

Editor's note: overruled prospectively -- See 99 IBLA 53, 94 I.D. 394 (Sept. 8, 1987).

CONOCO, INC.

IBLA 84-923

Decided February 28, 1986

Appeal from a decision of the Wyoming State Office, Bureau of Land Management, holding that lease W-87877 is continued for a fixed 2-year term and so long thereafter as oil or gas is produced in paying quantities.

Reversed.

1. Oil and Gas Leases: Communitization Agreements -- Oil and Gas Leases: Extensions -- Oil and Gas Leases: Unit and Cooperative Agreements

Where a producing unit agreement terminates after the conclusion of the primary term of the parent lease and part of the lands in the parent lease are simultaneously committed to a second producing unit, thereby effecting a segregation of the parent lease, the term of the nonunitized lease without production shall be for so long as oil or gas is produced in paying quantities upon the unitized lease, but not less than 2 years, and so long thereafter as oil or gas is produced in paying quantities on the nonunitized lease.

APPEARANCES: Floyd E. Radloff, Esq., Houston, Texas, for appellant.

OPINION BY ADMINISTRATIVE JUDGE IRWIN

Conoco, Inc., has appealed from a decision of the Wyoming State Office, Bureau of Land Management (BLM), dated August 23, 1984, holding that lease W-87877 is continued in effect through September 1, 1985, and so long thereafter as oil or gas is produced in paying quantities. This decision amended an earlier decision of BLM, dated March 7, 1984, holding that this lease is extended for as long as oil or gas is produced in paying quantities under unitized lease W-40794 or through September 1, 1985, if production ceases prior thereto on W-40794.

An understanding of the issue in this appeal must begin with the issuance of lease W-40794 for a 10-year period commencing September 1, 1973. 1/

1/ This lease was first issued to G. L. Wilbanks on Aug. 28, 1973, with an effective date of Sept. 1, 1973. An assignment of this lease to Conoco was approved effective Oct. 1, 1973.

Within a year, lease W-40794 was partially committed to the Spearhead Ranch Unit, causing a segregation of this lease into two leases. Those lands unitized (800 acres) retained lease serial number W-40794. The lands not unitized need not concern us.

In February 1981, BLM informed Conoco that the lease account for W-40794 had been transferred to Geological Survey by virtue of the partial commitment of lease W-40794 to the producing Spearhead Ranch Unit. The notice further stated that all or part of the land in lease W-40794 was within an undefined known geologic structure.

In March 1981, Geological Survey acknowledged the contraction of the Spearhead Ranch Unit pursuant to section 2(e) of the unit agreement. Lands eliminated from the unit were outside the Frontier Formation participating areas A and B. Part of lease W-40794, consisting of acreage in secs. 27 and 28, 2/ was eliminated; the remaining part, consisting of acreage in sec. 26, 3/ was retained in the unit.

Effective September 1, 1983, the Spearhead Ranch Unit was terminated as to all acreage in sec. 26, 4/ and this acreage was simultaneously committed to the Powell Pressure Maintenance (Powell) Unit. 5/ The commitment of this acreage in sec. 26 to the Powell Unit, a producing unit, caused a further segregation of lease W-40794 into two leases. The acreage in sec. 26 and now within the Powell Unit retained serial number W-40794. The acreage in secs. 27 and 28 eliminated from the Spearhead Ranch Unit by its 1981 contraction received serial number W-87877. It is lease W-87877 that is the focus of this appeal.

The entire text of the decision on appeal follows:

Decision of March 7, 1984, Amended

Oil and gas lease W-40794 issued with an effective date of September 1, 1973, was committed to the Spearhead Ranch Unit on August 9, 1974, and held by production in that unit until eliminated from the unit effective September 1, 1983, thereby extending the lease through September 1, 1985. Therefore, the lease

2/ More specifically, the NE 1/4 sec. 27 and the NE 1/4, W 1/2, SW 1/4 SE 1/4 sec. 28, T. 39 N., R. 74 W., sixth principal meridian, were eliminated. 3/ The S 1/2 NW 1/4 and SE 1/4 SW 1/4 sec. 26, T. 39 N., R. 74 W., sixth principal meridian, were retained.

