

POOLING OF PROPERTIES FOR OIL AND GAS PRODUCTION

Please note: This document is intended only to give a brief general description of oil and gas pooling, and is not to be construed as legal advice. If you are involved in a compulsory pooling matter, you may wish to contact an attorney.



Typical Michigan Oil Well

In the early days of oil and gas production, developers often drilled as many wells as they could on the properties they owned or leased. Each developer was in competition with his or her neighbors and wanted to pump as much oil as possible, as quickly as possible. This often resulted in many more wells than were necessary and in waste of oil and gas resources.

Oil and gas producing states soon took action to address this and other wasteful practices in the oil and gas industry. Michigan enacted what is now Part 615 of the Natural Resources and Environmental Protection Act. Part 615 designates the Director of the

Department of Environmental Quality as the “Supervisor of Wells,” and charges the Department with providing for the orderly and efficient development of Michigan’s oil and gas resources, while preventing damage to other resources, the environment, and public health and safety. Among other things, Part 615 provides for pooling of properties to form drilling units.

What is pooling?

Pooling is the combining of all oil and gas interests in a drilling unit. In most cases, the owners of oil and gas rights in a unit sign a lease with a developer that allows for pooling. If there is more than one developer in a unit, they voluntarily agree on a development plan. Each owner and developer receives his or her agreed upon share of proceeds from oil and gas produced from the unit. However, if an owner refuses to lease, or when two or more developers cannot agree on a plan, Part 615 provides for the Supervisor of Wells to pool the properties of those parties. This is termed “compulsory pooling.”

What is a drilling unit?

A drilling unit is a tract of land with a specified size and shape upon which one well may be drilled into a designated oil or gas reservoir. The purpose of drilling units is to set the optimum spacing and placement of wells, and to give each mineral owner a fair chance to benefit from development of oil and gas under his or her property.

Why compulsory pool?

The purpose of compulsory pooling is to provide for equitable and efficient development of oil and gas while preventing the drilling of unnecessary wells.



Early Oil Development, Bloomingdale

Compulsory pooling prevents the proliferation of wells that would occur if each owner of a separate small tract were allowed to drill a well on that tract. At the same time, it protects an owner from having his or her oil and gas drained without compensation.

How is compulsory pooling done?

Compulsory pooling can only be done by holding a hearing before the Supervisor of Wells. Any owner of a mineral interest in the area proposed to be pooled may participate in the hearing. Based on the hearing testimony, an order may be issued that sets the formula for sharing costs and revenues from a well or wells in the pooled area.

Who can be pooled?

Compulsory pooling may affect the following persons:

Oil and gas developers who have leased mineral rights in the unit but do not voluntarily agree to share the costs of drilling and producing a well. The compulsory pooling order will set the terms for sharing of costs and revenues from the well. The developer may choose to pay in advance his or her share of costs of the well, or to have those costs deducted from his or her revenues. If the developer chooses the latter, he or she is not required to pay any out-of-pocket expenses. However, an additional cost (typically 100 to 300 percent of drilling costs) may be assessed against his or her revenue to compensate the driller for the risk of an uneconomic well.

Mineral owners who do not agree to lease. If pooled, a mineral owner will be subject to the same provisions for revenue sharing and choices for participation in costs as a developer, except that he or she will receive 1/8 of his or her revenue share as a cost-free royalty. The costs of drilling and production are deducted from the remaining 7/8 interest.

Mineral owners who have leased but do not consent to voluntarily pool their interests with others to form a full drilling unit. A compulsory pooling order may pool the interests of such an owner, but does not impose costs or affect his or her royalties.

Can a company drill a well or construct a pipeline on my land if I do not sign a lease and I am compulsory pooled?

A compulsory pooling order does not give a developer the right to drill or otherwise trespass upon the land of an unleased owner. However, the developer may have certain rights of access under other legal provisions.

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