes' failure to timely report to RDT the production, productive zones, injection and disposal rates, etc. from the Carnes-operated tracts. RDT was then required to use public records in order to assign tract participation factors to the Carnes properties. While the tracts in question have been under Carnes' control for many years, the historical production figures of 14 to 15 BOPD were not contested. It is only the July production figures of 22 to 25 BOPD that are in direct contrast to the 14 to 15 BOPD. The significant increase in production

was only referred to at the hearing as being due to some type of maintenance work performed on the wells. However, this current production is the primary basis for the assertion that the RDT tract participation factor as well as the RDT calculation of remaining primary reserves are both inaccurate. As nothing more was presented to substantiate this increase in production, the ALJ is not persuaded to conclude that Carnes' fee property has 134,000 BO of primary reserves left to recover before secondary recovery should be implemented.

(4) Carnes' concerns over their cost of participating in the proposed unit are understandable. The \$1.7 million proportionate share denoted as Carnes' cost of participating is a large amount of money. However, the amount will not be due all at once. Further, no contacts had been made by Carnes as to financing the cost. The increase in production that will occur should result in a benefit that will relieve at least some of the burden of payment in a unitized area that will continue to consistently produce reserves for quite a long time to come. This benefit should outweigh the lower production that has historically been received from Carnes' tracts while still allowing Carnes' disposal well to continue operations.

(5) Thus, in light of the aforementioned conclusions, it is the recommendation of the ALJ that the application of RDT in CD 201100906-T be granted. Any order issuing out of this cause should contain the recommendations set forth above.

POSITIONS OF THE PARTIES

CARNES

1) **William H. Huffman**, attorney, appearing on behalf of Carnes stated that the center portion of this proposed unit has already been unitized and waterflooded. In 1954 Order No. 28979 established the waterflood unit encompassing large portions of Sections 19 and 20, with a second waterflood unit encompassing portions of Section 18 and 19, see Order No. 39531.

2) In 1988 RDT set up an enhanced recovery unit for these same common sources of supply by Order No. 328676. That Order indicated that there were approximately 750,000 barrels of recoverable reserves underlying that proposed unit. Mr. Jones for RDT testified that it has produced 928,000 barrels of oil. Mr. Kvach, engineer for Carnes, indicated that the center of this proposed unit is depleted.

3) Mr. Olmstead, president of RDT, indicated in a letter to Carnes, Exhibit #28, that over the last couple of years the field-wide oil cut has dropped to the

1% area. Carnes indicates that this is well beyond secondary recovery and into tertiary recovery.

4) Carnes takes issue with the \$4 million of prior costs RDT wants to assess to the owners of this particular unit. Those \$4 million in costs were expenditures that were made in the secondary enhanced recovery unit that was authorized by Order No. 328676, and were listed as pre-unit development costs. RDT stated that those wells are going to benefit the unit but Carnes takes the position that every well benefits the unit, and if RDT requires owners to pay for the drilling and development of those particular wells, it ought to be field-wide. Carnes should be able to get back 100% of the costs that they incurred for drilling their wells, not the fair market value under the plan of unitization. The plan of unitization does not provide for any type of pre-unit development costs to be incurred. Carnes argues that in order to pull those particular costs in, the Plan of Unitization would have to be a retroactive order, and case law makes it clear that cannot be done.

5) 52 O.S. §287.4 states that only so much of a common source of supply as has been defined and determined to be productive of oil and gas by actual drilling operations may be included within the unit. RDT has essentially asked for every formation to be included in this Plan of Unitization. The geologist for RDT testified that the Arbuckle is going to be a water supply formation, and when questioned he could only identify one well out of 1,760 acres that had produced some oil from the Arbuckle. Neither the Prue, the Lower Skinner or the Cottage Grove formations underlie all of the unit. The Simpson, Red Fork, Oswego and Big Lime formations are not even mapped. RDT has not really defined any of the formations that encompass the entire unit except for the Bartlesville and the Cleveland. The other formations, some of which RDT indicated have produced, by their own maps show that these particular formations are very localized and do not encompass the entire unit.