4/ By letter dated Aug. 31, 1983, BLM approved the termination of the Spearhead Ranch Unit agreement as it applies to all lands and formations covered by participating area B for the Frontier Formation and the initial participating area A for the third bench of the Frontier Formation. Sec. 26 was included in participating area B.

5/ This unit is known more formally as the Powell (First Bench of the First Frontier Formation) Pressure Maintenance Unit. Sec. 39 of the Powell Unit agreement is quoted in the record as providing for the simultaneous merger into the Powell Unit of those lands described in the preceding note.

was not extended by production on September 1, 1983, when segregated by the Powell Pressure Maintenance Unit -- the lease had a fixed term, September 1, 1985.

Consequently, lease W-87877 (segregated out of W-40794) will continue in effect, unless relinquished, through September 1, 1985, and so long thereafter as oil or gas is produced in paying quantities, but not so long as oil or gas is produced under the unitized lease. [Emphasis in original.]

Appellant opposes BLM's conclusion that lease W-40794 was not extended by production on September 1, 1983, and contends that this conclusion ignores the spirit of the Mineral Leasing Act, 30 U.S.C. § 181 (1982), encouraging unitization. Conoco seeks an extension of lease W-87877 for so long as oil or gas is produced under lease W-40794.

To understand what happens when a lease is partially committed to a unit and when a unit terminates, 30 U.S.C. § 226(j) (1982) must be examined. That section states in part:

Any * * * lease * * * which has heretofore or may hereafter be committed to any such [unit] plan that contains a general provision for allocation of oil or gas shall continue in force and effect as to the land committed so long as the lease remains subject to the plan: Provided, That production is had in paying quantities under the plan prior to the expiration date of the term of the lease. Any lease heretofore or hereafter committed to any such plan embracing lands that are in part within and in part outside of the area covered by any such plan shall be segregated into separate leases as to the lands committed and the lands not committed as of the effective date of unitization: Provided, however, That any such lease as to the nonunitized portion shall continue in force and effect for the term thereof but for not less than two years from the date of such segregation and so long thereafter as oil or gas is produced in paying quantities.

* * * * *

Any lease which shall be eliminated from any such approved or prescribed plan * * * and any lease which shall be in effect at the termination of any such approved or prescribed plan * * * shall continue in effect for the original term thereof, but for not less than two years, and so long thereafter as oil or gas is produced in paying quantities. [Emphasis supplied.]

Although the statute offers considerable guidance, it does not say what happens when unit termination and partial commitment occur simultaneously after the conclusion of the primary term, as here.

BLM's decision granting only a 2-year term to lease W-87877 unless oil or gas is produced in paying quantities encourages prompt development

of the 680 acres in this lease. See Conoco, Inc., 80 IBLA 161, 166, 91 I.D. 181, 184 (1984). In the absence of production in paying quantities on lease W-87877 or further unitization, the term of this lease is limited to 2 years. No production from outside this lease will affect its term, assuming the lease is not itself unitized.

On the other hand, to grant to lease W-87877 a term coextensive with production on lease W-40794 and in no case less than 2 years, as appellant urges, encourages unitization. The statute provides that the purpose of unitization is to more properly conserve the natural resources of any oil or gas pool, field, or like area. 30 U.S.C. § 226(j) (1982). This is accomplished by permitting the entire field (or a very substantial portion of it) to be operated as a single entity without regard to surface boundary lines. 6 H. Williams & C. Meyers, Oil & Gas Law § 901 (1984). Greater recovery at less cost can be achieved when the field is treated as an entity and wells are located to maximize the use of reservoir energy. Although desirable during primary production, unitization is virtually mandatory in secondary recovery operations where the location of input wells, the freedom to flood out parts of the reservoir, and the sharing of costs are vital to the success of the program. Id. 6/

It has been the consistent policy of the Department and of Congress since the enactment in 1931 of unit operation legislation to encourage unitization. Solicitor's Opinion, M-36518 (July 29, 1958); see Solicitor's Opinion, "Interpretation of the Mineral Leasing Act of February 25, 1920," 56 I.D. 174 (1937). Indeed, "extremely favorable treatment" has been accorded to the nonunitized portion of a lease that has been segregated during its extended term 7/ by partial commitment. This

6/ "Unitization is the agreement to jointly operate an entire producing reservoir or a prospectively productive area of oil and/or gas. The entire unit area is operated as a single entity, without regard to lease boundaries, and allows for the maximum recovery of production from the reservoir. Costs are reduced because the reservoir can be produced by utilizing the most efficient spacing pattern, separate tank batteries are not necessary, and there is no requirement to drill unnecessary offset wells. The objective of unitization is to provide for the unified development and operation of an entire geologic prospect or producing reservoir so that exploration, drilling and production can proceed in the most efficient and economical manner by one operator."

