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An International Comparison of the Operatorship Provisions Contained in Model Form Oil & Gas Joint Operating Agreements

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An International Comparison of the Operatorship Provisions Contained in Model Form Oil & Gas Joint Operating Agreements¹

Keith B. Hall*

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1. This Article is based in part on a paper entitled *The Operator Under Oil & Gas Joint Operating Agreements—The 3 Rs of Responsibilities, Removal, and Replacement*, which was delivered at the “Special Institute on Joint Operations and the New AAPL Form 610-2015 Model Form Operating Agreement,” a two-day conference hosted by the Rocky Mountain Mineral Law Foundation and the American Association of Professional Landmen on December 5 and 6, 2017, in Denver, Colorado.

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INTRODUCTION

Next to the “granting instrument”²—either an oil and gas lease in the United States and parts of Canada, or a host country agreement elsewhere—probably the most important type of contract governing oil and gas exploration and production rights is the joint operating agreement (often called a “JOA”). A joint operating agreement typically is entered by parties that each own exploration and production rights in the same tract or in nearby tracts that the parties believe should be operated in a coordinated fashion.

Often, the parties to a JOA will co-own exploration and production rights throughout the entire area governed by the JOA under a single granting instrument. This is sometimes the case in the United States, and it is typically the case in other countries, where sovereign ownership of minerals is the general rule and granting instruments may cover large areas.

Other times, the area governed by the JOA consists of multiple, nearby tracts, and different parties to the JOA may own exploration and production rights in different tracts under separate granting instruments. In such cases, the companies holding those rights sometimes enter a JOA

2. The “granting instrument” is the contract or other instrument by which an entity that owns the right to explore for and produce minerals grants the right to conduct exploration and production operations to someone else for a finite length of time. In most countries, the sovereign is the entity that owns oil and gas found naturally in the subsurface, as well as the exclusive right to explore for and produce those substances. In contrast, in the United States and parts of Canada, there is private ownership of minerals. Typically, mineral ownership is part of the bundle of rights that a landowner has. Accordingly, the landowner typically owns the minerals associated with his or her land, unless the landowner (or a predecessor-in-interest) has permanently alienated those rights, creating a “split estate” in which one person owns the land, but another person owns the minerals and the right to explore for and produce them.

to facilitate their joint operation of the separate tracts in a coordinated fashion. Occasionally, different companies will hold operating rights in the same tract, but pursuant to different granting instruments. Or, the exploration and production rights of one (or more) of the parties to the operating agreement may be based on that party's ownership of either the land itself or a severed mineral interest, rather than on holding rights under a granting instrument.

In any of these cases, however, the purpose of the joint operating agreement entered by the parties is to govern the exploration and production process, as well as the parties' rights and duties with respect to one another. Joint operating agreements almost always name one of the parties as the "Operator" and vest that party with the exclusive right to operate the parties' mineral interests in the area where the agreement applies, which is often called the "Contract Area" or something similar.

This Article covers issues relating to the Operator,³ including such topics as the selection of the Operator, the relationship between the Operator and non-operator parties, the duties of the Operator, the standard of care to which the Operator is held, resignation and removal of Operators, the selection of a successor Operator after an Operator resigns or is removed, whether Operators can assign the Operatorship, and the potential right of non-owners (persons who do not own an operating right in the mineral interests covered by the agreement) to serve as Operator.

To some extent, this Article will cover general legal principles and practices relating to the position of Operator, but the Article also will give special attention to how various issues are covered under certain model form joint operating agreements. Such attention is merited because, although some parties draft their own operating agreements, it is very common for parties to use model forms as their joint operating agreements. Further, there are a handful, but only a handful, of commonly used forms. This means that certain model forms are used with sufficient frequency to justify discussion of the forms, but such forms are few enough in number that a comparison of the forms in a law journal article is feasible.

3. Many joint operating agreements capitalize "Operator." When discussing specific provisions of those agreements, it sometimes would be appropriate for this Article to capitalize "Operator," even if the Article was not quoting the provision. On the other hand, when this Article is discussing general principles regarding the position of operator, it probably would be appropriate under rules of grammar to refrain from capitalizing "operator." But in writing this Article, the author found that in some sentences it was difficult to decide whether "Operator" or "operator" was more appropriate. For convenience, "Operator" will henceforth be used throughout the Article except in any quotation that used "operator" or when referring to the reasonably prudent operator standard.

