

RULE 37 EXCEPTIONS AND SMALL MINERAL TRACTS IN URBAN AREAS: AN ARGUMENT FOR INCORPORATING COMPULSORY POOLING INTO SPECIAL FIELD RULES IN TEXAS

Comment

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I. THE INSIGHTS OF LARRY LANDOWNER—A HYPOTHETICAL
ILLUSTRATION AND INTRODUCTION

Larry Landowner lives with his family in a brand new Fort Worth subdivision.¹ Larry owns both the surface and the minerals beneath his 0.33-acre residential tract. Portions of the Barnett Shale—an underground geologic formation containing natural gas—underlie Larry's neighborhood. Oil and gas production companies have flocked to the area in an effort to extract and sell natural gas from the formation. Larry, because he owns the minerals beneath his tract, is generally entitled to receive money—royalty payments—as compensation for the minerals extracted from beneath his land.² To receive those payments, however, Larry must enter into an oil and gas lease with an oil and gas production company (a producer). Larry has not entered into any lease agreements with a producer, but he has heard that several surrounding landowners leased their mineral rights to an oil and gas production company called Exxell Oil Company (Exxell).

Exxell owns mineral leases to several properties adjacent to Larry's residential tract, but unfortunately for Larry, Exxell has not executed an oil and gas lease with him. Exxell analyzed the size and shape of the leased surface acreage it acquired in the area and the subsurface geologic characteristics of the underlying portions of the Barnett Shale. Based on that analysis, it determined that in order to extract the maximum amount of natural gas possible, it should drill a horizontal well within 330 feet of Larry's residential tract. The Railroad Commission of Texas (RRC) promulgates oil and gas well-spacing regulations in Texas.³ It has adopted both statewide well-spacing regulations and specialized regulations for certain oil and gas fields (special field rules).⁴ According to the special field rules for the Barnett Shale, producers like Exxell are not permitted to drill horizontal wells within 330 feet of unleased property like Larry's.⁵ Under Texas law, if Exxell wishes to drill a horizontal well and

1. This hypothetical example is fictional and was developed by analyzing and combining factual scenarios presented to the Railroad Commission of Texas (RRC) in published recommendations for Rule 37 applications. Many of these recommendations are available at <http://www.rrc.state.tx.us/meetings/ogpfd/ogpor37/r37indx.php>.

2. See PATRICK H. MARTIN & BRUCE M. KRAMER, WILLIAMS & MEYERS MANUAL OF OIL AND GAS TERMS 855 (14th ed. 2009) [hereinafter MARTIN & KRAMER, MANUAL] (defining "royalty").

3. See *infra* Part II.A.

4. See *infra* notes 75-80 and accompanying text.

5. See *infra* notes 75-80 and accompanying text.

extract natural gas from within 330 feet of Larry Landowner's residential tract, it must attempt to lease Larry's adjacent property, apply to the RRC for a well-spacing exception, or attempt to constructively join the leased and unleased properties together through a process known as pooling.⁶

Texas's existing framework encourages producers to engage adjacent, unleased mineral owners directly and attempt to enter into lease agreements.⁷ If, however, the unleased mineral owners are not willing to lease or are unavailable, Texas's approach varies significantly from the approach taken in most other oil producing states.⁸ Most states allow regulatory agencies to constructively force two or more adjacent tracts to join together for oil and gas production purposes.⁹ This process is known as compulsory, or forced, pooling.¹⁰ The framework currently employed in Texas, on the other hand, encourages producers to apply for well-spacing exceptions from the RRC—Rule 37 exceptions—rather than pursue pooling options.¹¹ This policy creates significant issues for both unleased, small-tract mineral owners and producers in urban oil and gas fields.¹²

The existing methods by which Texas deals with unleased tracts in urban oil and gas fields leave unleased, small-tract mineral owners out in the cold.¹³ When producers obtain Rule 37 exceptions, they obtain the right to violate well-spacing regulations implemented to protect the property rights of all mineral owners over a common source of supply.¹⁴ Therefore, when producers drill horizontal wells within areas normally designated as off-limits by the applicable spacing rules, the wells can potentially capture hydrocarbons from beneath the adjacent, unleased property, and the neighboring mineral owner will receive no compensation for those minerals.¹⁵ Because neighboring, unleased mineral owners are not entitled to receive royalty payments for minerals drained from beneath their tracts, their correlative rights as mineral owners are not adequately protected.¹⁶ This issue is exacerbated by the fact that the RRC is granting Rule 37 exceptions at an unprecedented rate—granting an annual average of 582 exceptions statewide from 1919 through 2005 but granting an annual statewide average of 3,916 exceptions from 2006 through 2011.¹⁷ Although it seems producers receive a windfall under the Rule 37

6. *See infra* discussion Part II.D-F.

7. *See infra* Part II.F.

8. *See infra* Part II.F.

9. *See infra* Parts II.E, IV.A.

10. *See infra* Part II.E.

11. *See infra* Part II.D, F.

12. *See infra* Part III.B-C.

13. *See infra* Part III.B.

14. *See infra* Part II.B.

15. *See infra* Part II.B; MARTIN & KRAMER, MANUAL, *supra* note 2, at 261 (defining "drainage").

16. *See infra* Part II.B, E.

17. *See infra* notes 128-35 and accompanying text.

dominated system, producers do not benefit greatly from the existing framework either.¹⁸

Urban producers are not afforded the flexibility necessary to efficiently plan hydrocarbon development and extraction from urban oil and gas fields.¹⁹ Rule 37 exceptions, while granted more frequently than ever, can still be unpredictable due to the nature of the tests used by the RRC in analyzing Rule 37 applications.²⁰ Compulsory pooling would provide a more predictable tool for producers to use in planning urban oil and gas operations and would allow producers to maximize hydrocarbon production from urban fields.²¹ Unfortunately, Texas's current compulsory pooling statute contains inherent limitations, and its language has traditionally been interpreted narrowly, which fails to protect correlative rights generally or allow producers flexibility in development.²²

This Comment explores the interplay between Rule 37 exceptions and Texas's existing compulsory pooling statute and demonstrates the need for some form of compulsory pooling in urban oil and gas fields. Part II provides historical context and an overview of some of the relevant oil and gas law concepts implicated by the presence of unleased, small-tract mineral owners on urban oil and gas development. Part III extends the Larry Landowner hypothetical, framing the issues using the concepts discussed in Part II. Part IV evaluates three different forms of compulsory pooling provisions that could potentially provide better protection for unleased mineral owners and afford urban producers greater flexibility in urban development. Finally, Part V encourages the RRC to incorporate broad compulsory pooling provisions into special field rules in Texas because doing so strikes a balance between drastically altering traditional statewide policy and continuing to operate under the existing compulsory statute that was drafted to serve a different purpose.

II. A SUMMARY OF THE OIL AND GAS LAW PRINCIPLES LARRY LANDOWNER NEEDS TO KNOW

A. *The Railroad Commission of Texas—What Is It, and What Is Its Jurisdiction?*

The Texas oil and gas industry began in earnest on January 10, 1901, when Captain Anthony F. Lucas struck oil at Spindletop, near Beaumont, Texas.²³ The Spindletop discovery ignited Texas's rapid ascension as a

18. See *infra* Part III.C.

19. See *infra* Part III.C.

20. See *infra* Part II.D.

21. See *infra* Part II.E.2.

22. See *infra* Part II.F.

23. See *Oil and Texas: A Cultural History*, in TEXAS ALMANAC, 2000-2001, at 29 (Mary G. Ramos ed., 1999), available at <http://www.texasalmanac.com/topics/business/oil-and-texas-cultural-history>.

worldwide leader in petroleum production and as an industrial power.²⁴ Once word of Lucas's discovery at Spindletop spread, the Spindletop "boom turned into a feeding frenzy of human sharks: scores of speculators sniffing out a quick buck; scam artists peddling worthless leases; and prostitutes, gamblers and liquor dealers, all looking for a chunk of the [oilfield] workers' paychecks."²⁵ Over the next several years, the Texas oil craze spread from southeast Texas to literally every corner of the state.²⁶ Texas oilfield discoveries allowed previously nonexistent towns to flourish, small companies to grow into multinational conglomerates, and average people to amass boundless personal fortunes.²⁷

Today, the RRC is the administrative body that oversees the Texas oil and natural gas industry.²⁸ Started in 1891, the RRC was originally tasked with "administer[ing] the state's railroad laws; determin[ing] passenger fares, freight rates, and charges; hold[ing] public hearings; and receiv[ing] reports, mak[ing] investigations, and keep[ing] records on the financial aspects of trains, terminals, and other traffic services."²⁹ As a result of the Texas oil boom that started at Spindletop, oil producers needed a way to transport oil from wells to refineries.³⁰ Railroads provided the perfect transportation mechanism.³¹ Unsurprisingly the Texas oil and railroad industries became entwined, and over time the Texas Legislature granted the RRC additional regulatory authority in the oil and gas industry.³² Such authority was necessary due to the rapid expansion of the oil and gas industry in Texas and the "feeding frenzy of human sharks" that followed.³³ While the RRC no longer retains any of its original railroad responsibilities, the name remains unchanged.³⁴ Today, the RRC "has jurisdiction over the oil and natural gas industry, pipeline transporters, the natural gas and hazardous liquid pipeline industry, natural gas utilities, the LP-gas industry, alternative fuels, coal surface mining, and uranium exploration operations along with environmental and safety responsibilities related to oil and gas production."³⁵ Essentially all oil and gas matters in the State of Texas must comply with regulations promulgated by the RRC.³⁶

24. *See id.* at 31.

25. *Id.*

26. *See id.*

27. *Id.* at 29.

28. *See, e.g., Who Regulates Railroads in Texas?*, R.R. COMM'N OF TEX., <http://www.rrc.state.tx.us/about/railroads/index.php> (last visited May 22, 2012).

29. *Id.*

30. *See Oil and Texas: A Cultural History*, *supra* note 23.

31. *See id.*

32. *See Who Regulates Railroads in Texas?*, *supra* note 28.

33. *See Oil and Texas: A Cultural History*, *supra* note 23; *Who Regulates Railroads in Texas?*, *supra* note 28.

34. *Who Regulates Railroads in Texas?*, *supra* note 28.

35. *Id.*

36. *Id.*

The RRC is capable of retaining regulatory authority over the oil and gas industry because the Texas Legislature conferred executive, legislative, and judicial powers within the scope of the agency's delegated authority when it created the RRC.³⁷ Primary jurisdiction over disputes that arise within the RRC's delegated authority lies with the RRC.³⁸ As a result, parties with disputes that fall within the RRC's realm of authority must exhaust all administrative remedies before appealing to the Texas court system.³⁹ The RRC is specifically tasked with: (1) instituting suits; (2) hearing and determining complaints; (3) requiring the attendance of witnesses and paying their expenses out of funds provided for that purpose; and (4) punishing for contempt or disobedience of its orders in the manner provided for district courts.⁴⁰ Basically any issues relating to oil and gas matters in Texas fall within the RRC's jurisdiction, and the RRC has authority to regulate and adjudicate those matters.⁴¹ One area in which the RRC exerts substantial control over oil and gas production is in setting minimum well-spacing requirements.⁴²

B. Well Spacing in General

Well-spacing regulations are implemented by the RRC in an effort to protect the correlative rights of mineral owners as a result of the common law rule of capture.⁴³ The rule of capture governs oil and gas production in Texas, and it states: "The owner of a tract of land acquires title to the oil or gas [that] he produces from wells on his land, though part of the oil or gas may have migrated from adjoining lands."⁴⁴ A mineral owner "may thus appropriate the oil and gas that have flowed from adjacent lands without the consent of the owner of those lands, and without incurring liability to him for drainage."⁴⁵ The rule of capture imposes no liability on a landowner for draining the oil and gas beneath a neighboring landowner's property.⁴⁶ While the common law rule of capture is broad in scope, it has limitations.⁴⁷ Perhaps the most influential limitation on the rule of capture is the Doctrine of Correlative Rights, which essentially guarantees that every mineral owner is entitled to have a reasonable

37. See JOHN S. LOWE ET AL., CASES AND MATERIALS ON OIL AND GAS LAW 126 (5th ed. 2008).

38. See *id.*

39. See *id.*

40. TEX. NAT. RES. CODE ANN. § 81.053 (West 2011).

41. See *id.*

42. See 16 TEX. ADMIN. CODE §§ 3.37, 3.86 (2011).

43. See R.R. Comm'n of Tex. v. Shell Oil Co., 380 S.W.2d 556, 559 (Tex. 1964). "Well spacing" is defined as "[t]he regulation of the number and location of wells over an oil and gas reservoir, as a conservation measure." MARTIN & KRAMER, MANUAL, *supra* note 2, at 1058.