6) In the Pink Lime Structure Map, Exhibit #8, there was a fault which Bob Von Rhee, geologist for Carnes, discussed putting in there because there was an abrupt dip change calculated at .177, end .185. Mr. Von Rhee pointed out that in Tract #5 there is a big plunge, which is on the west side of the Carnes' property, and that there is an abrupt structural change. In the wells that are on both sides of that structural change there is a dip ratio of .18. This is significant because while the area has been waterflooded, Carnes property was always excluded from the water flood down to the south, possibly because there was a fault that runs through that separates the Carnes property from the bulk of this particular unit. RDT's contention was that a tracer survey appears to show that water moves from the southwest to the northeast and they think it shows there's a flow going to the Carnes property. However, upon cross-examination of Mr. Jones of specific wells, it turns out that a lot of those wells are not even open in the zone that they injected the tracer in.

7) This area was first developed in 1905, and since modern plugging techniques did not go into effect until 30 years ago, problems with break-outs, or cross-flows could be a major concern when putting together a big waterflood unit like this.

8) RDT's Plan of Unitization for the Carnes property would be to only take over certain wells, and require Carnes to plug the rest of the wells.

9) Carnes argues that the tract participation factor should take into account the reservoir, porosity, and remaining reserves, and that this tract participation does not take any of it into account. Mr. Jones, engineer for RDT, testified that the bulk of the remaining primary reserves are in the north central, the northeast, and the east portion of the proposed unit, and the Carnes property is in the northeast.

10) Wells were one of the major contributing portions of the tract participation factor, and RDT admitted they planned on using six wells on the Carnes tract, but when they did the tract participation for Carnes they only listed three wells. Tract #6 is the Carnes' tract, and they have a 4.410406 share, but their production from four wells is 330 barrels of oil per month while Tract #16 only produces 300 barrels per month from 11 wells, yet it gets a 6.683684% of the production. The engineer for Carnes testified that the Carnes Tract is getting somewhere in the neighborhood of 130 barrels of fluid and out of that it produces around 20 barrels of oil a day. This ratio of approximately 15% oil cut indicates that there are still good primary reserves left.

11) The engineer for Carnes testified that he believes that there are 134,171 barrels of remaining reserves on the Carnes property, while RDT estimates that there are 56,241 barrels of remaining reserves. Even taking the lesser number of 56,241 barrels, at \$90.00 a barrel, that is \$5 million worth of oil. RDT wants to make Carnes pay almost \$1.7 million in order to get a share of what they have already discovered and what is already available to produce.

12) Tract #16 on Exhibit 10 has no oil under it, yet it gets fifty percent more production than the Carnes Tract which has a 30-foot thick oil column under it.

13) Carnes takes the position that RDT's Application should be denied or that it should be remanded with the requirement that RDT utilize the statutory parameters and do a Tract Participation Factor based on that.