In the United States, the most commonly used model form for onshore joint operations is the AAPL Form 610.⁴ The first version of the Form 610 was the 1956 version. Later versions include the 1977 version, 1982 version, 1989 version, a version of the 1989 form that was modified in 2013 with suggested revisions for use with horizontal wells, and finally the “2015” version, which was released in 2016. This Article often starts the discussion of a particular issue by considering how relevant provisions in the 2015 version of AAPL Form 610 address the issue, after which this Article considers how analogous provisions in earlier versions of the AAPL Form 610 deal with the issue. (The earlier versions of Form 610 remain relevant because parties sometimes use the earlier versions of the forms when entering new agreements and also because many older agreements, which parties entered before the newer versions of the form became available, remain in effect today.) Sometimes, particularly when different model forms take a very similar approach, the examination of some forms will be reserved for footnotes to avoid discussion of multiple very similar provisions in the text of this Article.

The model forms that will be discussed in this Article include the:

- AAPL Form 610 (2015), as well as the 1989, 1982, 1977, and 1956 versions of Form 610, and AAPL 610-HN (a version of the 1989 Form 610 modified for use with horizontal wells)
- AAPL Form 710-2002 (hereinafter, “AAPL 710”) (designed for offshore)
- AAPL Form 810 (2007) (designed for deep water operations) (hereinafter, “AAPL 810”)
- Rocky Mountain Joint Operating Agreement Form 3 (“Rocky Mountain Form 3”)
- CAPL 2007⁵ (a form often used in Canada) (hereinafter, “CAPL”)
- 2012 AIPN Model Form⁶ (a form commonly used internationally)
- UKCS 2009⁷ (a form used on the United Kingdom’s

4. “AAPL” is an acronym for the American Association of Professional Landmen, formerly known as the American Association of Petroleum Landmen. The AAPL has produced a number of model forms, with the most commonly used perhaps being the AAPL Form 610 Model Form Operating Agreements.

5. “CAPL” is an acronym for the Canadian Association of Petroleum Landmen.

6. “AIPN” is an acronym for the Association of International Petroleum Negotiators.

7. “UKCS” is an acronym for the United Kingdom Continental Shelf. “Oil and Gas UK,” a trade group, developed the UKCS 2009 form.

- continental shelf) (hereinafter, “UKCS”)
- AMPLA (an Australian form).

I. THE INITIAL SELECTION OF OPERATOR

As a general rule, it would be inefficient if more than one of the parties to a joint operating agreement attempted to conduct operations.⁸ Accordingly, model form joint operating agreements almost always provide that a single party will be designated as the “Operator,” and only the Operator will have authority to conduct most operations.⁹ This is true

8. David H. Sweeney, *Oil and Gas Joint Operating Agreements: A Comparative World-Wide Analysis* §§ 2.01 and 6.01 (Lexis Nexis 2016); CLAUDE DUVAL ET AL., *INTERNATIONAL PETROLEUM EXPLORATION AND EXPLOITATION AGREEMENTS: LEGAL, ECONOMIC, AND POLICY ASPECTS*, 289 (2d ed. 2009).

9. The 2015, 1989, 1982, and 1977 versions of AAPL Form 610 each provide in Article V.A for the designation of an Operator that will have “full control of all operations.” Similarly, Paragraph 5 of the 1956 version of AAPL Form 610 provides for an Operator that would have “full control of all operations.” *See also* AAPL 710 art. 5.1; AAPL 810 art. 5.1.

In the 2012 AIPN Model Form JOA, Article 4.1 provides for designation of an “Operator” and Article 4.2 provides that the Operator “shall have exclusive charge of Joint Operations, and shall conduct all Joint Operations.”

Clause 6.1 of the AMPLA Form provides for appointment of the “Operator” and Clause 7.2 provides that “the Operator is entitled to have possession and control of all Joint Venture Property and must, either itself or through such third parties as it may engage” perform various tasks, including joint operations.

Section 5.1 of the UKCS Form provides for designation of an “Operator” and Section 6.1 provides that “the Operator has the right and is obliged to conduct the Joint Operations by itself, its agents or its contractors.”

The CAPL Form provides for an Operator that is named in a “Heads of Agreement” to which the joint operating agreement is attached. *See* CAPL art. 3.01; *see also* CAPL art. 1.01 (definition of “Heads of Agreement”). Further, art. 3.01 states that “the Parties delegate to the Operator, on their behalf, management of the exploration, development and operation of the Joint Lands.”

Article 4.1 of Rocky Mountain Form 3 states that the “Operator shall direct and have control of all operations conducted hereunder and shall have exclusive custody of all materials, equipment, and other property owned by the parties.”