44. See, e.g., Elliff v. Texon Drilling Co., 210 S.W.2d 558, 561-62 (Tex. 1948).

45. *Id.* at 562.

46. See JOSEPH SHADE, PRIMER ON THE TEXAS LAW OF OIL AND GAS 5 (4th ed. 2008).

47. See *id.* at 6 (noting that the common law limitations recognized by Texas courts include trespass, negligence, nuisance, waste, violation of rules promulgated by conservation agencies, and interfering with a neighbor's correlative rights).

opportunity to produce his fair share of the minerals in a shared oil and gas reservoir.⁴⁸ Because correlative rights play such a vital role in Texas oil and gas law, a brief summary of the doctrine's common law background is useful.

The touchstone Texas case regarding the limitation placed on the rule of capture by the Correlative Rights Doctrine is *Elliff v. Texon Drilling Co.*⁴⁹ There, Texon Drilling Company negligently allowed a vertical oil well, 446 feet from Elliff's property line, to blow out and crater.⁵⁰ A fissure in the earth developed and destroyed an oil well on Elliff's property.⁵¹ Elliff's oil well subsequently blew out, cratered, and resulted in a fire that burned for several years.⁵² The disaster lasted so long that large quantities of hydrocarbons were drained from beneath Elliff's property and burned into the atmosphere.⁵³ Two water wells also failed, considerable surface damages occurred, and Elliff lost a portion of his cattle herd.⁵⁴ Elliff sued under a negligence cause of action, and the trial court held in his favor by awarding him compensation damages for the drained hydrocarbons.⁵⁵ The appellate court reversed, holding that the rule of capture voided any property right Elliff had to the hydrocarbons when they migrated from beneath his lands, regardless of what caused the migration.⁵⁶ The Texas Supreme Court recognized that the common law rule of capture defines the absolute real property ownership rights that mineral owners in Texas enjoy; however, it also noted that each landowner has a common law right "to produce his fair share of the oil and gas" underlying his tract.⁵⁷ Accordingly, the Texas Supreme Court limited the rule of capture by adopting the Correlative Rights Doctrine and recognizing the RRC's function in implementing conservation statutes and orders.⁵⁸ The *Elliff* court also solidified the RRC's jurisdiction to regulate the Texas oil and gas industry by recognizing that regulations promulgated by the RRC exist to protect correlative rights by affording each mineral owner "a reasonable opportunity to produce his proportionate part of the oil and gas from the entire pool and to prevent operating practices injurious to the common reservoir."⁵⁹ As a result, the RRC "is vested with the power and charged with the duty of regulating the

48. See *Elliff*, 210 S.W.2d at 562.

49. See *id.* at 558.

50. See *id.* at 559. A "blow out" is customarily defined as "[a] sudden, violent expulsion of oil, gas[,] and [mud] (and sometimes water) from a drilling well, followed by an uncontrolled flow from the well. It occurs when high pressure gas is encountered in the hole and sufficient precautions . . . have not been taken." MARTIN & KRAMER, MANUAL, *supra* note 2, at 88. "Crater" is customarily defined as "[a] bowl shaped depression around a blow out well caused by the caving in and collapse of the earth's structure." *Id.* at 209.

51. See *Elliff*, 210 S.W.2d at 559.

52. See *id.*

53. See *id.*

54. See *id.*

55. See *id.* at 560.

56. See *id.*

57. *Id.* at 562.

58. See *id.*

59. *Id.*

production of oil and gas for the prevention of waste as well as for the protection of correlative rights.”⁶⁰

One way that the RRC fulfills its duties in preventing waste and protecting correlative rights is by implementing well-spacing regulations.⁶¹ As the facts in *Elliff* demonstrate, Texas’s adoption of the rule of capture as its primary oil and gas ownership doctrine created the need for well-spacing regulation.⁶² The RRC implemented its first statewide well-spacing regulation, Rule 37, on November 26, 1919.⁶³ Rule 37 was implemented because the RRC recognized that regulating the location of wells was necessary to protect the correlative rights of mineral owners.⁶⁴ While Rule 37 has been amended over time, its purpose remains the same—to prevent the waste and confiscation of property and to protect correlative rights.⁶⁵ Recent increases in the amount of horizontal wells challenged Rule 37’s ability to adequately serve those purposes because Rule 37 contemplates only vertical oil and gas wells.⁶⁶

The widespread adoption of horizontal drilling provided a new wrinkle for RRC well-spacing regulations.⁶⁷ The challenge developed because statewide well-spacing regulations were implemented with vertical wells in mind.⁶⁸ In response to the widespread adoption of horizontal drilling, the RRC implemented statewide Rule 86, which regulates the spacing of horizontal wells.⁶⁹ Statewide Rule 86 is designed to function as a supplement to Rule 37, so it is not the exclusive regulation that governs the spacing of horizontal wells.⁷⁰ It specifically stipulates that “[a]ll wells developed with horizontal drainholes shall otherwise comply with Statewide Rule 37 . . . or other applicable spacing rules.”⁷¹ The spacing regulations in Rule 37 and Rule 86 reference other applicable spacing rules that may apply in a given field.⁷² Recognizing the unique characteristics of oil and gas fields, the RRC justifies the implementation of customized spacing provisions differently from the default statewide rules.⁷³ Such customized provisions are referred to as special field rules.⁷⁴

60. R.R. Comm’n of Tex. v. Shell Oil Co., 380 S.W.2d 556, 559 (Tex. 1964).

61. See Robert E. Hardwicke, *Oil-Well Spacing Regulations and Protection of Property Rights in Texas*, 31 TEX. L. REV. 99, 101-02 (1952).

62. See Bruce M. Kramer, *Pooling for Horizontal Wells: Can They Teach an Old Dog New Tricks?*, 55 ROCKY MTN. MIN. L. INST. 8-1, 8-4 (2009); *supra* notes 49-54 and accompanying text.

63. See Hardwicke, *supra* note 61, at 101-02.

64. See *id.*

65. See 16 TEX. ADMIN. CODE § 3.37 (2011).

66. See *id.*

67. See Eric C. Camp, *Dealing With Missing Persons and Holdouts: Using Rule 37 and MIPA for Urban Gas Development*, DALLAS BAR ASS’N—ENERGY LAW SECTION 3 (Jan. 19, 2011).

68. See *id.*

69. See 16 TEX. ADMIN. CODE § 3.86 (2011).

70. § 3.86(b)(3).

71. *Id.*

72. See *id.* §§ 3.37(d), 3.86(b)(3).

73. See § 3.37(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

Special field rules modify statewide well-spacing rules to serve designated fields.⁷⁵ These customized rules allow producers to implement field-specific well-spacing requirements in order to maximize production.⁷⁶ For example, producers may apply to the RRC for special field rules when, after drilling an initial discovery well, they believe conditions are such that the default statewide well-spacing provisions will not enable producers to efficiently extract the maximum amount of hydrocarbons possible.⁷⁷ In fields that have special rules, the RRC may grant exceptions under Rule 37.⁷⁸ As of 2011, the RRC has adopted over sixty different special field rules in Texas.⁷⁹ Some fields that have adopted special rules include the Barnett Shale near Fort Worth, the Eagle Ford formation in south-central Texas, and the Haynesville formation in northeast Texas.⁸⁰

C. The Nuts and Bolts of Horizontal Drilling and Hydraulic Fracturing

Hydraulic fracturing (fracing) in horizontal wells creates a set of issues different from all other issues Texas oil and gas law has faced over the past

geothermal resource fields to enter special orders increasing or decreasing the minimum distances provided by this section.”).

74. See, e.g., Hardwicke, *supra* note 61, at 103.

75. See TEX. NAT. RES. CODE ANN. § 85.042(b) (West 2011) (stating that “[w]hen necessary, the commission shall make and enforce rules either general in their nature or applicable to particular fields for the prevention of actual waste of oil or operations in the field dangerous to life or property”); see also Camp, *supra* note 67, at 4 (noting that “[s]tatewide Rule 86 governs horizontal wells unless preempted by a special field rule”); Hardwicke, *supra* note 61, at 103 (noting that “[s]tatewide Rule 37 governs spacing, unless modified by special spacing rules for designated fields”).

76. See 1 BRUCE M. KRAMER & PATRICK H. MARTIN, *THE LAW OF POOLING AND UNITIZATION* § 8.05 (3d ed. 2011).

77. See generally 16 TEX. ADMIN. CODE § 3.43 (2011) (authorizing producers to apply to the RRC for temporary special field rules); Tex. R.R. Comm’n, *Application of Chesapeake Oil and Gas Operating, Inc. to Amend the Field Rules for the Newark, East (Barnett Shale) Field*, Docket No. 09-0253880, (Oil & Gas Div. Apr. 9, 2008) (proposal for decision), available at <http://www.rrc.state.tx.us/meetings/ogpfd/ogpofdrules/09-53880.fr1.pdf> (providing an example of a producer’s successful application to amend the Barnett Shale’s special field rules).

78. See Camp, *supra* note 67, at 4; Ben Elmore, *Texas Statewide Rule 37 Exceptions and the Mineral Interest Pooling Act*, SHALEBIZ.COM (Feb. 1, 2011, 6:00 PM), <http://www.gohaynesvilleshale.com/profiles/blogs/texas-statewide-rule-37>.

79. Camp, *supra* note 67, at 4.

80. *Field Rules for the Eagle (Eagle Ford), Field Number 27066200*, R.R. COMM’N OF TEX., <http://webapps.rrc.state.tx.us/DP/fieldSelectAction.do> (select “Matching this Number Exactly” button; type “27066200” into field and click “Search” button; select “27066200 01 EAGLE (EAGLE FORD)” and select “View Field Rules” button) (last visited May 30, 2012) [hereinafter *Eagle Ford Special Field Rules*]; *Field Rules for the Newark, East (Barnett Shale), Field Number 65280200*, R.R. COMM’N OF TEX., <http://webapps.rrc.state.tx.us/DP/fieldSelectAction.do> (select “Matching this Number Exactly” button; type “65280200” into field and click “Search” button; select “65280200 09 NEWARK, EAST (BARNETT SHALE)” and select “View Field Rules” button) (last visited May 30, 2012) [hereinafter *Barnett Shale Special Field Rules*]; *Field Rules for the Waskom (Haynesville), Field Number 95369260*, R.R. COMM’N OF TEX., <http://webapps.rrc.state.tx.us/DP/fieldSelectAction.do> (select “Mathing this Number Exactly” button; type “95369260” into field and click “Search” button; select “95369260 06 WASKOM (HAYNESVILLE)” and select “View Field Rules” button) (last visited May 30, 2012) [hereinafter *Haynesville Shale Special Field Rules*].

century.⁸¹ These new issues arise because of the amount of the producing formation that is accessible using a horizontal well bore.⁸² A producer can now traverse through a continuous, horizontal portion of a formation instead of vertically intersecting the formation at various points using vertical wells.⁸³ A horizontal well is usually drilled in three general stages: the vertical stage, the build stage, and the lateral stage.⁸⁴ During the vertical stage, a vertical well is drilled straight down into the earth as if the final result were a traditional vertical oil or gas well.⁸⁵ Once the well bore reaches the “kick-off point,” the process transitions into the build stage.⁸⁶ The kick-off point is the point at which the well transforms from a traditional vertical well into a horizontal well.⁸⁷ During the build stage, the angle of the well bore will gradually curve from vertical, at a few hundred feet above the target formation, to horizontal within the target formation.⁸⁸ Once the well bore has completed the turn from vertical to horizontal, the operation enters the lateral stage.⁸⁹

During the lateral stage, the producer will extend the horizontal well bore as far through the formation as the formation itself—and the applicable spacing regulations—will allow.⁹⁰ The producer may then perforate and frac the well bore throughout the entire productive zone.⁹¹ When used in combination with fracing, horizontal drilling allows a producer to extract far more hydrocarbons than were accessible using traditional methods.⁹² An added benefit of using fracing with horizontal drilling is that the overall surface footprint from oil and gas production is dramatically reduced—one horizontal well can produce the same amount of hydrocarbons as multiple vertical wells.⁹³ Fracing was first employed as a reservoir stimulant roughly sixty years ago, but the technique is expensive, so its use did not become prevalent until the early 2000s when high oil and gas prices made its use more economically feasible.⁹⁴

Fracing is an economically feasible reservoir stimulation technique when oil and gas prices are high.⁹⁵ Although fracing has been commercially available for some time, recent oil and gas prices have made the technique viable on a

81. See Thomas E. Kurth et al., *American Law and Jurisprudence on Fracing*, 47 ROCKY MTN. MIN. L. INST. 277, 278-79 (2010). Hydraulic fracturing is also frequently abbreviated as “fracking” and “fraccing,” although each abbreviation is pronounced as “fracking.” See *id.* at 278.