RDT

- 1) **Ron M. Barnes**, attorney, appearing on behalf of RDT, takes the position that the main question at issue is which experts to believe, and that the Judge who heard the testimony made the determination that RDT had conducted extensive studies and tests which indicate a unitization plan will ultimately increase production and benefit all of the other owners.
- 2) RDT has the necessary approval of both the mineral owners and the working interest owners and the consent portion of the statutory requirements have been met.
- 3) The ALJ was not convinced by Carnes' claims that the leases are fault separated from the remainder of the unit. The expert witnesses for Carnes agreed that they had not spent very much time on the evidence, and there are no geological or other exhibits besides a cross-section and a few simple exhibits. The experts that testified for RDT have been working this particular area for years.
- 4) RDT takes the position that their evidence met statutory and commission requirements, while Carnes did not timely report production information to RDT. After repeated efforts, RDT had to rely on information that was reported by Carnes to the State. The ALJ noted that in the month of July, Carnes was claiming an increase over historical production, but the ALJ was not persuaded that the Carnes' leases produced 134,000 barrels. Witness for Carnes admitted that the most production that the leases producing in the first 20-25 years would be closer to 78,000 barrels, not 134,000 barrels.
- 5) RDT states that the gross increase in production to all parties of the entire area is 2,203,718 additional barrels, not including the Cleveland. If the Cleveland was included, it would be approximately another two million.
- 6) With regards to the \$4 million that has been invested in this particular area in anticipation of this secondary recovery, that was to install pilot waterflood in the Cleveland; install a pilot waterflood in the Prue; drill several development wells which have increased production; build a water supply well which allows increase in production; recomplete a number of wells in the Layton and the Cottage Grove Sands; all done in anticipation of this particular waterflood, which is why the costs have been included.
- 7) RDT states that the plan has been approved by 87% of the working interest Owners and 68% of the mineral owners. Allocation is based on the thickness and quality of the reservoir, and the amount of production. If it produces 30 barrels a day, it will get the benefit of a 30-barrel a day reservoir, which is one of the factors which equates to quality of reservoir.

8) The engineer for Carnes testified that Tract #7, which is Carnes' lease, exhibits an oil cut of 1%. The engineer earlier stated that the 1% cut on the RDT operated leases indicate a very mature waterflood. RDT takes the position that the water would not get there if it did not migrate from where it is being flooded, if there is a fault there. There were not exhibits presented and not enough evidence to justify the claims that there is a fault there. There is the same kind of watercut and there is no disposal or waterflooding occurring theoretically on Carnes' lease because the disposal well they have disposes into the Arbuckle, which would not be flooding the other zone that shows the 1% oil cut.

9) The statute does not state that the operator or any working interest owner has to provide for a loan to a working interest owner. The statute has a provision that if they do not pay, there is a 300% non-consent, and this appears in RDT's plan of unitization which was approved by all of the parties that were indicated and whose names and percentages appear on their actual consent forms.

10) As far as production in this area, and wells that have produced, Exhibit 1 shows various wells which the ALJ found met the criteria for established production.

11) RDT states that the issues are not questions of law but rather questions of whom the ALJ believed and which expert witness was most reliable. RDT takes the position that based on the exhibits and testimony that was presented, and the experience and effort that went into this case, that RDT was obviously the expert in the area. Based on this, the ALJ's opinion was well-reasoned, based on substantial evidence, and should be upheld.

RESPONSE OF CARNES

1) Carnes states that Mr. Jones testified that plugging liability is going to be somewhere between \$40,000 to \$100,000 to plug the four wells remaining on the Carnes property, but Mr. Jones does not have any answer as to whose responsibility that is going to be. Therefore there does not appear to be a plan of unitization which provides for whose responsibility it will be to plug those particular wells.

2) Carnes argues that just because there is a small land owner or mineral owner with limited resources who cannot hire an army of experts to do extensive studies is not a reason to automatically lose a case.

3) Carnes states that based on the calculations in RDT's own exhibits, the disparity of the impact of the tract participation factors is obvious between what the RDT tracts are going to be receiving versus what the Carnes are going to be receiving.

4) Carnes would be responsible immediately to pay RDT \$263,000 in order to continue receiving the oil from their oil and gas wells that they are receiving today.

5) Regarding the pilot flood, it was discussed by Mr. Jones to inject the water into the producing well. That producing well has been recovering the oil, RDT has been selling the oil, and they have been taking the benefit of that particular oil and have received the benefits of that pilot program, and every other pilot program that RDT has done, but RDT did not make any provision at all for Carnes to get the benefit that they have been receiving all this time.

6) Carnes takes the position that the tract allocation factors are unfair, inequitable, and do not comply with statute, because if they did, each tract would get their fair share of the remaining recoverable reserves that are underlying each tract.