Cox, "Unitization and Communitization," § 18.01[2], in Law of Federal Oil and Gas Leases, Rocky Mountain Mineral Law Foundation (1985).

7/ While such treatment has also been accorded to the nonunitized portion of a lease segregated during its primary term by partial commitment, segregation at that point produces a different result. In such a case, the term of a nonunitized lease created by partial commitment of the parent lease during the primary term is the remainder of the primary term but not less than 2 years from the date of segregation.

Solicitor's Opinion, M-36543 (Jan. 23, 1959). Moreover, production during the primary term of a lease does not change the character of the existing term of years. Id. Thus, BLM erred in

nonunitized portion is extended for the term of the unitized parent lease as that term exists on the date of segregation. Solicitor's Opinion, M-36349, 63 I.D. 246 (1956). 8/

[1] Had lease W-40794 entered its extended term held by production within the Spearhead Ranch Unit and no Powell Unit been created, all 800 acres in that lease would have been regarded as held by production with an indefinite term. 9/ 30 U.S.C. § 226(j) (1982). Although the facts of this case appear more complicated than in such hypothetical example, all that actually happened to lease W-40794 on September 1, 1983, was the substitution of the producing Spearhead Ranch Unit by the producing Powell Unit and the segregation of this lease. As noted above, the segregation of a lease does not necessarily cause the resultant two leases to have independent terms. 10/ To deny to the 680 acres in lease W-87877 a term coextensive with lease W-40794 is to discourage unitization in such cases where partial commitment and unit termination are simultaneous. Where, as here, no abuse of the Department's policy in favor of unitization is evident, such a denial is contrary to the Department's practice of granting favorable treatment to nonunitized lands segregated from their parent lands during the extended term. BLM's decision of August 23, 1984, is, accordingly, reversed. Moreover, the record reveals that BLM agreed that partial commitment and unit termination occur simultaneously. 11/ Indeed, a file document requesting termination of the Spearhead Ranch Unit states that BLM required that the Spearhead Ranch Unit be terminated as to any lands under that agreement that were to be included in the Powell Unit. 12/

The term of lease W-87877 shall be for so long as oil or gas is produced in paying quantities under unitized lease W-40794, but for not less than 2 years, and if before the expiration of this term production is obtained on lease W-87877, for so long thereafter as oil or gas is produced thereon in paying quantities.

stating that lease W-40794 was "held by production" in the Spearhead Ranch Unit until eliminated on Sept. 1, 1983, if by this phrase BLM meant that the lease was held by production during its primary term.

8/ See also Husky Oil Co., GFS (O&G) BLM-24 (1961).

9/ It is axiomatic that actual production on any lease committed to a unit is constructive production on all other leases within the unit. Yates Petroleum Corp., 67 IBLA 246, 256 (1982). When, in 1981, 680 acres were eliminated from the Spearhead Ranch Unit by unit contraction, no segregation of lease W-40794 occurred. See Marathon Oil Co., 78 IBLA 102, 106 (1983). Thus, these 680 acres remained in lease W-40794 throughout its primary term.

10/ See, e.g., Bass Enterprises Production Co., 47 IBLA 53, 55 (1980); Ann Guyer Lewis, 68 I.D. 180 (1961); Solicitor's Opinion, M-36592 (Jan. 21, 1960.)

11/ Letter of August 31, 1983, to Wexpro Company from the Acting State Director. See Wexpro Co., 90 IBLA 394 (1986).

12/ Request for termination, filed August 30, 1983, to the Director, BLM, from working interest owners in the Spearhead Ranch Unit area.

Therefore, pursuant to the authority delegated to the Board of Land Appeals by the Secretary of the Interior, 43 CFR 4.1, the decision of the Wyoming State Office, dated August 23, 1984, is reversed.

Will A. Irwin
Administrative Judge

We concur:

Bruce R. Harris
Administrative Judge

Franklin D. Arness
Administrative Judge