82. See *id.*

83. See *id.*

84. See Kramer, *supra* note 62, at 8-3.

85. See *id.*

86. See *id.*

87. See *id.*

88. See *id.*

89. See *id.*

90. See *id.*

91. See Kurth et al., *supra* note 81, at 282.

92. See *id.*

93. See *id.*

94. See *id.* at 279.

95. See *id.*

large commercial scale.⁹⁶ The production technique “was first tested in 1903 and first used commercially in 1948.”⁹⁷ Applicable to vertical and horizontal wells, fracking increases the amount of hydrocarbons produced from a formation by artificially increasing the formation’s porosity.⁹⁸ During the process, companies inundate a perforated well bore with fluids at a very high pressure.⁹⁹ The high pressure, in combination with “proppants” mixed into the fluid, causes the rock formation to crack—or fracture—which allows hydrocarbons to flow more freely into the well bore.¹⁰⁰ Shale formations were once constructively inaccessible for hydrocarbon production because of shale’s extremely small porosity.¹⁰¹ Now that hydraulic fracturing is used in conjunction with horizontal drilling, oil and gas production is economically feasible from shale formations.¹⁰² In addition, hydraulic fracturing and horizontal drilling can reinvigorate old oil and gas wells that were considered dry or in decline.¹⁰³ Because the conjoined use of horizontal drilling and hydraulic fracturing is a relatively new technique, mineral owners, producers, and the RRC must cope with RRC regulations originally crafted for vertical wells.¹⁰⁴ One area that is receiving increased attention involves exceptions to statewide and special field well-spacing requirements.¹⁰⁵

D. Statewide Rule 37 Exceptions

Issues arise, especially in urban areas, when small-tract mineral owners are either unavailable or simply refuse to sign an oil and gas lease.¹⁰⁶ The small-tract mineral owners may want to holdout for a better deal later or may simply be unreachable.¹⁰⁷ In those situations, small-tract mineral owners, by their unavailability or unwillingness to enter into an oil and gas lease, can substantially delay multi-million dollar oil and gas operations.¹⁰⁸ As a result,

96. *See id.*

97. *Id.*

98. *See id.* at 278. Porosity is a measure of the amount of air space available inside of a rock formation in which hydrocarbons and water exist. *See* MARTIN & KRAMER, MANUAL, *supra* note 2, at 729.

99. *See* Kurth et al., *supra* note 81, at 278. “Perforation” is defined as “[t]he making of holes in casing and cement (if present) to allow formation fluids to enter the well bore. One common method of perforating is by shooting pellets through the casing by means of a special gun lowered into the hole.” MARTIN & KRAMER, MANUAL, *supra* note 2, at 699.

100. *See* Kurth et al., *supra* note 81, at 278-79. A “proppant” is “typically sand, ceramic pellets[,] or other small granular material that is carried into the fractures where it remains to prop the crack open thereby allowing the oil or gas to flow.” *Id.* at 279.

101. *See id.* at 278.

102. *See id.*

103. *See id.*

104. *See* Camp, *supra* note 67, at 3.

105. *See id.*

106. *See id.* at 5.

107. *See generally id.* at 23 (noting that Rule 37 exceptions and the Mineral Interest Pooling Act (MIPA) are two different methods of dealing with missing persons and holdouts).

108. *See generally id.* at 35 (discussing the various reasons why producers pursue Rule 37 exceptions).

oil and gas producers must take action in order to avoid losing oil and gas leases and to continue development and production.¹⁰⁹

One avenue through which producers may deal with a missing mineral owner or holdout is to obtain a statewide Rule 37 spacing exception from the RRC.¹¹⁰ Exceptions may be granted if the applicant demonstrates that the exception “is necessary either to prevent waste or to prevent the confiscation of property.”¹¹¹ To obtain a statewide Rule 37 well-spacing exception in order to prevent waste, an applicant must prove that unusual or exceptional circumstances exist such that a spacing exception is necessary to recover hydrocarbons and that the desired exception will allow the recovery of otherwise unrecoverable oil and gas.¹¹²

For a producer to prove that a Rule 37 exception is necessary in order to prevent confiscation, it must show the following: (1) the applicant will “not be afforded a reasonable opportunity to recover its fair share of hydrocarbons currently in place by drilling a well at a regular location” and (2) “that the proposed irregular location is reasonable.”¹¹³ According to the Texas Supreme Court, every landowner or lessee is entitled to a fair and reasonable chance to recover the oil and gas beneath his or her tract of land.¹¹⁴ Within the meaning of confiscation under Rule 37, a denial of that fair and reasonable chance would constitute a confiscation of property.¹¹⁵

Notice is also a key component of the Rule 37 exception process.¹¹⁶ If the RRC grants a Rule 37 exception, affected parties—neighboring unleased mineral owners—will receive zero compensation for hydrocarbons drained from their tracts.¹¹⁷ Notice is accordingly indispensable.¹¹⁸ In defining affected persons, statewide Rule 37 recognizes individual special field rules when it states:

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

109. *See id.*

110. *See* 16 TEX. ADMIN. CODE § 3.37 (2011); Camp, *supra* note 67, at 4-5; Elmore, *supra* note 78.

111. § 3.37(a)(3).

112. *See, e.g.*, R.R. Comm’n of Tex. v. Shell Oil Co., 161 S.W.2d 1022, 1026-27 (Tex. 1942).

113. Tex. R.R. Comm’n, *Application of Chesapeake Operating, Inc. for an Exception to Statewide Rule 37 to Drill Well No. 1H on the Ramey Unit, Newark East (Barnett Shale) Field, Tarrant County, Texas*, Rule 37 Case No. 0251216, at 5 (Feb. 11, 2009) (proposal for decision), available at <http://www.rrc.state.tx.us/meetings/ogpfd/ogpor37/0251216-mjh.pdf> [hereinafter *Rule 37 Ramey*].

114. *See, e.g.*, Gulf Land Co. v. Atl. Ref. Co., 131 S.W.2d 73, 80 (Tex. 1939).

115. *See id.*

116. *See* § 3.37(a)(2).

117. *See* Camp, *supra* note 67, at 5-6.

118. *See id.*

record for tracts that have no designated operator; and (iii) all owners of record of unleased mineral interests.¹¹⁹

Failure to provide adequate notice to any of the affected persons described above will render a Rule 37 application void from the beginning.¹²⁰ If one of the affected parties protests the Rule 37 application within twenty days of receiving notice, the RRC will hold a hearing in which the applicant has the sole burden of demonstrating that the exception “is necessary either to prevent waste or to prevent the confiscation of property.”¹²¹

From a producer’s perspective, Rule 37 exceptions are an effective method for dealing with unavailable and unwilling small-tract mineral owners because the exceptions are relatively inexpensive, and the entire exception process is reasonably fast—sometimes as quick as one month from the filing of an application.¹²² In instances where affected parties received notice but failed to protest within twenty-one days, the RRC may grant Rule 37 exceptions administratively.¹²³ In these situations, Rule 37 applicants pay only the RRC’s application fee, and the applicant obtains its Rule 37 exception automatically.¹²⁴ If one or more affected parties protest a Rule 37 application, the RRC will schedule a hearing on the matter.¹²⁵ In those instances, both the Rule 37 applicant and the protesting parties must appear at an RRC hearing in Austin at which the applicant bears the burden of proving the exception is necessary to prevent waste and the confiscation of property.¹²⁶ Although the hearing process increases the time and expense necessary to obtain an exception, a Rule 37 hearing may nevertheless provide the quickest and least expensive method for operators to deal with unavailable or unwilling mineral owners.¹²⁷

While statewide Rule 37 has been in existence for nearly a century, the RRC only granted 49,531 exceptions from 1919 through 2005—granting an annual average of 582 Rule 37 exceptions statewide per year.¹²⁸ By

119. § 3.37(a)(2)(A).

120. See, e.g., Camp, *supra* note 67, at 5-6 (citing Tex. R.R. Comm’n, *Complaint of Long Trusts Regarding Whether Proper Notice Was Given By Union Pacific Resources Co. of its Application for a Rule 37 Exception for the Barksdale Estate Gas Unit, Well No. 8, Oak Hill (Cotton Valley) Field, Rusk County, Texas*, Docket No. 06-0229019 (Oil & Gas Div. Sept. 12, 2002) (final order)).

121. § 3.37(a)(3).

122. See Camp, *supra* note 67, at 24.

123. See § 3.37(h).

124. See *id.*; Camp, *supra* note 67, at 6.

125. See § 3.37(h); Camp, *supra* note 67, at 6.

126. See § 3.37(h); Camp, *supra* note 67, at 6.

127. See Camp, *supra* note 67, at 6, 24.

128. Tex. R.R. Comm’n Online Drilling Permit Application Research Query, R.R. COMM’N OF TEX., <http://www.rrc.state.tx.us> (follow “Online Research (Queries)” hyperlink; follow “Launch Application” hyperlink under the “Drilling Permit (Form W-1) Application Query” field; select “37” from the “SWR” drop-down menu; select “no” from the “Amended” drop-down menu; enter “01/01/1919” into the “Approved Date Begin:” field; enter “12/31/2005” into the “Approved Date End:” field; click “Submit”). The author obtained this data through a request submitted to the RRC under the Texas Public Information Act, TEX GOV’T CODE ANN. § 552.001 (West 2011).

comparison, from 2006 through 2011, the RRC granted 19,583 Rule 37 exceptions—an average of 3,916 Rule 37 exceptions statewide per year.¹²⁹ In the Barnett Shale formation alone, the RRC granted 3,135 Rule 37 exceptions from 2006 through 2011.¹³⁰ This dramatic increase in the number of Rule 37 exceptions is attributable to the newfound prevalence of horizontal drilling and hydraulic fracturing technologies in urban areas.¹³¹ One study done by the *Powell Shale Digest* using RRC data shows that the number of producing horizontal wells present in the Fort Worth area alone grew from 75 in 2003 to 2,901 by 2008.¹³² One of the issues raised by such a dramatic increase is the fact that statewide rules were designed for traditional vertical wells—not for horizontal wells.¹³³ It follows that the Rule 37 exception process was not designed to accommodate situations in which one horizontal well bore could potentially create multiple unleased small tract issues by producing adjacent to a suburban neighborhood.¹³⁴ The rapid increase in the number of horizontal wells in urban areas has created particularly complicated issues with pooling in Texas.¹³⁵

E. Pooling in General

One mechanism through which small tracts may be brought together in order to satisfy applicable well-spacing regulations and obtain a drilling permit is pooling.¹³⁶ Simply defined, pooling involves the constructive joining of at least two separately owned tracts of land so that they are treated as one tract for oil and gas production purposes.¹³⁷ This method of constructively pooling multiple tracts generally covers an area large enough to drill one oil or gas well.¹³⁸ If a producer wishes to join multiple tracts in order to drill and operate multiple wells, it will employ a procedure similar to pooling—unitization.¹³⁹

129. See *id.* (If using the online research tool, enter “01/01/2006” into the “Approved Date Begin:” field and “12/31/2011” into the “Approved Date End:” field before submitting.)