Of course, in addition to ensuring that multiple parties do not attempt to conduct operations, it is important to make sure that someone conducts operations. The same clauses that confer exclusive operational authority on the Operator often also impose on the Operator a duty to conduct operations. *See* Section II of this Article.

A potential exception to the general rule that the Operator perform all operations concerns operations in which the Operator chooses not to participate—that is, it chooses not to participate in the cost of a particular operation. Most operating agreements provide for the possibility of operations in which some parties participate and other parties do not. *See, e.g.*, Art. V.B.2 of the 2015, 1989, 1982, and 1977 versions of AAPL Form 610; AAPL Form 710, art. 10.5; AAPL Form 810, art. 8.4; Rocky Mountain Form 3, § 9.3; 2012 AIPN art. 7; AMPLA cl. 13; CAPL arts. 9.03 & 10; UKCS cl. 15. Under some operating agreements, if the

for model forms used in the United States and those used elsewhere. The 2015 version of AAPL Form 610 is a typical example. It states that the Operator “shall conduct and direct and have full control of all operations conducted under this agreement as permitted and required by, and within the limits of this agreement.”¹⁰

Typically, if parties contemplate agreeing to a JOA, they select an Operator prior to executing the JOA as part of their negotiations regarding the JOA (instead of executing a JOA and then selecting the Operator later). Indeed, most standard JOA forms provide a blank for the parties to insert the name of the party designated as Operator. This is the case with the 2015 version of AAPL Form 610. The first sentence of Article V.A of that form begins: “_____ shall be the Operator of the Contract Area....” In the 1989, 1982, and 1977 versions, the first sentence of Article V.A begins exactly the same way.¹¹

The parties to a joint operating agreement usually select the party with the largest working interest to be the Operator,¹² and some model forms

Operator chooses not to participate in a particular operation, the participating parties have the option to request that the Operator perform the work on behalf of the participating parties, but they also have the right to designate one of the participating parties to conduct that particular operation. *See, e.g.*, Art. V.B.2 of the 2015, 1989, 1982, and 1977 AAPL Forms. *See also* AAPL Form 710 art. 4.2; AAPL Form 810 art. 4.2; 2012 AIPN arts. 7.2.E.1 (optional provision) and 7.12.F (optional provision); AMPLA cl. 13.3(a); CAPL cl. 10.04; UKCS cl. 15.2.9.

10. 2015 AAPL art. V.A. Older versions of AAPL Form 610, as well as other model form joint operating agreements, contain similar provisions. In Article V.A., the 1989 and 1982 Forms each stated that the Operator “shall conduct and direct and have full control of all operations on the Contract Area as permitted and required by, and within the limits of this agreement.” Article V.A of the 1979 Form had language that is identical, but for a comma after “limits of.”

11. The first sentence of Paragraph 5 of the 1956 AAPL Form begins: “_____ shall be the Operator of the Unit Area....” Article 4.1 of the 2012 AIPN Form begins: “_____ is designated as Operator...” The AMPLA Form contains a blank for naming the actual Operator in Schedule 1 to the JOA. Article 5.1 of the UKCS form begins: “[] is hereby designated and agrees to act as the Operator.” Article 4.1 of the 2002 AAPL Form 710 begins: “_____ is designated as the Operator of the Lease.” Article 4.1 of the 2007 AAPL Form 810 begins: “_____ is designated as the Operator of the Contract Area.” In Rocky Mountain Form 3, Article 1.5 begins, “‘Operator’ means _____ herein designated as Operator.....”

12. *Texas Oil & Gas Corp. v. Hawkins Oil & Gas, Inc.*, 282 Ark. 268, 668 S.W. 2d 16 (1984) (plaintiff “was to be named the operator of the unit drilling operations in as much as it had a predominant position ...”); Scott C. Styles, *Joint Operating Agreements* 375, in *OIL AND GAS LAW—CURRENT PRACTICE AND EMERGING TRENDS* (Greg Gordon et al. eds., 2d ed. 2010) (“Usually, the JOA member with the largest percentage interest in the JOA will be the operator....”); CLAUDE DUVAL ET AL., *INTERNATIONAL PETROLEUM EXPLORATION AND EXPLOITATION AGREEMENTS*, 289 (2d ed. 2009).