CONCLUSIONS

It is the recommendation of the Appellate Referee that the Report of the Administrative Law Judge should be affirmed in part and reversed in part.

I.

FAULT SEPARATION OF THE CARNES PROPERTY

1) The Referee concludes that the findings of the ALJ concerning the issue of fault separation of the Carnes property is supported by the weight of the evidence, free of reversible error and in accordance with law, hence, should be affirmed.

2) The ALJ is the initial finder of fact and it is the ALJ's duty as the finder of fact to observe the demeanor of the witnesses, assess their credibility, and assign the appropriate weight to their opinions. *Grison Oil Corp. v. Corporation Commission*, 99 P.2d 134 (Okla. 1940).

3) The ALJ had a battle of the experts presented before her and has written a well-reasoned report based upon the technical evidence presented before her

concerning this fault issue and in accordance with the law. The Referee can find no reason to vary that determination.

4) It is clear that the Commission must follow the procedures set forth in *Haymaker v. Oklahoma Corporation Commission*, 731 P.2d 1008 (Ok1.App. 1986) wherein the Court stated:

...Proper appraisal of the expert testimony requires observance of the following benchmark principle approved in *Downs v. Longfellow Corp.*, 351 P.2d 999 (Okl. 1960):

"The reasons given in support of the opinions [of an expert witness] rather than the abstract opinions are of importance, and the opinion is of no greater value than the reasons given in its support. If no rational basis for the opinion appears, or if the facts from which the opinion was derived do not justify it, the opinion is of no probative force, and it does not constitute evidence sufficient to...sustain a finding or verdict."

5) In regard to the weight to be given opinion evidence, the Supreme Court stated in *Palmer Oil Corporation v. Phillips Petroleum Company*, 231 P.2d 997 (Okla. 1951):

At the hearing herein the testimony adduced was chiefly that of petroleum engineers and geologists who testified on the basis of both personal surveys made and of an interpretation of the accumulated data in the hands of the Commission. The testimony of these experts was in direct conflict but that of each was positive upon the issue. Under the circumstances the objection is necessarily addressed to only the weight of the evidence. Under the holding of this Court and that of courts generally, *Chicago, R.I. and P. Ry. Co. v. Pruitt*, 67 Okl. 219, 170 P. 1143; 22 C.J. 728, Section 823, 32 C.J.S., Evidence, § 567, p. 378, the weight to be given opinion evidence is, within the bounds of reason, entirely for the determination of the jury or of the court, when trying an issue of fact, it taking into consideration the intelligence and experience of the

witness and the degree of attention he gave to the matter. The rule should have peculiar force herein where by the terms of the Act the Commission is recognized as having peculiar power in weighing the evidence. Since the evidence before the Commission was competent and sufficient if believed, to sustain the order we must, and do, hold that the order is sustained by the evidence and that the contention is without merit. *Ft. Smith & W. Ry Co. v. State*, 25 Okl. 866, 108 P. 407; *Bromide Crushed Rock Company v. Dolese Brothers Company*, 121 Okl. 40, 247 P. 74.

6) The ALJ found that:

While the potential of faulting that may result in some separation of the Carnes tracts was indicated using cross-sections and by highlighting some of the RDT exhibit maps, the geological evidence presented by the protestants did not convince the ALJ that the proposed unit operations would be precluded (by the referenced faulting potential) from affecting the Carnes properties. Therefore, the Carnes tracts should not be deleted from the proposal unit area as it appears that the tracts will be affected and should participate as one of the contributing properties. Thus, the ALJ finds that the RDT evidence met the statutory and Commission requirements for the unitization as to the proposed area.

7) The Referee can find no reason to vary the determination of the ALJ and having reviewed the transcripts and the documents in the present case would adopt the conclusions of the ALJ concerning the issue of fault separation of the Carnes property.

II.