130. See *id.* (If using the online research tool, enter “Barnett Shale” into the “Field Name:” content field before submitting.); see also Camp, *supra* note 67, at 5 (noting that the RRC granted approximately 3,000 Rule 37 exceptions from the early 2000s to March of 2010).

131. See Kurth et al., *supra* note 81, at 279.

132. *Powell Shale Digest: Number of New Vertical and Horizontal Producing Wells by Year as of Jan. 1, 2010: All Counties/Fields in Fort Worth Basin*, BARNETTSHALESNEWS.COM, <http://www.barnettshalenews.com/documents/2010%20charts/VH%20Chart%20to%201-1-2010.pdf> (last visited May 25, 2012).

133. See Camp, *supra* note 67, at 3.

134. See *id.*

135. See Ronnie Blackwell, *Forced Pooling Within the Barnett Shale: How Should the Texas Mineral Interest Pooling Act Apply to Units with Horizontal Wells?*, 17 TEX. WESLEYAN L. REV. 1, 16 (2010).

136. See KRAMER & MARTIN, *supra* note 76, § 1.02, at 1-3; MARTIN & KRAMER, MANUAL, *supra* note 2, at 726.

137. See MARTIN & KRAMER, MANUAL, *supra* note 2, at 726.

138. See KRAMER & MARTIN, *supra* note 76, § 1.02, at 1-3; Paula C. Murray & Frank B. Cross, *The Case For A Texas Compulsory Unitization Statute*, 23 ST. MARY’S L.J. 1099, 1100 (1992).

139. See KRAMER & MARTIN, *supra* note 76, § 1.02, at 1-3; MARTIN & KRAMER, MANUAL, *supra* note 2, at 1026-27.

Sometimes producers are unable to obtain the requisite number of acres in order for the RRC to grant a drilling permit so that the producer may drill an oil or gas well.¹⁴⁰ In those circumstances pooling may become necessary in order for the producer to obtain a drilling permit.¹⁴¹ The primary objective of pooling is to avoid physical and economic waste by preventing the drilling of unnecessary and uneconomic wells.¹⁴² Pooling may be accomplished either through voluntary pooling or compulsory pooling.¹⁴³ Whether voluntary or compulsory, pooling “serves important public purposes, including the prevention of waste, the conservation of oil and gas, and the protection of correlative rights.”¹⁴⁴

1. *Voluntary Pooling*

Voluntary pooling is, as the name implies, voluntary in nature.¹⁴⁵ Consent is therefore indispensable.¹⁴⁶ For voluntary pooling to occur, the lessee in an oil and gas lease must obtain the permission of the lessor.¹⁴⁷ A lessee may obtain the lessor’s permission to pool in three different ways: (1) by executing a community lease, (2) by entering into a separate pooling agreement, and (3) by exercising an oil and gas lease’s pooling clause.¹⁴⁸ Each method of voluntary pooling contains its own intricacies, but every voluntary pooling method shares the basic requirement that the lessor’s consent must be obtained in order for the producer to pool.¹⁴⁹

2. *Compulsory Pooling*

Compulsory pooling—sometimes referred to as forced pooling—provides the second method through which tracts may be pooled together.¹⁵⁰ Nearly every major oil and gas producing state has enacted statutes authorizing

140. See, e.g., KRAMER & MARTIN, *supra* note 76, § 1.02, at 1-3.

141. See *id.*; MARTIN & KRAMER, *MANUAL*, *supra* note 2, at 726. Drilling permits are found in states that regulate well spacing, and the drilling permit serves as authorization from the regulatory state agency to drill a well. MARTIN & KRAMER, *MANUAL*, *supra* note 2, at 270.

142. See MARTIN & KRAMER, *MANUAL*, *supra* note 2, at 726.

143. See KRAMER & MARTIN, *supra* note 76, § 10.01, at 10-2; SHADE, *supra* note 46, at 117 (providing a simplified explanation of the various methods of pooling).

144. KRAMER & MARTIN, *supra* note 76, § 10.01, at 10-2.

145. See, e.g., SHADE, *supra* note 46, at 123.

146. See *id.*

147. See *id.*

148. See KRAMER & MARTIN, *supra* note 76, §§ 7.01-.05. “Community lease” is defined as “[a] single lease covering two or more separately owned tracts of land.” MARTIN & KRAMER, *MANUAL*, *supra* note 2, at 159. A “pooling agreement” is “[a]n agreement bringing together separately owned interests for the purpose of obtaining a well permit under applicable spacing rules.” *Id.* at 726. A “pooling clause” is defined as “[a] lease clause authorizing a lessee to ‘pool’ or join the particular leased premises with other leases for the purpose of aggregating a tract sufficient for a well permit under applicable spacing regulations.” *Id.* at 727.

149. See KRAMER & MARTIN, *supra* note 76, §§ 7.01-.05.

150. See *id.* § 10.01, at 10-2.

compulsory pooling.¹⁵¹ Jurisdictions handle the specifics differently, but most compulsory pooling statutes “provide that any person seeking a drilling permit may force the inclusion of the necessary adjacent tracts . . . to meet the minimum requirements for a drilling permit.”¹⁵² Compulsory pooling statutes generally share four key attributes:

- (1) They expressly presuppose the existence of an established drilling or spacing unit[;]
- (2) [t]hey permit the owners of separate tracts in the unit to pool their respective interests[] on a voluntary basis[;]
- (3) [t]hey require notice and public hearing before pooling can be required[;]
[and]
- (4) [t]hey are based on the proposition that each separate owner shall receive his just and equitable share of production.¹⁵³

Statutorily authorized compulsory pooling serves the important public purposes of preventing waste and conserving oil and gas by minimizing the number of wells drilled, avoiding dramatic declines in natural reservoir energy, and protecting the correlative rights of all mineral owners in a common reservoir.¹⁵⁴ The ultimate premise supporting compulsory pooling is that the state will mandate a pooling agreement for two parties when each would benefit from doing so, but the parties themselves cannot reach a pooling agreement on their own.¹⁵⁵

Oklahoma and New Mexico implemented the first statewide compulsory pooling statutes in 1935.¹⁵⁶ The New Mexico statute was more limited, while the Oklahoma compulsory pooling statute provided the model for what is now the majority view of compulsory pooling.¹⁵⁷ The Oklahoma statute was also the first statewide compulsory pooling statute to undergo a constitutional test.¹⁵⁸ In *Patterson v. Stanolind Oil & Gas Co.*, Patterson owned a royalty interest in a 6.25-acre tract of land that was force-pooled with a neighboring 3.75-acre tract

151. See LOWE ET AL., *supra* note 37, at 189.

152. *Id.*

153. KRAMER & MARTIN, *supra* note 76, § 10.01, at 10-4 to -5 (citing John W. Gee, *Comparative Study of Compulsory Pooling-Enforcement Against Owners of Divided Interests in the Spaced Tract*, 3 ROCKY MTN. MIN. L. INST. 241, 247 (1956)).

154. See *id.* at 10-2. “Reservoir energy” is defined as “[t]he forces in a reservoir [that] propel the oil or gas to the well bore.” MARTIN & KRAMER, MANUAL, *supra* note 2, at 833. Generally, reservoir energy is created by one or more of four natural forces: (1) gas expansion, (2) water encroachment, (3) expansion of reservoir oil, and (4) gravity. *Id.*

155. See SHADE, *supra* note 46, at 117.

156. See KRAMER & MARTIN, *supra* note 76, § 3.02[1]; LOWE ET AL., *supra* note 37, at 219.

157. See KRAMER & MARTIN, *supra* note 76, § 3.02[1].

158. *Patterson v. Stanolind Oil & Gas Co.*, 77 P.2d 83, 85 (Okla. 1938), *appeal dismissed*, 305 U.S. 376 (1939); KRAMER & MARTIN, *supra* note 76, § 3.02[1].

to form a ten-acre drilling unit.¹⁵⁹ Stanolind drilled an oil well on Patterson's 6.25-acre tract, and due to the Oklahoma compulsory pooling provision, Patterson was forced to share the well production with the owners of the 3.75-acre tract.¹⁶⁰ Alleging that the state's police powers did not extend so far as to permit the state to proportionally distribute the oil and gas produced solely from one tract with other force-pooled tracts, Patterson claimed the Oklahoma compulsory pooling statute violated his right to due process guaranteed by both the state constitution and the Federal Constitution.¹⁶¹ Accordingly, Patterson filed suit to recover \$988.68—the amount owed as royalty if Oklahoma's compulsory pooling statute that provided for proportionate distribution of royalty payments was unconstitutional.¹⁶² The trial court held that the state's compulsory pooling statute did not violate Patterson's constitutional right to due process and awarded Patterson \$824.32—Patterson's proportionate royalty share under the compulsory pooling statute.¹⁶³ The Oklahoma Supreme Court noted that “it is not beyond the police power of the state to . . . authorize a ‘just distribution’ among the various owners of mineral rights in land overlying the common source of supply.”¹⁶⁴ In addition, the court reasoned that the correlative rights of mineral owners over a common source of supply are well protected by the implementation of compulsory pooling provisions that distribute production from common reservoirs proportionally among overlying owners.¹⁶⁵ Ultimately, the court held that the compulsory pooling provision did not constitute a taking; rather, Patterson's royalty interest was merely “restricted and qualified,” and the state's inherent police powers prevented a violation of Patterson's due process rights under both the state constitution and the Federal Constitution.¹⁶⁶

Today, Oklahoma's compulsory pooling statute provides, in part:

[where two adjoining small tract owners] have not agreed to pool their interests[,] and where one such separate owner has drilled or proposes to drill a well on said unit [in]to the common source of supply, the Commission, to avoid the drilling of unnecessary wells, or to protect correlative rights, shall . . . require such owners to pool and develop their lands in the spacing unit as a unit.¹⁶⁷

159. See *Patterson*, 77 P.2d at 87. A “royalty interest” is created when the mineral estate is severed from the surface estate. See MARTIN & KRAMER, MANUAL, *supra* note 2, at 860. Generally, “[t]he owner of a royalty interest is entitled to a share of [oil and gas] production . . . free of the costs of production.” *Id.*

160. See *Patterson*, 77 P.2d at 87.

161. See *id.* 86-87.

162. See *id.* at 85.

163. See *id.*

164. *Id.* at 88.

165. *Id.* at 89.

166. *Id.*

167. OKLA. STAT. ANN. tit. 52, § 87.1(e) (West 2011).

The compulsory pooling provisions adopted in Oklahoma follow the general principle noted above—if pooling would benefit two neighboring parties, and the parties cannot reach a pooling agreement on their own, Oklahoma’s oil and gas regulatory agency will mandate a pooling agreement for them.¹⁶⁸ Texas’s compulsory pooling statute, on the other hand, takes a different approach.¹⁶⁹

F. The Mineral Interest Pooling Act—Texas’s Current Compulsory Pooling Statute

The Mineral Interest Pooling Act (MIPA) is Texas’s version of a compulsory pooling statute.¹⁷⁰ First enacted in 1965, MIPA is widely regarded as a compulsory pooling provision that will activate only once all voluntary pooling efforts are exhausted.¹⁷¹ Some believe Texas varies the general principle supporting compulsory pooling in most states—if individual mineral owners are unable to reach a pooling agreement then the applicable state agency will compel the parties to pool—by adding the caveat that compulsion will only be used as a last resort.¹⁷² A brief glance at the requirements a mineral owner must satisfy to pool under MIPA demonstrates the weight the statute places on preliminary efforts to pool voluntarily and the legislature’s reluctance to authorize the RRC to exercise compulsory pooling under MIPA.¹⁷³ The contentious history of compulsory pooling in Texas reveals the reasoning behind the legislature’s hesitancy to adopt a true compulsory pooling statute.