clearly assume that this will be the case.¹³ Commentators have explained that this typical practice is grounded in the rationale that the company with the largest interest will have the greatest motivation to operate prudently and efficiently.¹⁴ Further, the party with the largest ownership interest often desires to be the Operator. Such a desire generally will not be based on hopes of making a profit by serving in the role as Operator. As discussed further in Section IV(C) of this Article, the Operator generally is not entitled to make a profit from its service as Operator, though it is entitled to reimbursement of its expenses. In part, the desire to serve as Operator may arise from the attitude encapsulated in the old adage, “If you want something done right, do it yourself.” But perhaps the primary reason a company might wish to serve as Operator is that the Operator “de facto has much more say” and control of operations than do any of the other parties.¹⁵

Notwithstanding the general tendency to choose the party with the largest ownership interest as Operator, parties are free to agree to the selection of some other company as Operator. Parties sometimes do this, particularly if a company with a smaller working interest has special expertise or if there is some other reason why another company should serve as Operator.¹⁶

13. The AMPLA Form provides that, “if the largest Participating Interest is no longer held by the Operator,” the Operator’s term continues (assuming it does not end for some other reason) “until the Operating Committee determines if and when a new Operator should be appointed.” AMPLA cl. 6.2(c). AAPL Form 710 provides for the possible removal of the Operator if, because of an assignment to a Non-Affiliate, its working interest is reduced to “less than the Working Interest of a Non-operator.” AAPL Form 710 art. 4.4(c). The 2012 AIPN Form provides for the possibility of removing the Operator if its ownership interest falls below a specified fraction. *See* 2012 AIPN 4.10(C). The new 2015 AAPL Form 610 contains a provision whereby the parties can provide for that the Operator will be deemed to have resigned if it loses or transfers more than a specified portion of its ownership interest. 2015 AAPL Form 610 art. V.B.2.

14. David H. Sweeney, *Oil and Gas Joint Operating Agreements: A Comparative World-Wide Analysis* § 6.01 (LexisNexis 2016) (“The party with the largest interest in the contract area is frequently selected as the operator under the theory that this party has the most ‘skin in the game.’”); CLAUDE DUVAL ET AL., *INTERNATIONAL PETROLEUM EXPLORATION AND EXPLOITATION AGREEMENTS: LEGAL, ECONOMIC, AND POLICY ASPECTS* 289 (2d ed. 2009).

15. Scott C. Styles, *Joint Operating Agreements* 375, in *OIL AND GAS LAW—CURRENT PRACTICE AND EMERGING TRENDS* (Greg Gordon et al. eds., 2d ed. 2010).

16. David H. Sweeney, *Oil and Gas Joint Operating Agreements: A Comparative World-Wide Analysis* § 6.01 (LexisNexis 2016).

A. The Requirement that the Operator Generally Must Own an Interest Governed by the JOA

Many joint operating agreements either state or implicitly assume that only a party who owns an interest governed by the agreement may serve as Operator.¹⁷ For example, the 1989 and 1982 Versions of AAPL Form 610 seem to assume that the Operator must own an interest. Those forms state that the Operator will “be deemed to have resigned” if it ceases to own an interest that is governed by the joint operating agreement.¹⁸ AAPL forms 710 and 810, which are designed for use offshore, contain similar language about a “deemed” resignation.¹⁹ The 1977 version of Form 610 states that the Operator will “cease to be Operator” if it no longer owns an interest.²⁰ The 2015 version of AAPL Form 610 expressly states a general rule that the Operator must own an interest, though it recognizes that parties can agree to hire a “contract Operator” that does not own an interest.²¹

Some of the other model form JOAs give parties to the agreement the right to remove the Operator if the ownership interest of the Operator (or, of the Operator and its affiliates together) falls below a specified level. The AMPLA form and the two AAPL offshore forms each provide for the possibility of removing the Operator if the Operator makes an assignment of interest that results in any other party having a larger ownership share than the Operator.²² The 2012 AIPN form contains an optional provision that would allow the Non-Operators to remove the Operator if the combination of the Operator’s interest and its affiliates’ interests falls below a percentage that is to be specified by the parties (the form contains a blank for the parties to fill-in with a percentage). The UKCS form provides that the Operator may be removed if neither it nor its affiliates holds an ownership interest.²³

B. Selecting an Operator that Does Not Own an Interest

In most cases, the parties to a joint operating agreement choose one of the owners of the interest governed by the joint operating agreement to serve as Operator. Occasionally, however, the parties hire a non-owner to

17. Perhaps this is due to some of the same reasons that the parties typically choose the party with the largest interest as Operator.

18. 1989 AAPL 610 art. V.B.1.; 1982 AAPL 610 art. V.B.1.

