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**STATE OF NEW MEXICO**
**DEPARTMENT OF ENERGY, MINERALS AND NATURAL RESOURCES**
**OIL CONSERVATION DIVISION**

**APPLICATION OF MARATHON OIL PERMIAN LLC FOR COMPULSORY POOLING, EDDY COUNTY, NEW MEXICO**

**Case No. 20865**

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# BTA OIL PRODUCERS, LLC'S POST-HEARING BRIEF

BTA Oil Producers, LLC ("BTA") submits the following Post-Hearing Brief in opposition to Marathon Oil Permian, LLC's ("Marathon's") applications for compulsory pooling.

## I. Introduction

In these cases, Marathon seeks to eviscerate BTA's correlative rights by pooling acreage that BTA controls under a Joint Operating Agreement ("JOA"). BTA acquired the JOA for the purpose of fully developing the N/2 of Section 7 and the NW/4 of Section 8, Township 23 South, Range 29 East in Eddy County (the "Ochoa Acreage"). Marathon has chosen to disregard the JOA in proposing to develop its adjacent acreage in Section 12, and its proposal strands BTA's acreage in the northwest quarter of Section 8. And although Marathon could develop its acreage in a manner that would not impair BTA's correlative rights or strand BTA's acreage, it has elected not to do so. Marathon should not be permitted to ignore the JOA and develop its acreage in a manner that violates BTA's correlative rights and results in waste.

Marathon's applications should also be denied because Marathon failed to engage BTA in a good-faith effort to secure BTA's voluntary participation in Marathon's proposed wells and because granting Marathon's applications would run contrary to the Oil and Gas Act's preference

for voluntary agreements over compulsory pooling and New Mexico's public policy regarding the enforcement of contracts. The JOA is a voluntary agreement that should be honored.

Further, the reasonable expectations of the parties require denial of Marathon's applications. BTA, through the JOA, has secured 100% of the working interest in its acreage, while Marathon acquired its interests after BTA acquired the JOA and with knowledge that its development plan was contingent on obtaining BTA's participation or pooling BTA's acreage. Marathon's request that the New Mexico Oil Conservation Division ("Division") issue an order pooling the Ochoa Acreage is inconsistent with New Mexico law and should be denied.

## II. Factual Background

Pursuant to the JOA, BTA is the operator of the Ochoa Acreage. *See* [11-15-19 Tr. 61:6-20]. 100 percent of the working interest in the lands covered by the JOA is committed to the JOA. *Id.* BTA owns 73 percent of the working interest and Oxy Y-1 Company ("Oxy") owns the remaining 27 percent of the working interest. *Id.* Because all of the working interest owners are committed to the JOA, BTA can develop the Ochoa Acreage without the need for compulsory pooling – and it was precisely the existence of the JOA that made the acreage attractive to BTA. *See* [11-14-19 Tr. 50:22-51:5, 11-15-19 Tr. 66:18-23]. BTA already operates a producing well under the terms of the JOA, has proposed four lateral wells in the Wolfcamp formation, and has present plans to propose further drilling in the Bone Spring formation. *See* [11-15-19 Tr. 64:10-19]. BTA intends to fully develop the Ochoa Acreage under the JOA. *Id.* BTA's development plans are based on extensive experience and expertise in the Loving area of Eddy County, where it is an active and successful operator. *See* [11-15-19 Tr. 66:18-23, 85:14-86:23].

Approximately five months after BTA acquired the JOA, Marathon acquired its interests in adjacent tracts. *See* [11-14-19 Tr. 50:2-5]. Although Marathon could drill one-mile lateral wells

in its adjacent acreage in Section 12 without impairing BTA's correlative rights, it has chosen to pursue a development plan that requires it to pool a significant portion of the Ochoa Acreage. *See* [11-14-19 Tr. 50:5-51:23, 54:1-55:18]. Marathon's proposal also strands BTA's acreage in the northwest quarter of Section 8. *See* [11-14-19 Tr. 50:2-5, 74:25-75:7]; *see also* BTA Exhibit 1.

Marathon failed to negotiate with BTA in good faith to reach an amicable solution prior to filing its applications for compulsory pooling. *See* [11-15-19 Tr. 65:10-66:23]. After receiving Marathon's well proposal, BTA initiated discussions with Marathon, hoping to reach a voluntary agreement. *See id.* The discussions between the parties resulted in Marathon making one offer to BTA whereby BTA would swap its operating interests in the area for other operating interests held by Marathon. *Id.* BTA reasonably rejected the offer because it did not view the acreage that Marathon proposed to trade as geologically comparable. [11-15-19 Tr. 66:12-23]. Although BTA and Marathon discussed other potential trades, Marathon made no further offers to BTA. [11-15-19 Tr. 66:24-67:1, 82:1083:5]. BTA has not proposed additional trades to Marathon because it does not know what acreage Marathon owns. *Id.* Marathon now asks the Division to extinguish BTA's operating rights under the JOA, rendering the JOA meaningless and nullifying BTA's correlative rights.