Historically, Texas was one of the only major oil producing states that took an adverse stance to compulsory pooling.¹⁷⁴ The basis of this stance was rooted firmly in the common law rule of capture—all landowners have the right to produce as much oil and gas from beneath their property as they are capable of producing.¹⁷⁵ Early on, many interpreted this rule to mean that landowners, regardless of how large or small their tracts were, had the unlimited right to drill and produce from their tracts.¹⁷⁶ Essentially, this meant that landowners were entitled to drill a well on their property.¹⁷⁷ In the early twentieth century,

168. See SHADE, *supra* note 46, at 118.

169. See TEX. NAT. RES. CODE ANN. § 102 (West 2011); KRAMER & MARTIN, *supra* note 76, § 10.02, at 10-5.

170. See § 102; KRAMER & MARTIN, *supra* note 76, § 10.02, at 10-5.

171. See § 102; KRAMER & MARTIN, *supra* note 76, § 10.02, at 10-6; Lisa Vaughn, *New Facets of Old Alternatives for Unleased Mineral Interests*, 16 TEX. WESLEYAN L. REV. 113, 119-20 (2009).

172. See SHADE, *supra* note 46, at 121.

173. See § 102; Ernest E. Smith, *The Texas Compulsory Pooling Act*, 43 TEX. L. REV. 1003, 1009 (1965).

174. See KRAMER & MARTIN, *supra* note 76, § 10.02, at 10-6; Smith, *supra* note 173, at 1009.

175. See KRAMER & MARTIN, *supra* note 76, § 10.01, at 10-3; see also *Elliff v. Texon Drilling Co.*, 210 S.W.2d 558, 561-62 (Tex. 1948) (explaining the common law rule of capture).

176. See KRAMER & MARTIN, *supra* note 76, § 10.01, at 10-3; Smith, *supra* note 173, at 1003-04.

177. See, e.g., *R.R. Comm’n of Tex. v. Humble Oil & Ref. Co.*, 245 S.W.2d 488, 490 (Tex. 1952) (holding that the owner of a legally subdivided mineral tract was entitled to a Rule 37 exception because mineral ownership included the right to drill a well as a matter of law).

this interpretation caused significant problems in areas that contained many small tracts because spacing and density requirements, if strictly enforced, would have inevitably prevented some small-tract owners from producing oil and gas from beneath their property.¹⁷⁸ Most oil producing states remedied this problem by enacting compulsory pooling and unitization legislation, and delegating authority to appropriate statewide agencies, but the Texas Legislature viewed compulsory pooling and unitization as “a ‘socialistic’ intrusion upon free enterprise” that went against the common law rule of capture.¹⁷⁹ The RRC ultimately took the position that each small-tract mineral owner was entitled to drill and produce from at least one well.¹⁸⁰ Notably, the RRC created allowable formulas—RRC stipulated production limitations on how much oil or gas may be produced from a well over a period of time—that greatly favored small-tract mineral owners.¹⁸¹ Instead of calculating allowables strictly on an acreage basis, the RRC calculated them partially on an acreage basis and partially on a per-well basis.¹⁸² This effectively discouraged voluntarily pooling because small-tract mineral owners were not only entitled to drill and produce, but the Texas judicial system guaranteed them the right to produce enough oil and gas to realize a reasonable profit.¹⁸³ Calculating allowables in this manner essentially gave small-tract mineral owners a license to drain oil and gas from neighboring mineral owners, thus the Texas Supreme Court finally changed course in 1961.¹⁸⁴

Two Texas Supreme Court cases struck down the RRC’s method of calculating allowables in the early 1960s and changed the course of compulsory pooling in Texas.¹⁸⁵ In *Atlantic Refining Co. v. Railroad Commission of Texas (Normanna)*, the Texas Supreme Court invalidated a gas production allowable structure that calculated allowables based on a one-third acreage, two-thirds per-well formula.¹⁸⁶ The court noted that the RRC is authorized to calculate

178. See Smith, *supra* note 173, at 1003-04.

179. Murray & Cross, *supra* note 138, at 1153; see Smith, *supra* note 173, at 1003-04.

180. See, e.g., *Humble Oil*, 245 S.W.2d at 490; Smith, *supra* note 173, at 1004.

181. See MARTIN & KRAMER, MANUAL, *supra* note 2, at 37-38 (defining “allowable”); see also 6 PATRICK H. MARTIN & BRUCE M. KRAMER, WILLIAMS & MEYERS OIL AND GAS LAW § 933.6 (2010) [hereinafter MARTIN & KRAMER, OIL AND GAS LAW] (summarizing the one-third, two-thirds gas production allowable formula).

182. See *Atl. Ref. Co. v. R.R. Comm’n of Tex. (Normanna)*, 346 S.W.2d 801, 803 (Tex. 1961) (providing an example of a formula that calculated allowable gas production based on a one-third acreage and two-thirds per-well basis); *R.R. Comm’n of Tex. v. Humble Oil & Ref. Co.*, 193 S.W.2d 824, 826 (Tex. Civ. App.—Austin 1946, writ ref’d n.r.e.), *aff’d*, 331 U.S. 791 (1947) (providing an example of a formula that calculated allowable oil production based on a one-half acreage and one-half per-well basis).

183. See *Humble Oil*, 193 S.W.2d at 832 (holding that a mineral owner’s allowable production could not be cut down so that his well will not produce or cut below the point at which he could make a reasonable profit).

184. See, e.g., Smith, *supra* note 173, at 1005.

185. See *Halbouty v. R.R. Comm’n of Tex. (Port Acres)*, 357 S.W.2d 364, 376 (Tex. 1962); *Normanna*, 346 S.W.2d at 812.

186. See *Normanna*, 346 S.W.2d at 803. *Atlantic Refining Co.* is commonly referred to as the *Normanna* decision because the well at issue was located in the Normanna Field. See Smith, *supra* note 173, at 1005.

production allowables in oil and gas fields, and that the court should not interfere by setting rules that it deems appropriate—the RRC alone is tasked with creating regulatory rules that conserve oil and gas and protect correlative rights.¹⁸⁷ The court also reasoned, however, that the judicial system may determine the validity of the rules and regulations promulgated by the RRC.¹⁸⁸ Acting in that capacity, the *Normanna* court held that the one-third, two-thirds allowable gas production formula was invalid because it did not “afford each producer in the field an opportunity to produce his fair share of the gas from the reservoir.”¹⁸⁹ In *Halbouty v. Railroad Commission (Port Acres)*, the Texas Supreme Court reaffirmed its holding in *Normanna* by invalidating a gas production allowable formula based on the one-third, two-thirds model.¹⁹⁰ The *Port Acres* court invalidated the allowable formula set by the RRC because it allowed small-tract mineral owners to produce a significantly disproportionate amount of gas and did not “afford an [o]ppportunity to all of the parties to produce and save their fair share of the minerals.”¹⁹¹ In light of the *Normanna* and *Port Acres* decisions, small-tract mineral owners were no longer entitled to produce enough oil or gas to realize a reasonable profit; rather, small-tract mineral owners were limited to producing their fair share in order to protect the correlative rights of other mineral owners in the field.¹⁹² Even though allowable formulas no longer favored production from small tracts, the *Normanna* and *Port Acres* decisions opened the door for the Texas Legislature to implement a form of compulsory pooling.¹⁹³

After *Normanna* and *Port Acres*, small-tract mineral owners were no longer entitled to produce oil and gas at rates that would garner reasonable profits, so absent the license to drain previously held by small-tract mineral owners, production from small tracts was no longer economically feasible in most cases.¹⁹⁴ Even though production from small tracts was no longer indirectly favored, problems still arose between large-tract and small-tract mineral owners.¹⁹⁵ Prior to *Normanna* and *Port Acres*, large-tract mineral owners protested the disproportionate production allowable small-tract owners enjoyed, whereas after *Normanna* and *Port Acres*, small-tract owners found themselves at the mercy of large-tract mineral owners.¹⁹⁶ Small-tract mineral owners remained entitled to a Rule 37 exception to drill a well in violation of

187. See *Normanna*, 346 S.W.2d at 812.

188. See *id.*

189. See *id.* at 811.

190. See *Halbouty*, 357 S.W.2d at 376. *Halbouty* is commonly referred to as the *Port Acres* decision because the well at issue was located in the Port Acres Field. See Smith, *supra* note 173, at 1005.

191. *Halbouty*, 357 S.W.2d at 376.

192. See *id.*; *Normanna*, 346 S.W.2d at 811; see also MARTIN & KRAMER, OIL AND GAS LAW, *supra* note 181, § 933.6 (describing the ultimate impact of the *Normanna* and *Port Acres* decisions on the development of Texas’s compulsory pooling statute).

193. See KRAMER & MARTIN, *supra* note 76, § 10.02, at 10-5.

194. See MARTIN & KRAMER, OIL AND GAS LAW, *supra* note 181, § 933.6.

195. See KRAMER & MARTIN, *supra* note 76, § 10.01, at 10-3.

196. See, e.g., Smith, *supra* note 173, at 1007-08.

RRC spacing regulations, but they were not guaranteed a reasonable profit from those wells.¹⁹⁷ This meant that to reap the benefits of production from mineral tracts too small to meet RRC spacing regulations, small-tract mineral owners would have to pool with neighboring mineral owners.¹⁹⁸ Absent a compulsory pooling statute, the only way for small tracts to pool with neighboring mineral tracts was to pool voluntarily.¹⁹⁹ Voluntary pooling, as described in Part II.E.1 above, hinges on consent.²⁰⁰ Obtaining consent is not always easy or expeditious.²⁰¹ Accordingly, small-tract mineral owners, once the most ardent opponents of compulsory pooling, became the strongest proponents of a compulsory pooling scheme in Texas.²⁰²

In 1965, shortly after the *Normanna* and *Port Acres* decisions, the Texas Legislature enacted MIPA.²⁰³ Technically, MIPA is Texas's compulsory pooling statute.²⁰⁴ In practice, however, the limitations contained in the statute and the limited construction MIPA has received render the statute merely a tool to encourage separate mineral owners to pool voluntarily.²⁰⁵ Some of MIPA's explicit limitations include: (1) application only to oil and gas reservoirs discovered and produced after March 8, 1961—the date of the *Normanna* decision; (2) no application to state owned lands or lands in which the state has a direct or indirect interest; (3) RRC authorization to pool only acreage that “reasonably appears to lie within the productive limits of the reservoir”; and (4) RRC jurisdiction to force pool contingent upon a “fair and reasonable offer to pool voluntarily.”²⁰⁶ If these limitations, or one of the other limitations contained in the statute, do not render MIPA unavailable, the elements established by the statute require that: (1) there must be two or more separately owned tracts, (2) contained in a common reservoir of oil or gas, (3) for which special field rules have established the size and shape of proration units, (4) where the separately owned interests are within a proposed or existing proration unit in the common reservoir, (5) the separate owners have not agreed

197. See KRAMER & MARTIN, *supra* note 76, § 10.01, at 10-3; Smith, *supra* note 173, at 1007-08.

198. See KRAMER & MARTIN, *supra* note 76, § 10.02, at 10-5; Smith, *supra* note 173, at 1007-08.

199. See Smith, *supra* note 173, at 1007-08.

200. See discussion *supra* Part II.E.1.

201. See discussion *supra* Part II.E.1. See generally Smith, *supra* note 173, at 1007 (describing the effect support from small-tract mineral owners had on the implementation of a compulsory pooling statute in Texas).

202. See Smith, *supra* note 173, at 1007.

203. See generally TEX. NAT. RES. CODE ANN. § 102 (West 2011) (codifying MIPA); KRAMER & MARTIN, *supra* note 76, § 10.02, at 10-5.