INCLUSION OF ALL THE COMMON SOURCES OF SUPPLY REQUESTED BY RDT

1) The Referee finds that the ALJ's determination that the Cottage Grove (Peoples), Layton, Cleveland, Big Lime, Oswego, Prue, Skinner, Red Fork, Bartlesville, Simpson and Arbuckle common sources of supply should be

included within the proposed unit is also supported by the weight of the evidence and in accordance with law, and should thus be affirmed.

2) 52 O.S. Section 287.4 provides in part:

Each unit and unit area shall be limited to all or a portion of a single common source of supply. Only so much of a common source of supply as has been defined and determined to be productive of oil and gas by actual drilling operations may be so included within the unit area.

3) Carnes alleged that there was no evidence presented as to actual drilling operations for the Big Lime, Oswego, Red Fork, Simpson or Arbuckle formations. Carnes alleged that the evidence was devoid of any contribution by any formation except the Bartlesville and Prue formations. Having reviewed the exhibits presented by RDT and the testimony presented by RDT there are Red Fork wells; the Airport #4-A and #2-A; Arbuckle wells, the LM Jones #46 and #54; Big Lime wells, the Mullendore and Berry #33 and #34; Oswego wells, the LM Jones 52 and 53; and the Simpson produces in the Miller #29 (see Exhibits 1 and 13).

4) If these formations are not included in the unit plan then they would not be able to be produced and thus would constitute waste.

5) On review, based upon the evidence, the Referee can find no reason to vary the ALJ's determination that the common sources of supply have been defined or determined by actual drilling operations. The ALJ found:

Additionally, all of the named zones have already been established as productive intervals within the unit boundaries. While the majority of the reserves will be from the largest zones, those being the Cleveland and Bartlesville formations, the rest of the named zones will also be contributors.

III.

RDT'S METHOD TO ALLOCATE UNIT PRODUCTION

(1) 52 O.S. 287.4 provides in relevant part:

The plan of unitization for each such unit and unit area shall be one suited to the needs and requirements of the particular unit dependent upon the facts and conditions found to exist with respect thereto. In addition to such other terms, provisions, conditions and requirements found by the Commission to be reasonably necessary or proper to effectuate or accomplish the purpose of this act, and subject to the further requirements hereof, each such plan of unitization shall contain fair, reasonable and equitable provisions for:

* * *

(b) The division of interest or formula for the apportionment and allocation of the unit production, among and to the several separately owned tracts within the unit area such as will reasonably permit persons otherwise entitled to share in or benefit by the production from such separately owned tracts to produce or receive, in lieu thereof, their fair, equitable and reasonable share of the unit production or other benefits thereof. **A separately owned tract's fair, equitable and reasonable share of the unit production shall be measured by the value of each such tract for oil and gas purposes and its contributing value to the unit in relation to like values of other tracts in the unit, taking into account acreage, the quantity of oil and gas recoverable therefrom, location on structure, its probable productivity of oil and gas in the absence of unit operations, the burden of operation to which the tract will or is likely to be subjected, or so many of said factors, or such other pertinent engineering, geological, or operating factors, as may be reasonably susceptible of determination.** Unit production as that term is used in this act shall mean and

include all oil and gas produced from a unit area from and after the effective date of the order of the Commission creating the unit regardless of the well or tract within the unit area from which the same is produced. (Emphasis added)

2) Professor Meyers stated in Meyers, The Law of Pooling and Unitization, Voluntary-Compulsory, Chapter X (1957):

The formula is the heart of the unitization agreement. It is usually the most difficult problem to solve, but unitization is impossible until it is agreed upon by the operator. The formula determines the portion of the unitized substance each participant is to receive, and is usually arrived at only after long and laborious negotiation. The idea is that each operator's share of production from the unit shall be in exact proportion to the contribution which he makes to the unit.