## III. Argument

### A. The applications should be denied because Marathon's proposal would impair BTA's correlative rights.

"The Oil Conservation Commission is a creature of statute, expressly defined, limited and empowered by the laws creating it. The commission has jurisdiction over matters related to the conservation of oil and gas in New Mexico, but the basis of its powers is founded on the duty to prevent waste and to protect correlative rights." *Continental Oil Co. v. Oil Conservation Commission*, 1962-NMSC-062, ¶ 11, 70 N.M. 310. Here, granting Marathon's applications would

destroy BTA's correlative rights in the acreage subject to the JOA. Marathon, on the other hand, is seeking compulsory pooling in an attempt to mitigate risks it knew were inherent in the acreage when it was acquired, which is an improper use of compulsory pooling.

As explained above, BTA controls 100% of the Ochoa Acreage under the JOA and acquired the JOA precisely because it wanted to develop the acreage. BTA acquired its interests in a trade with EOG for the purpose of fully developing the Bone Spring and Wolfcamp formations underlying the Ochoa Acreage. The acreage is particularly desirable because it can be developed from a surface location outside of the Potash Area.

At the hearing in this matter, Marathon suggested that because BTA would become a non-operating revenue recipient if the applications are granted, BTA's correlative rights would not be impaired. This position is untenable – if correlative rights only encompass the right to passively receive revenue, there would be no basis for the Division to deny an application for the sake of protecting those rights. Correlative rights, in fact, encompass a much broader concept and are defined as "the opportunity afforded, so far as it is practicable to do so, to the owner of each property in a pool to produce without waste the owner's just and equitable share…" 1978 NMSA, § 70-2-33(H).

In determining what is meant by a "just and equitable share," courts generally agree that a person's correlative rights include more than the right to simply receive a pro rata share of production. Texas courts, for example, have found that proration based only on acreage is not sufficient to ensure each party receives a just and equitable share – consideration must be given to the different burdens placed on the respective parties. *See, e.g. Coleman v. Railroad Commission*, 445 S.W.2d 790, 797 (Tx. Ct. App. 1969) ("[I]t should be pointed out that determining whether or

not an offer meets the statutory test of being fair and reasonable, etc., would ordinarily require consideration of more than the acreage of the owners.").

The Supreme Court of Oklahoma has held that the measure of a just and equitable share is the present market value of the *right to drill* on a tract of land. *See Home-Stake Royalty Corp. v. Corporation Commission,* 594 P.2d 1207, 1210 (Okla. 1979). Oklahoma's interpretation of "just and equitable" in this context is particularly instructive. Oklahoma is both a major oil-producing state and a state with a compulsory pooling regime similar to New Mexico's. *See* U.S. ENERGY INFORMATION ADMINISTRATION, THE DISTRIBUTION OF U.S. OIL AND NATURAL GAS WELLS BY PRODUCTION RATE B43 (2019) (indicating there were 15,077 horizontal wells in Oklahoma as of December 2019); Okla. Stat. § 165:5-7-7, *et seq.*; § 165:5-15-3, *et seq.* By placing the right to drill at the center of the correlative rights inquiry, the rule recognizes that the right to develop one's resources is the very heart of a person's correlative rights. New Mexico's statutory language makes this clear as well by stating that correlative rights include "the opportunity…to produce…the owner's just and equitable share." § 70-2-33(H). Thus, the right to actually direct the development of the mineral estate is part of – and the very core of – BTA's correlative rights.

This fact underscores the severe damage to BTA's correlative rights that Marathon's applications would cause. BTA is not a mineral owner in the area by happenstance. BTA is a company actively engaged in drilling operations and the production of oil – it acquired its interests under the JOA for the express purpose of developing the acreage and specifically contracted for the operating rights. In addition to the considerable resources expended to acquire the interest and operating rights, BTA has invested substantial time and money in forging its own development plan. Loss of its opportunity to produce would mean loss of these investments, loss of business, and loss of revenue to BTA.

Marathon should not be permitted to impair BTA's correlative rights by precluding BTA from developing the Ochoa Acreage under the JOA. This is especially true given that Marathon admitted it could develop its acreage without impairing BTA's correlative rights by drilling one-mile lateral wells in Section 12. The Division should not allow Marathon's development choice to render the JOA meaningless.