204. See § 102; KRAMER & MARTIN, *supra* note 76, § 10.02, at 10-5; Smith, *supra* note 173, at 1009-17.

205. See 3 ERNEST E. SMITH & JACQUELINE L. WEAVER, TEXAS LAW OF OIL AND GAS, ch. 12, § 12.1(B), at 7 (1989-1992) (stating “courts have consistently construed MIPA as limited in function to protecting small-tract lessees rather than as a broad act designed to protect correlative rights generally, or as an act allowing large-tract lessees more flexibility in development”).

206. See TEX. NAT. RES. CODE ANN. § 102.003 (West 2011) (March 8, 1961 limitation); *id.* § 102.004 (public land limitation); *id.* § 102.013 (voluntary pooling offer limitation); *id.* § 102.018 (productive limits of reservoir limitation); see also Blackwell, *supra* note 135, at 7-8 (summarizing the requirements and limitations explicitly contained in the MIPA statute); Smith, *supra* note 173, at 1009-17 (summarizing some of the limitations contained in MIPA).

to pool their interests, and (6) at least one of the separate owners has drilled or plans to drill on the existing or proposed proration unit.²⁰⁷ In addition, the most notable MIPA requirement is contained in § 102.013—the reasonable and fair offer to voluntarily pool requirement.²⁰⁸ The MIPA statute specifically creates a condition precedent with regard to a voluntary offer to pool—if the RRC finds that a fair and reasonable offer to pool voluntarily was not made, the commission must dismiss the MIPA pooling application.²⁰⁹ Unfortunately, the statute does little to define what constitutes a fair and reasonable offer to pool voluntarily.²¹⁰ MIPA does provide four examples of offers to pool voluntarily that are not considered fair and reasonable.²¹¹ The MIPA statute states:

A pooling agreement, offer to pool, or pooling order is not considered fair and reasonable if it provides for an operating agreement containing any of the following provisions:

- (1) preferential right of the operator to purchase mineral interests in the unit;
- (2) a call on or option to purchase production from the unit;
- (3) operating charges that include any part of district or central office expense other than reasonable overhead charges; or
- (4) prohibition against nonoperators questioning the operation of the unit.²¹²

Aside from these four characterizations of voluntary pooling offers that do not meet the fair and reasonable standard, MIPA provides little guidance as to what constitutes a fair and reasonable offer to voluntarily pool.²¹³ It follows that most forced pooling litigation in Texas centers on MIPA's fair and reasonable offer to voluntarily pool requirement.²¹⁴ The most instructive guidance as to what constitutes a fair and reasonable offer to voluntarily pool came in 1984 from the Texas Supreme Court in *Carson v. Railroad Commission of Texas*, when the court noted that generally the offer "must be one [that] takes into consideration those relevant facts, existing at the time of the offer, which would be considered important by a reasonable person in entering into a voluntary agreement concerning oil and gas properties."²¹⁵ Overall the Texas compulsory pooling statute's historical use is largely limited to encouraging voluntary

207. See TEX. NAT. RES. CODE ANN. § 102.011 (West 2011).

208. See *id.* § 102.013; SMITH & WEAVER, *supra* note 205, § 12.1(B), at 7; Blackwell, *supra* note 135, at 5; Smith, *supra* note 173, at 1009.

209. § 102.013(b).

210. See *id.*

211. See *id.* § 102.015.

212. See *id.*

213. See § 102; KRAMER & MARTIN, *supra* note 76, § 10.02, at 10-6.

214. See *Carson v. R.R. Comm'n of Tex.*, 669 S.W.2d 315, 316 (Tex. 1984); *Coleman v. R.R. Comm'n of Tex.*, 445 S.W.2d 790, 794-95 (Tex. Civ. App.—Texarkana 1969), *modified on other grounds*, 460 S.W.2d 404 (Tex. 1970); *Buttes Res. Co. v. R.R. Comm'n of Tex.*, 732 S.W.2d 675, 678 (Tex. Civ. App.—Houston [14th Dist.] 1987, writ ref'd n.r.e.); see also KRAMER & MARTIN, *supra* note 76, § 10.02[1], at 10-7 to -11 (summarizing MIPA litigation and the fair and reasonable offer to voluntarily pool requirement).

215. *Carson*, 669 S.W.2d at 318.

pooling and allowing small-tract mineral owners to “muscle in” to existing units in which mineral production has previously commenced.²¹⁶

III. REMEMBER LARRY LANDOWNER AND EXXELL OIL CO.?

A. *The Likely Outcome*

Larry Landowner, the fictional character introduced in Part I of this Comment, owns the surface and mineral estates to a 0.33-acre residential tract of land near Fort Worth.²¹⁷ Exxell Oil Co. owns several mineral leases adjacent to Larry Landowner’s neighborhood, but Larry Landowner’s minerals remain unleased.²¹⁸ Exxell believes, to maximize gas production from the Barnett Shale formation underlying its leased tracts, it must drill and produce from a horizontal well bore located within 330 feet of Larry Landowner’s residential property.²¹⁹ This proposed horizontal well bore location violates the spacing requirements found in the Barnett Shale’s special field rules.²²⁰ Assuming Larry Landowner is unwilling to lease or is unavailable, Exxell must either seek a spacing exemption from the RRC or attempt to force-pool Larry’s tract in order to produce oil and gas from within 330 feet of Larry’s property.²²¹

Under the current framework, applying for a Rule 37 exception is probably Exxell’s quickest and least expensive option.²²² In theory, MIPA may allow Exxell to force-pool Larry’s tract, along with the rest of the unleased tracts in Larry’s neighborhood; however, cases in which such efforts were attempted successfully are extremely rare.²²³ Additionally, complying with MIPA requirements and navigating MIPA proceedings is very expensive due to the amount of time the process takes.²²⁴ One of the few successful MIPA forced pooling attempts in which the producer attempted to pool neighboring unleased mineral owners rather than pursue Rule 37 exceptions occurred in

216. See KRAMER & MARTIN, *supra* note 76, § 10.02[1], at 10-7 to -11; SMITH & WEAVER, *supra* note 205, § 12.1(B), at 7.

217. See *supra* Part I.

218. See *supra* Part I.

219. See *supra* Part I; see also discussion *supra* Part II.C (summarizing the horizontal drilling and hydraulic fracturing process).

220. See *Barnett Shale Special Field Rules*, *supra* note 80 (requiring a distance of 330 feet between producing well bores and unleased mineral acreage).

221. See 16 TEX. ADMIN. CODE § 3.37 (2011); TEX. NAT. RES. CODE ANN. § 102 (West 2011).

222. See Camp, *supra* note 67, at 4 (noting that pursuing a Rule 37 exception is the most attractive option for producers dealing with unleased small-tract mineral owners).

223. See TEX. NAT. RES. CODE ANN. § 102; Blackwell, *supra* note 135, at 9-16 (summarizing several recent RRC proposals for decision regarding MIPA forced pooling orders).

224. See Tex. R.R. Comm’n, *Application of Finley Resources, Inc., for the Formation of a Unit Pursuant to the Mineral Interest Pooling Act for the Proposed East Side Unit, Newark, East (Barnett Shale) Field, Tarrant County, Texas*, Docket No. 09-0252373, at 4-6 (Oil & Gas Div. Aug. 5, 2008) (proposal for decision) (noting that Finley Resources obtained a MIPA order from the RRC three years after beginning efforts to produce from the mineral acreage), available at <http://www.rrc.state.tx.us/meetings/ogpfd/ogpomipa/FinleyOriginalPFD05-12-08.pdf> [hereinafter *Finley Resources Proposal for Decision*].

2008 when Finley Resources, Inc. (Finley) successfully force-pooled twenty-eight residential lots covering approximately 5.7 acres of land.²²⁵ Finley began efforts to lease the small, unleased mineral tracts located within two miles of downtown Fort Worth in 2005.²²⁶ Production from the unit was delayed for three years while Finley attempted to lease or enter into voluntary pooling agreements with the unavailable or unwilling mineral owners in the neighborhood.²²⁷ Finley eventually submitted an application to force-pool the unleased tracts under MIPA in 2007.²²⁸ The RRC application examiners recommended approval, and the RRC ultimately approved Finley's MIPA unit.²²⁹ Notably, the examiners specifically stated Finley's case was unique and that MIPA should generally not be used to avoid Rule 37 exceptions or to simply make production more convenient for the producer.²³⁰ Other recent MIPA proceedings in the Barnett Shale follow a similar line of reasoning.²³¹ As a result, Exxell Oil Co. will likely pursue a Rule 37 exception instead of attempting to use MIPA to force-pool Larry Landowner's tract.²³²

If Exxell decides to apply for a Rule 37 spacing exception to drill and produce from its proposed horizontal well bore location, it will have to file an application with the RRC.²³³ Once the application is filed, Larry Landowner and all other "affected parties" will receive notice of Exxell's application.²³⁴ If none of the affected parties object to Exxell's application for a Rule 37 spacing exception, the RRC may automatically grant Exxell a permit to drill and produce from within 330 feet of unleased mineral acreage.²³⁵ Should an affected party object, however, Exxell will bear the burden of proving the exception is necessary to prevent waste or to prevent confiscation of property.²³⁶ If Exxell meets its burden at the RRC hearing in Austin, and the RRC grants the Rule 37 exception, the horizontal well bore will inevitably drain Larry Landowner's—and all other affected parties'—minerals.²³⁷ Unfortunately for Larry and other affected parties, the common law rule of capture will preclude recovery for the drained hydrocarbons.²³⁸

225. See *id.* at 2; Tex. R.R. Comm'n, *Application of Finley Resources, Inc. for the Formation of a Unit Pursuant to the Mineral Interest Pooling Act for the Proposed East Side Unit, Newark, East (Barnett Shale) (65280200) Field, Tarrant County, Texas*, Docket No. 09-0252373, at 1 (Oil & Gas Div. Aug. 25, 2008) (final order), available at <http://www.rrc.state.tx.us/meetings/ogpfd/ogpomipa/FinleySignedFinalOrder.pdf>.

226. See *Finley Resources Proposal for Decision*, *supra* note 224, at 4.

227. See *id.* at 4-6.

228. See *id.* at 2.

229. See *id.* at 9-10.

230. See *id.* at 2, 9-10.

231. See Blackwell, *supra* note 135, at 9-16; Camp, *supra* note 67, at 4.

232. See Blackwell, *supra* note 135, at 9-16; Camp, *supra* note 67, at 4.

233. See 16 TEX. ADMIN. CODE § 3.37(a)(2) (2011); *supra* Part II.D.

234. See § 3.37(a)(2).

235. See *id.*

236. See *id.*

237. See Camp, *supra* note 67, at 5-6.

238. See *Elliff v. Texon Drilling Co.*, 210 S.W.2d 558, 562 (Tex. 1948); Tex. R.R. Comm'n, *Application of Anadarko E&P Co. LP for an Exception to Statewide Rule 37*, Docket No. 0246122, at 5, 7 (Oil & Gas

B. The Gloomy Outlook for Unleased, Small-Tract Mineral Owners

Unleased mineral owners like the fictitious Larry Landowner are left out in the cold under the current framework.²³⁹ If Exxell obtains its Rule 37 exception—either administratively or after a hearing—the common law rule of capture will apply, and Larry will receive no compensation for the minerals drained from beneath his tract.²⁴⁰ Because producers have little incentive to pursue voluntary—and especially not compulsory—pooling options, the most efficient option for producers is to seek Rule 37 exceptions from the RRC.²⁴¹ While neighboring unleased mineral owners are left out in the cold under the current framework, producers are not greatly benefitted by the current interplay between Rule 37 exceptions and Texas’s forced pooling statute either.²⁴²

C. Producers Suffer Too

From a producer’s perspective, the current framework inadvertently encourages spacing exceptions and discourages pooling.²⁴³ This decreases producers’ productive and economic efficiency.²⁴⁴ Producers face a difficult task in creating reasonable development and production plans in urban areas due to the looming possibility of encountering unavailable or unleased mineral owners.²⁴⁵ In addition, if a producer attempts to pool neighboring unleased mineral tracts, development and production may be delayed for substantial periods of time—three years in *Finley*.²⁴⁶ Given the typically short primary terms taken on leases in the Texas Shale Plays, extended delays jeopardize leases and thwart development and production.²⁴⁷ Issues with Rule 37 exceptions and pooling in urban Texas Shale Plays are twofold—the correlative rights of unleased, small-tract mineral owners are not protected because the RRC is essentially granting producers licenses to drain, and production is not maximized due to producers’ inability to adequately plan development and production throughout urban fields.²⁴⁸

Div. Apr. 19, 2006) (proposal for decision) (recognizing the protesting, unleased mineral owners’ drainage concerns but refusing to deny the Rule 37 exception on that basis).