3) What is important is that the formula allocates to each tract its fair, equitable and reasonable share of unit production. See *Jones Oil Company v. Corporation Commission*, 382 P.2d 751 (Okl. 1963). *Eason Oil Company v. Corporation Commission*, 535 P.2d 283 (Okl. 1975) stated:

The plan of unitization must contain fair, reasonable and equitable provisions for the apportionment and allocation of the unit production among the separately-owned tracts. A separately-owned tract's share of the unit production must be measured by the value it contributes to the total value of the unit for oil and gas purposes. Each tract must be measured by the same set of values as must the unit as a whole. In the construction of statutes, the word "shall" is usually given its common meaning of "must" and interpreted as implying a command or mandate depending upon the construction of the statute as a whole and the intention of the Legislature. *Oklahoma Alcoholic Beverage Control Board v. Moss*, Okl. 509 P.2d 666 (1973).

4) The guidelines of 52 O.S. Section 287.4(b) include a consideration of the acreage of a tract, the quantity of oil and gas recoverable therefrom, its location on structure, its probable productivity of oil and gas in the absence of unit

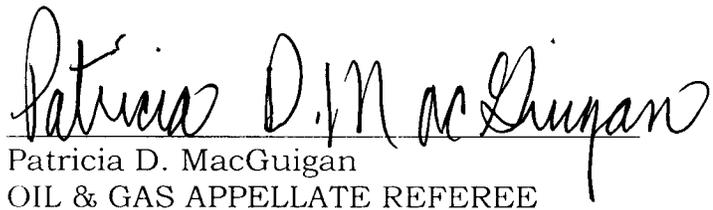
operations, and the burden of operation to which the tract well is likely to be subjected. The overriding consideration is: "...the value of each tract for oil and gas purposes and its contributing value to the unit in relation to like values of other tracts in the unit."

5) The Referee finds that RDT's formula does not satisfy the guidelines set forth in Section 287.4(b) and does not measure each separately owned tract's share of unit production by the value it contributes to the total value of the unit for oil and gas purposes. The tract participation factor proposed by RDT is not equitable because they did not use a tract participation formula which focuses on the ratio of remaining primary reserves underlying the Carnes tracts and the RDT tracts. The most theoretically accurate formula is one that gives the greatest weight to recoverable remaining saturated hydrocarbon pore volume utilizing more concrete factors in the formula. See the article by Bryan J. Standley and Scott B. Cline, *Participation Formula in Waterflood Units: What are the Statutory and Judicial Guidelines?*, 66 Okl.B.J. 3373, October 28, 1995.

6) The RDT tract participation factor did not use any remaining reserves. They didn't use porosity and they didn't assign the Carnes tract any remaining reserves. Carnes estimated that there were 134,171 barrels remaining reserves on the Carnes property while the RDT expert stated that there was an estimate of 56,241 barrels remaining reserves. There was no accommodation to the Carnes for any oil remaining.

7) For the above stated reasons the Referee would recommend that a formula must be used which most closely satisfies the guidelines set forth in Section 287.4(b) which measures each separately owned tract's share of unit production by the value it contributes to the total value of the unit for oil and gas purposes. Thus, the Referee would reverse the recommendation of the ALJ concerning the allocation formula and remand to the ALJ with the requirement that the parameters under Section 287.4(b) be used. The allocation factor should not be based solely on surface acreage, number of wells and current production but it should be determined by the quantity of oil and gas recoverable from the Carnes tracts and the Carnes share of unit production should be the value it contributes to the total value of the unit for oil and gas purposes. They should allocate remaining reserves to all of the tracts included in the unit and compile a tract participation factor on those figures.

RESPECTFULLY SUBMITTED THIS 16th day of November, 2011.


 Patricia D. MacGuigan
 OIL & GAS APPELLATE REFEREE

PM:ac

xc: Commissioner Murphy
Commissioner Anthony
Commissioner Douglas
Jim Hamilton
ALJ Kathleen M. McKeown
Ron M. Barnes
William H. Huffman
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Office of General Counsel
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