**B. Marathon's applications should be denied because they would result in waste.**

The Oil and Gas Act precludes development that would result in waste, which includes "the locating, spacing, drilling, equipping, operating or producing, of any well or wells in a manner to reduce or tend to reduce the total quantity of crude petroleum oil or natural gas ultimately recovered from any pool . . ." NMSA 1978, §§ 70-2-2 and 70-2-3(A). As explained above, Marathon's pooling applications would result in waste by stranding BTA's acreage in the northwest quarter of Section 8. Because Marathon's applications would result in waste, they should be denied.

**C. The applications should be denied because Marathon failed to make a good-faith effort to secure BTA's voluntary participation in the proposed wells.**

New Mexico law and Division precedent require parties to make a good-faith effort to secure voluntary participation prior to seeking a compulsory pooling order. *See* 1978 NMSA, § 70-2-18(A) (obligation of operator to seek voluntary agreements). The factual record in this case demonstrates that Marathon did not make a good faith effort to secure BTA's voluntary participation in its proposed wells. In fact, BTA is the only party who has made a good faith effort to resolve this matter.

As explained above, Marathon did not contact BTA prior to sending its well proposal letters and after the well proposals were sent, BTA initiated a meeting with Marathon. BTA's representatives traveled to Marathon's office in Houston, Texas in an attempt to find a solution

that was acceptable to all parties involved, including a trade or that Marathon drill one-mile laterals. None of BTA's proposals were acceptable to Marathon, who ultimately proposed swapping BTA's operating interest in the lands subject to the JOA for less desirable operating interests in a geologically dissimilar area. Although BTA was willing to consider additional proposals, Marathon never made them.

Marathon's proposal to trade less desirable acreage for BTA's acreage was not a good faith offer. Marathon knows that BTA is an operating company that specifically chose the acreage under the JOA because of BTA's expertise and past success in the area. Marathon's disregard for BTA's rights under the JOA is underscored by the fact that it made no subsequent offers. Under these circumstances, the Division cannot conclude that Marathon made anything other than a perfunctory effort to secure BTA's voluntary participation. *See The Comparisons, Contrasts, and Effects of Compulsory Pooling Statutes,* 28 RMMLF-INST 15 (1982) ("At a minimum, it seems that the person requesting compulsory pooling should be required to show that he has made a firm, fair, and reasonable offer in writing to all parties. Ideally, the terms of the offer should be identical with the terms which the applicant requests the agency to fix."); *see also Railroad Comm'n of Texas v. Pend Oreille Oil & Gas Co., Inc.*, 817 S.W.2d 36, 40 (Tex. 1991) (an offer must consider the facts relevant to the party who may enter into the voluntary agreement).

Here, Marathon's offer was decidedly unreasonable. Marathon asked BTA to exchange the Ochoa acreage for less desirable acreage. And Marathon only agreed to a meeting after BTA asked for one and refused to make any follow-up offers even though BTA did not indicate that additional offers would be futile. Marathon's failure to negotiate with BTA in good faith prior to seeking compulsory pooling warrants denial of Marathon's applications.

**D. Granting Marathon's applications would run contrary to the purposes of the Oil and Gas Act and New Mexico public policy by discouraging voluntary agreements.**

The statutory scheme created by the New Mexico Oil and Gas Act favors voluntary agreements over compulsory pooling. This is evident in Section 70-2-17's prohibition of compulsory pooling when the parties have entered into a voluntary agreement and is also evident in the requirement that a party seeking a compulsory pooling order must first attempt to secure the voluntary participation of the parties it seeks to pool.

In this regard, the Oil and Gas Act is no different from the law in general, which favors voluntary agreement over government action. *See, e.g., Attorney General of the State of New Mexico v. New Mexico Public Service Commission*, 1991-NMSC-021, ¶ 13, 111 N.M. 636 ("a cooperative approach in reconciling the interests of the parties was consistent with the public policy favoring settlement of disputes."). New Mexico's courts have long recognized that "public policy favors freedom to contract and enforces contracts that do not violate law…" *McMillan v. Allstate Indemnity Co.*, 2004-NMSC-002, ¶ 10, 135 N.M. 17. The heavy weight given to private contracts has been described by our Supreme Court as "The paramount public policy…" *Tharp v. Allis-Chalmers Manufacturing Co.*, 1938-NMSC-044, ¶ 13, 42 N.M. 443. To this end, a private agreement should only be voided by government action "in cases free from doubt." *Id.*

Here, granting Marathon's applications would void the JOA and run afoul of this important public policy. BTA's extensive efforts to develop its acreage entirely through voluntary agreement would be rendered meaningless and the Division would be incentivizing the offensive use of compulsory pooling, rather than subordinating government action to the preferred method of private negotiation. Further, the invalidation of the JOA would result in instability and discourage development in violation of the Oil and Gas Act. The existence of the JOA is not only relevant to

the Division's decision but requires denial of Marathon's applications. Section 70-2-17, in conjunction with New Mexico's public policy of encouraging and enforcing voluntary agreements, demonstrates the longstanding and consistent policy in favor of voluntary agreements that permeates the Oil and Gas Act and New Mexico law in general. This public policy runs directly contrary to extinguishing BTA's rights under the JOA.