239. See *supra* notes 222-38 and accompanying text.

240. See *Elliff*, 210 S.W.2d at 562.

241. Camp, *supra* note 67, at 4-6, 24.

242. See Murray & Cross, *supra* note 138, at 1100-02.

243. See *id.*

244. See *id.*

245. See *id.*

246. See *Finley Resources Proposal for Decision*, *supra* note 224, at 4-6.

247. See Glenn E. Johnson, *A Look at Recent RRC Decisions on Forced Pooling*, 22 (25) FORT WORTH BUSINESS PRESS—ENERGY REPORT 22, 23 (June 2010).

248. See Blackwell, *supra* note 135, at 9-16; Camp, *supra* note 67, at 4.

IV. POTENTIAL SOLUTIONS TO THE PROBLEMS ILLUSTRATED IN THE LARRY
LANDOWNER HYPOTHETICAL

*A. Implement a Revised Statewide Compulsory Pooling Statute Resembling
the Compulsory Pooling Statutes Enacted in Most Other Oil Producing
States*

One way to protect the correlative rights of unleased mineral owners, promote efficiency in planning among producers, and maximize hydrocarbon extraction from urban fields is for the Texas Legislature to replace MIPA with a revised statewide compulsory pooling statute akin to the statutes adopted in most other oil producing states.²⁴⁹ This is a drastic solution considering Texas's historically adverse position toward compulsory pooling.²⁵⁰ If Texas were to adopt a new compulsory pooling statute, however, mineral owners in urban areas would benefit from the royalties received from production, and production from urban fields would benefit from added efficiency.²⁵¹

Broad compulsory pooling statutes, the kind available in most oil producing states, protect the correlative rights of unleased mineral owners by ensuring that pooled mineral owners receive compensation for hydrocarbons produced from any location within the pooled area.²⁵² The methods in which compensation is afforded vary among states, but the important fact is that all pooled mineral owners, no matter what their interest, receive compensation proportionate to the size of their pooled tract.²⁵³ That is a stark contrast to the common result if a producer obtains a Rule 37 exception under the current Texas framework.²⁵⁴ The goals of preventing waste and conserving natural resources are also advanced by most compulsory pooling statutes because the flexibility compulsory pooling provides promotes efficiency in planning field-development and production.²⁵⁵ The efficiency afforded by added flexibility demonstrates why producers would also benefit from the implementation of a broader compulsory pooling statute.²⁵⁶

Under most compulsory pooling statutes, producers are able to efficiently plan development within pre-existing spacing or drilling units because they may automatically apply for a compulsory pooling order if they encounter unleased or unavailable mineral owners.²⁵⁷ There is no requirement, as there is under MIPA, for the producer to exhaust all efforts to pool voluntarily prior to filing

249. See LOWE ET AL., *supra* note 37, at 189; Murray & Cross, *supra* note 138, at 1100-02.

250. See *supra* notes 174-84 and accompanying text.

251. See Murray & Cross, *supra* note 138, at 1100-02.

252. See KRAMER & MARTIN, *supra* note 76, §§ 12.01-03 (summarizing and discussing the varying ways in which pooled mineral interest owners receive compensation from hydrocarbon production).

253. See *id.*

254. See *supra* notes 239-48 and accompanying text.

255. See *supra* Part II.E.

256. See *infra* notes 257-62 and accompanying text.

257. See KRAMER & MARTIN, *supra* note 76, § 10.02, at 10-5 to -17.

an application for a compulsory pooling order.²⁵⁸ The absence of such a rigid requirement expedites the compulsory pooling process in most states.²⁵⁹ The availability of compulsory pooling, and the relatively quick timeframe in which producers may obtain compulsory pooling orders, enables producers to efficiently plan urban oil and gas development.²⁶⁰ Added efficiency is especially important in urban oil and gas fields because, by employing horizontal drilling technologies, producers are able to minimize the number of wells drilled, thereby reducing the surface footprint of production operations and reducing the costs of developing urban fields.²⁶¹ Efficiency in planning also prevents waste by allowing producers to extract the maximum amount of hydrocarbons economically possible from producing, urban formations.²⁶²

If the Texas Legislature were to adopt a broader compulsory pooling statute to replace MIPA, compulsory pooling—as opposed to Rule 37 exceptions and MIPA—would become a viable option for producers to consider in developing urban fields.²⁶³ At the same time, a revised statewide compulsory pooling statute would better protect the correlative rights of unleased mineral owners because, once pooled, they would receive royalty payments proportionate to the size of their tract for the minerals extracted from the entire pooled unit.²⁶⁴ Unfortunately, the Texas Legislature is not likely to replace MIPA with a broader statewide compulsory pooling statute similar to those adopted in most states—the history surrounding compulsory pooling is too contentious, and the change is likely too drastic to garner support from state politicians.²⁶⁵ A more realistic solution might involve broadening the interpretation of the existing language in MIPA.²⁶⁶

B. Broaden the Interpretation of MIPA So That It Protects Correlative Rights Generally and Allows Large Tract Producers More Flexibility in Development

Another way to resolve the issues illustrated in the Larry Landowner hypothetical is to interpret the existing language in MIPA more broadly so that it operates comparable to other compulsory pooling statutes in oil producing

258. *See id.* But most statutes allow producers and unleased mineral owners to pool voluntarily or enter into lease agreements at will. *Id.* at 10-4 to -5.

259. *See id.* at 10-5 to -17 (discussing the specific requirements of select oil producing states' compulsory-pooling statutes); Smith, *supra* note 173, at 1009 (discussing MIPA's unique requirement that applicants exhaust all efforts to pool voluntarily before applying for a compulsory pooling order under MIPA).

260. *See* Murray & Cross, *supra* note 138, at 1100-02.

261. *See supra* Part II.C.

262. *See* Murray & Cross, *supra* note 138, at 1100-02, 1153-54.

263. *See id.* at 1143-45.

264. *See* KRAMER & MARTIN, *supra* note 76, §§ 12.01-.03 (summarizing and discussing the varying ways in which pooled mineral interest owners receive compensation from hydrocarbon production).

265. *See supra* notes 174-216 and accompanying text.

266. *See infra* Part IV.B.

states.²⁶⁷ Several commentators have advocated this approach.²⁶⁸ Section 102.011 of MIPA contains language similar to that of many common compulsory pooling statutes around the country.²⁶⁹ But MIPA has traditionally been narrowly “construed . . . as limited in function to [protect owners of small tracts] rather than as a broad act designed to protect correlative rights generally, or as an act allowing [owners of large tracts] more flexibility in development.”²⁷⁰ The *Finley* case, discussed in Part III above, provides one example of an evolving MIPA interpretation.²⁷¹ There, the RRC examiners afforded § 102.011 a broader interpretation than traditionally allowed, providing the producer in *Finley* the ability to employ MIPA as a tool in urban oil and gas development.²⁷² While *Finley* may have opened the door to future MIPA applications outside the interpretative constraints that have traditionally hindered its use as a field-development tool, producers still have little incentive to pursue a MIPA application—Rule 37 exceptions are simply easier and faster to obtain.²⁷³ If the RRC deemphasizes producers’ reliance on Rule 37 exceptions and employs a broader interpretation of § 102.011, then MIPA may theoretically solve the issues demonstrated in the Larry Landowner hypothetical.²⁷⁴

While MIPA’s traditional interpretation serves to protect the correlative rights of small-tract mineral owners rather than correlative rights generally, such an interpretation fails to protect small, unleased mineral owners in urban fields.²⁷⁵ The problem is that when the Texas Legislature enacted MIPA, it did not contemplate horizontal drilling in urban areas.²⁷⁶ Applying the plain language of § 102.011, producers should be able, upon complying with § 102.013’s offer to voluntarily pool requirement, to apply to the RRC for a compulsory pooling order.²⁷⁷ Once the notice and public hearing requirements

267. See Blackwell, *supra* note 135, at 16-17 (“[T]he RRC has lost sight of the plain language of the statute and the true purpose of MIPA in applying the statute to horizontal wells in the Barnett Shale.”); Camp, *supra* note 67, at 14 (“MIPA’s plain language . . . does not limit its use to small tracts force pooling their way into larger pools.”).

268. See Blackwell, *supra* note 135, at 16-17; Camp, *supra* note 67, at 14; Kramer, *supra* note 62, at 8-30 to -32; Vaughn, *supra* note 171, at 124.

269. Compare TEX. NAT. RES. CODE ANN. § 102.011 (West 2011) (providing the plain language of MIPA’s requirements to force pool), with OKLA. STAT. ANN. tit. 52, § 87.1(e) (West 2011) (providing the relevant portion of Oklahoma’s compulsory pooling statute), LA. REV. STAT. ANN. § 30:10 (2007) (providing the relevant portion of Louisiana’s compulsory pooling statute), and N.M. STAT. ANN. § 70-2-17 (A)-(C) (West 1978) (providing the relevant portion of New Mexico’s compulsory pooling statute).

270. SMITH & WEAVER, *supra* note 205, § 12.1(B), at 12-5.

271. See *supra* notes 225-30 and accompanying text.

272. See Camp, *supra* note 67, at 14.

273. See *supra* notes 122-34 and accompanying text; see also Vaughn, *supra* note 171, at 124 (discussing the difficulties and disadvantages of using MIPA as a tool for producers in urban development).

274. See Camp, *supra* note 67, at 23-24; Vaughn, *supra* note 171, at 125-26.

275. See *supra* notes 223-48 and accompanying text.

276. See Blackwell, *supra* note 135, at 16-17.

277. See TEX. NAT. RES. CODE ANN. §§ 102.011, 013 (West 2011); Vaughn, *supra* note 171, at 120 (“Regardless of its ‘voluntary encouragement goals,’ however, MIPA can be used to force absent or unwilling parties to pool in the right circumstances.”).

are met to satisfy affected parties' procedural due process rights, the RRC, under the plain language of § 102.011, has authority to force-pool mineral interests into a MIPA drilling unit.²⁷⁸ Such a compulsory pooling order protects the correlative rights of small, unleased mineral owners because, once pooled, they will receive compensation for minerals produced from the entire pooled area.²⁷⁹ This provides greater protection for unleased mineral owners than under the current Rule 37 dominated framework where unleased mineral owners receive no compensation for minerals drained from beneath their tracts.²⁸⁰ It follows that allowing producers to employ MIPA as an urban field-development tool ensures protection for the correlative rights of small, unleased mineral owners—protection that is absent under the current framework.²⁸¹ Producers will also benefit from a broader interpretation of MIPA's existing language.

Applying the plain language of MIPA benefits producers because, as with most compulsory pooling statutes, producers will have more flexibility in planning urban development, which will increase efficiency.²⁸² Currently, urban producers depend on Rule 37 exceptions when confronted with unleased or unwilling mineral owners.²⁸³ In fact, the RRC expressly encourages producers to use Rule 37 exceptions rather than pursue forced pooling via MIPA.²⁸⁴ Urban development may be contingent upon the ability to obtain Rule 37 exceptions, so the existing emphasis on the exceptions provides little security to producers when planning.²⁸⁵ While Rule 37 exceptions are generally easily obtainable, they do not provide a uniform method for constructing urban production plans—Rule 37 exceptions operate on an individual well-by-well basis.²⁸⁶ Pooling, on the other hand, allows producers to plot development in a more uniform pattern based on the underground geologic characteristics of the producing formation.²⁸⁷ If the plain language of MIPA is interpreted so that urban producers may use MIPA as a tool in planning urban development—as in *Finley*—producers will benefit from added flexibility.²⁸⁸ This allows producers to develop urban fields in a way that minimizes the surface footprint of drilling

278. See § 102.011.

279. See *id.* § 102.051 (providing that compensation among pooled mineral interest owners is, unless the RRC deems otherwise, to be allocated based on the proportion of surface acres owned by the mineral owner compared to the total number of surface acres in the pooled unit).

