January 2016 | Volume 8 | Issue 1

BEATTY & WOZNIAK, P.C.
ENERGY IN THE LAW

IBLA Halts BLM's Attempt to Beef Up Net Revenue

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On December 28, 2015, the Interior Board of Land Appeals (IBLA) set aside a Bureau of Land Management (BLM) decision approving a communitization agreement (CA) which would have increased the net revenue BLM received on the federal lease. A copy of the IBLA decision can be found here.

BLM's Deputy State Director in the Colorado State Office (CSO) approved the CA on June 14, 2013 after several appeals following an initial denial by the Colorado River Valley Field Office. The Hilton family—owner of a 50% fee interest in the minerals in an 80-acre tract in the spacing unit the operator sought to communitize—appealed the approval of the CA because, it argued, the operator had not met the requirements for communitization, namely: (1) the federal lease could not be independently developed and operated without communitization; and (2) the communitization agreement would serve the public interest. Mineral Leasing Act § 17(m).

Attorneys for WPX—the operator of the federal lease in the spacing unit at issue—and BLM asserted that the federal lease could not be independently developed because a producing well existed in the Colorado Oil and Gas Conservation Commission's (COGCC) designated 640-acre spacing unit. Contrarily, the Hiltons claimed that the COGCC's optional drilling pattern indicates that the federal lease can be developed to avoid waste and protect correlative rights.

The IBLA agreed with the Hiltons, and set aside the approval of the CA because the proposed agreement did not pass the two element test set forth in Section 17(m) of the Mineral Leasing Act.

First, the IBLA stated that evidence proved the federal lease could be independently developed. When the CSO approved the CA, it claimed that the federal lease could not be independently developed because a well had already been drilled in the 640-acre spacing unit approved by the COGCC. However, the CSO did not place any significance on the COGCC's prior orders which not only recognized a 640-acre drilling and spacing unit, but *also* granted an option of drilling one well per 10 acres. The COGCC specifically stated that this optional drilling would assure greater recovery of minerals. Consequently, the IBLA found that the federal lease could be developed consistent with an established well-spacing or development program without communitization.

Second, the IBLA stated that approving the CA without considering the 10-acre well-spacing option was not in the public interest because communitization discouraged development by relying on a single well to recover minerals despite the optional 10-acre drilling pattern.

Finally, the IBLA ruled that the Hiltons were a necessary party to the CA. The CSO asserted that the CA need not be signed by all parties because the conditions of the Hilton Lease would be honored. The IBLA stated that such an assertion contradicted established policies in the BLM Communitization Manual without justification. Specifically, BLM policies require non-federal royalty interest owners to either "sign the agreement, be force-pooled by a State order, or be signers of a lease that already contains a force-pooling provision," none of which applied to the Hiltons. Communitization Manual 3160-9.11.F. Notably, the Hiltons' underlying mineral interest proceeds would be reduced under communitization, and the additional net revenue would accrue to the BLM.

In approving the proposed CA, the IBLA found that the BLM only relied on the facts which would result in its desired outcome—an increase in the BLM's net revenue in the spacing unit. The IBLA's insistence that BLM rely on established procedures and consider all facts in the record provides warning that unwarranted communitization will be prevented.

For more information on the IBLA's decision, please contact Michael Cross or Bret Sumner.