**E. Marathon's argument that the JOA is irrelevant lacks merit.**

At the hearing in this matter, Marathon argued that Order No. R-14140 in Case No. 15433 is directly on point and favors granting Marathon's applications. Marathon further argued that based on this precedent, BTA's JOA is irrelevant to Marathon's compulsory pooling applications. Marathon's argument that the existence of a JOA is irrelevant is based on a misapprehension of both the law and the facts.

Order No. R-14140 is inapposite. In that case, Nearburg sought to dismiss Matador's compulsory pooling application based on the existence of a JOA. Nearburg did not present evidence or argument that it was the designated operator under the JOA or that pooling would impair its correlative rights or result in waste, and the Division did not address those issues. *See Nearburg's Motion to Dismiss* filed in Case No. 15433; Order No. R-14140. Thus, the case has no bearing here, where BTA has presented evidence that it is the designated operator under the JOA and that granting Marathon's applications would impair its correlative rights and result in waste.

As explained above, granting Marathon's application would impair BTA's correlative rights by rendering the JOA meaningless. This result is contrary the Oil and Gas Act and New Mexico public policy, which express a strong preference for voluntary agreements. Further, BTA presented evidence that it acquired the Ochoa acreage for the sake of fully developing it, without the need for compulsory pooling – BTA is not a holdout landowner stalling the efficient

development of the mineral estate. Marathon's argument that the JOA is irrelevant lacks merit and should be rejected.

### F. The reasonable expectations of the parties require denial of Marathon's applications.

The Division is charged with ensuring that its pooling orders are issued "upon such terms and conditions as are just and reasonable..." § 70-2-17(C). Marathon's applications are neither. The facts show that: (A) Marathon acquired its interest after BTA acquired its interests subject to the JOA; (B) Marathon could develop its acreage in a manner that would protect BTA's correlative rights but has elected not to do so; and (C) Marathon has not negotiated with BTA in good faith. BTA, on the other hand, acquired a 100% working interest in its acreage through the JOA and has present plans to fully develop its position without the need to pool adjacent mineral owners.

Under these circumstances, Marathon's proposal is neither just nor reasonable. It is unjust and unreasonable for one operator to pay a premium for operating rights and complete control of an area, only for another operator to later purchase neighboring interests and insist that the first operator abandon its plans and investments. This is especially true given that Marathon could fully develop its acreage without impairing BTA's correlative rights but does not wish to do so. Neither the Oil and Gas Act nor Division precedent permits the result Marathon seeks here.

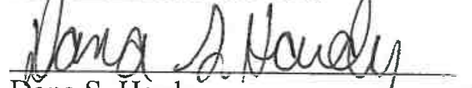
## IV. Conclusion

For the reasons discussed above, the Division should deny Marathon's request that the Division allow Marathon to strand a portion of BTA's Ochoa Acreage and nullify BTA's correlative rights by pooling the acreage that BTA acquired under the JOA. BTA acquired the JOA prior to Marathon's acquisition of the acreage Marathon seeks to pool, and Marathon acquired its acreage with knowledge that it would be required to secure BTA's voluntary participation or pool the Ochoa Acreage. Marathon also failed to negotiate with BTA in good faith prior to seeking

compulsory pooling. The Oil and Gas Act and New Mexico public policy preclude compulsory pooling in this circumstance. Marathon's applications must be denied.

Respectfully submitted,

HINKLE SHANOR LLP



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## CERTIFICATE OF SERVICE

I hereby certify that on this 21st day of January, 2020 I served a true and correct copy of the foregoing ***BTA Oil Producers, LLC's Post-Hearing Brief*** on the following counsel of record by electronic mail.

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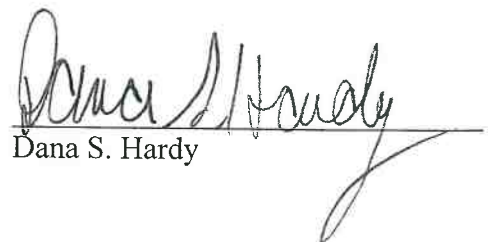

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