280. See *supra* notes 237-42 and accompanying text.

281. Blackwell, *supra* note 135, at 27-28.

282. See KRAMER & MARTIN, *supra* note 76, § 10.01, at 10-2.

283. See *supra* notes 222-48 and accompanying text.

284. See *Finley Resources Proposal for Decision*, *supra* note 224, at 2, 9-10.

285. See *supra* notes 222-48 and accompanying text.

286. See *supra* notes 128-33 and accompanying text (discussing the recent, unprecedented rate at which the RRC has granted Rule 37 exceptions); *supra* notes 110-15 and accompanying text (discussing the tests applied by the RRC in analyzing Rule 37 exception applications).

287. See KRAMER & MARTIN, *supra* note 76, § 10.02, at 10-5 to -17.

288. See *Finley Resources Proposal for Decision*, *supra* note 224, at 4-6.

operations and maximizes production from urban fields without jeopardizing the correlative rights of unleased, small-tract mineral owners.²⁸⁹

If the RRC were to adopt a broader interpretation of the existing language in MIPA, the correlative rights of small, unleased mineral owners in urban areas would be better protected and producers would benefit from added flexibility in planning field-development and production.²⁹⁰ Some of the difficulties that currently render MIPA's application cumbersome would still exist as disadvantages.²⁹¹ For instance, MIPA's strict requirement that all efforts to pool voluntarily must be exhausted before applying for a MIPA forced pooling order, and any subsequent MIPA hearings and procedures would still consume considerable amounts of time and resources.²⁹² If, however, the RRC adopted the MIPA interpretation employed in *Finley* as the standard, rather than as a unique circumstance, delays in production would be offset by the added protection—currently absent—of small, unleased mineral owners' correlative rights and the additional flexibility available to urban producers.²⁹³ Should the RRC determine otherwise, another solution might take the form of broad compulsory provisions implemented in the special field rules of individual Texas oil and gas fields.²⁹⁴

C. Incorporate Customized Compulsory Pooling Provisions into the Special Field Rules of Texas's Oil & Gas Fields

One way to strike a balance between replacing MIPA with a new compulsory pooling statute and broadening how the RRC interprets the existing language in MIPA is to incorporate broad, customized compulsory pooling provisions into the special field rules of individual oil and gas fields. Replacing MIPA with a broad, statewide compulsory pooling statute is a drastic measure, one that is unlikely to gain traction, and broadening MIPA's historical interpretation does not provide as much flexibility to urban producers because its use is hindered by its inherently stringent requirements.²⁹⁵ Incorporating compulsory pooling provisions into special field rules would provide a middle road.²⁹⁶ Compulsory pooling provisions, implemented through special field rules, would adequately protect the correlative rights of small, unleased mineral owners and provide producers the flexibility needed to efficiently develop and

289. See *supra* Part II.C.

290. See *supra* notes 267-88 and accompanying text.

291. See Vaughn, *supra* note 171, at 124.

292. See *id.*

293. See *supra* notes 267-88 and accompanying text.

294. See *infra* Part IV.C.

295. See *supra* notes 249-66 and accompanying text (presenting a solution that involves replacing MIPA with broader statewide compulsory pooling statute); *supra* notes 267-93 and accompanying text (presenting a solution that involves interpreting MIPA's existing language more broadly).

296. See *supra* discussion Part IV.A-B.

produce from urban oil and gas fields.²⁹⁷ Notably, this solution would offer those benefits without drastically changing Texas's existing statewide compulsory pooling rules—the new compulsory pooling provisions would only apply within fields that adopt special field rules containing compulsory pooling provisions, and MIPA would still serve as the default statewide compulsory pooling statute.²⁹⁸

Incorporating broad compulsory pooling statutes into special field rules will protect correlative rights generally because all mineral owners—including unleased, small-tract mineral owners—will have the same opportunity to reap the benefits of production from shared mineral formations.²⁹⁹ The existing prevalence of Rule 37 exceptions in urban production does not provide adequate protection for unleased, small-tract mineral owners because the rule of capture precludes recovery for drainage.³⁰⁰ Special field rules with broad compulsory pooling provisions will ensure that unleased, small-tract mineral owners receive compensation for production—just as a broad statewide compulsory pooling provision would.³⁰¹ The advantage that the special field rules option has is that it does not change the default statewide compulsory pooling statute.³⁰² The compulsory pooling provisions would only apply in areas where the RRC specifically adopted those provisions into the applicable special field rules.³⁰³ This allows the RRC to serve its stated purpose of protecting correlative rights generally while still maintaining its traditional stance against broad, statewide compulsory pooling.³⁰⁴ Producers in urban oil and gas fields would also benefit from incorporating compulsory pooling provisions into special field rules.

Urban producers would also benefit from compulsory pooling provisions contained in special field rules because of the added flexibility afforded through compulsory pooling.³⁰⁵ Instead of complying with MIPA's requirement to exhaust all efforts to voluntarily pool before attempting to force-pool under MIPA, producers in urban areas may automatically apply for a compulsory pooling order.³⁰⁶ The facts of the *Finley* case demonstrate the difficult task producers face in attempting to enter into voluntary lease agreements with small-tract mineral owners in urban areas.³⁰⁷ Automatically applying for a

297. See *supra* Part IV.A (discussing the advantages statewide compulsory pooling statutes provide).

298. See *supra* notes 72-80 and accompanying text (noting the reasons for creating special field rules and the statutory authority for doing so).

299. See *supra* text accompanying notes 48-60.

300. See *supra* Part III.B.

301. See *supra* text accompanying notes 251-54.

302. See *supra* notes 72-80 and accompanying text.

303. See *supra* notes 72-80 and accompanying text.

304. See *supra* Part II.F.

305. See *supra* notes 257-72, 282-89 and accompanying text.

306. See *supra* notes 257-72 and accompanying text.

307. See *Finley Resources Proposal for Decision*, *supra* note 224, at 2 (noting that the producer, Finley Resources, spent approximately two years attempting to enter into voluntary lease agreements with twenty-eight small-tract mineral owners near downtown Fort Worth).

compulsory pooling order under the Barnett Shale's special field rules could have potentially decreased Finley's three-year delay in obtaining production by months or even years.³⁰⁸ Accordingly, the ability to automatically apply for compulsory pooling orders under the special field rules of Texas's oil and gas fields will improve producers' efficiency in planning field-development and ultimately maximize production from urban fields.³⁰⁹ The major advantage in equipping special field rules with compulsory pooling provisions is that urban small-tract mineral owners and producers will reap the benefits of compulsory pooling, but the existing statewide policy against compulsory pooling will remain unchanged.³¹⁰

V. CONCLUSION

The system Texas currently uses in dealing with unavailable or unwilling small-tract mineral owners in urban areas fails to protect correlative rights generally, and it fails to provide urban oil and gas producers the flexibility needed to develop oil and gas fields efficiently.³¹¹ Part of the problem is that the existing framework was designed to accommodate vertical oil and gas wells, but production in urban areas is largely conducted using horizontal wells.³¹² Horizontal wells allow producers to traverse through continuous, horizontal portions of oil and gas formations rather than intersecting formations at various points using vertical wells.³¹³ They also decrease the surface footprint of oil and gas development—a major benefit in urban oil and gas production.³¹⁴ But the RRC did not contemplate horizontal wells when it promulgated most of the existing statewide well spacing and pooling regulations.³¹⁵ Texas's traditional adverse stance to broad compulsory pooling—the solution most oil producing states employ in dealing with unleased, small-tract mineral owners—only exacerbates the problem.³¹⁶

Today, producers' preferred method of dealing with unleased, small-tract mineral owners in Texas's urban oil and gas fields is by obtaining Rule 37 spacing exceptions.³¹⁷ They are generally quick to obtain, relatively inexpensive, and favored by the RRC over MIPA compulsory pooling.³¹⁸ This is unfortunate for small-tract mineral owners because, when spacing exceptions are granted, the rule of capture precludes recovery for minerals drained from

308. *See supra* notes 257-72 and accompanying text.

309. *See supra* notes 282-89 and accompanying text.

310. *See supra* notes 302-04 and accompanying text.

311. *See supra* Part III.

312. *See Camp, supra* note 67, at 3.

313. *See supra* Part II.C.

314. *See supra* Part II.C.

315. *See Camp, supra* note 67, at 3.

316. *See supra* Part II.F.

317. *See supra* Part III.A.

318. *See supra* notes 122-27, 222-38 and accompanying text.

unleased tracts.³¹⁹ This issue is especially acute due to the unprecedented rate at which the RRC is granting Rule 37 exceptions and the recent exponential increase in the number of producing horizontal wells in urban areas.³²⁰ Even if producers wanted to force-pool unleased mineral owners rather than pursue Rule 37 exceptions, the RRC has specifically stated that Texas's existing compulsory pooling statute—MIPA—is not intended to afford producers flexibility in development and should not normally be used as a tool in that regard.³²¹ MIPA is traditionally viewed as limited in scope to allow owners of small tracts to “muscle in” to existing productive units rather than as a broad provision that protects the correlative rights of all mineral owners and affords producers flexibility in development.³²² That traditional interpretation does not protect unleased, small-tract mineral owners in urban fields because the act was not designed to accommodate horizontal drilling in urban areas.³²³ Urban producers are not benefitted by the existing framework either—neither Rule 37 exceptions nor MIPA provide the flexibility in field-development necessary in order to efficiently produce the maximum amount of hydrocarbons from urban formations.³²⁴ The most effective way to solve the problem, both for unleased, small-tract mineral owners and for urban producers, is to implement a broader form of compulsory pooling.³²⁵ The Texas Legislature and the RRC need only to decide which form to implement.³²⁶

Each of the proposed solutions presented in Part IV effectively protects the correlative rights of unleased, small-tract mineral owners and affords producers flexibility in urban oil and gas development.³²⁷ Each option carries its own benefits and drawbacks, but the net outcome under each solution is an improvement over the current framework.³²⁸ The most effective and least drastic option is to incorporate broad compulsory pooling provisions into the special rules of individual Texas oil and gas fields.³²⁹ That way, the correlative rights of urban, small-tract mineral owners receive protection—the type of protection well-spacing regulations are promulgated to serve—and producers retain the developmental flexibility needed in order to efficiently produce from urban oil and gas formations.³³⁰ The special field rules option provides a

319. *See supra* Part III.A-B.

320. *See supra* notes 128-32 and accompanying text (noting that the RRC granted an annual average of 582 Rule 37 exceptions from 1919 through 2005 and granted an annual average of 3,916 Rule 37 exceptions from 2006 through 2011). For comparison, the number of producing horizontal wells in the Fort Worth area alone grew from 75 in 2003 to 2,901 in 2008. *See Powell Shale Digest, supra* note 132.

321. *See Finley Resources Proposal for Decision, supra* note 224, at 9-10.

322. *See SMITH & WEAVER, supra* note 205, § 12.1(B), at 12-5.

323. *See supra* notes 275-76 and accompanying text.

324. *See supra* Part IV.

325. *See supra* Part IV.

326. *See supra* Part IV.

327. *See supra* Part IV.

328. *See supra* Part IV.

329. *See supra* Part IV.C.

330. *See supra* Part IV.C.

middle road because it affords the benefits of a broad compulsory pooling provision without drastically altering traditional statewide policy.³³¹ Ultimately, implementing a broader compulsory pooling provision, no matter the form, fulfills the functions and duties the RRC was charged to serve—preventing waste and protecting correlative rights—better than the existing interplay between Rule 37 exceptions and MIPA.³³²

331. *See supra* Part IV.C.

332. *See supra* note 60 and accompanying text; *supra* Part II.A.