19. 2002 AAPL 710 art. 4.3; 2007 AAPL 810 art. 4.3.

20. 1977 AAPL 610 art. V.B.1.

21. 2015 AAPL 610 art. V.A.

22. AMPLA cl. 6.2(c); 2002 AAPL 710 art. 4.4(c); 2007 AAPL 810 art. 4.4.1.

23. UKCS cl. 5.3.2(g).

serve as Operator. Such non-owner Operators are sometimes called “contract Operators.” A contract Operator might be a company that is not affiliated with any of the owners, or it may be an affiliate of one of the owners. One of the reasons owners of mineral interests typically avoid the use of contract Operators is a concern that a contract Operator’s interest will not be aligned with the owners, and that the contract Operator’s primary interest will be to make a profit by serving as Operator, rather than to maximize profits for the owners. Such non-alignments of interest can occur in many types of commercial transactions, but that does not diminish the concerns of some owners in the JOA context. The concerns may be lessened somewhat if the contract Operator is an affiliate of one of the owners, but even in those circumstances the concerns may remain.

The pre-2015 versions of AAPL Form 610 do not expressly address whether the initial Operator must own an interest that is governed by the joint operating agreement. But most of the pre-2015 Forms seem to implicitly preclude the selection of a person that does not own an interest under the agreement to serve as the initial Operator (of course parties would be free to agree to deviate from the model language—either by express revision or by simply choosing a non-owning Operator).²⁴

The 2015 AAPL Form makes a change. It recognizes that, as a general rule, the Operator must own an interest, but the parties can agree to a non-owning person serving as Operator.²⁵ The Form provides, however, that before a person that does not own an interest governed by the joint operating agreement can serve as Operator, the person must either enter a separate agreement with the Non-Operators to govern their relationship, or insert Article XVI provisions into the agreement to govern the relationship.²⁶

C. Considerations in the International Context

In the international context, additional considerations may exist. For example, outside the United States, mineral rights are typically owned by the sovereign, rather than by private landowners; and the government reserves the right to approve or disapprove the parties’ selection of an

24. Parties who choose to use an older form but deviate from the implicit requirement that the Operator own an interest should be careful to make clear whether their intent is to waive the ownership requirement for all future selections of successor Operators under their joint operating agreement or just for the initial selection.

25. 2015 AAPL 610 art. V.A.

26. *Id.*

Operator.²⁷ Indeed, the Operator often is named in the instrument by which the government grants companies exploration and production rights.²⁸ Sometimes, the government requires that its national oil company serve as Operator.²⁹

II. DUTIES OF THE OPERATOR

Joint operating agreements typically impose a variety of duties on the Operator. For convenience, these can be grouped into three types of duty: operational, financial, and informational and reporting. Each of these is discussed below.

A. Operational Duties

An earlier section of this Article noted that joint operating agreements give one party, known as the “Operator,” the exclusive authority to operate in order to avoid the inefficiencies and other problems that might arise from duplicative or conflicting operations by different parties.³⁰ It also is important, however, to ensure that someone conducts operations. Accordingly, joint operating agreements typically impose on the Operator a *duty* to operate. The 2015 version of AAPL Form 610 provides an

27. David H. Sweeney, *Oil and Gas Joint Operating Agreements: A Comparative World-Wide Analysis* §§ 6.01 and 6.02 (LexisNexis 2016); Scott C. Styles, *Joint Operating Agreements* 375, found in *OIL AND GAS LAW—CURRENT PRACTICE AND EMERGING TRENDS* (Greg Gordon et al. eds., 2d ed. 2010) (in the U.K., the choice of operator must be approved by government).

28. David H. Sweeney, *Oil and Gas Joint Operating Agreements: A Comparative World-Wide Analysis* § 6.02 (LexisNexis 2016).

29. *Id.* § 6.01.

30. First, these provisions seek to avoid the possibility of duplicative or conflicting operations by different parties by vesting exclusive operating authority in one party. *See* Section I of this Article. Second, these provisions attempt to give the Operator a degree of control over operations that is characteristic of the control that an independent contractor has over the work it is hired to do (as opposed to the lesser degree of control that is held an employee or agent who works under the direction of the principal). For reasons that will be discussed in more detail later, the parties to joint operating agreements often would prefer that the Operator be classified as an independent contractor, rather than as the agent of the Non-Operators. This issue will be discussed in Section IV of this Article.

These clauses typically do this with relatively little discussion, simply declaring that the Operator shall conduct “all” operations or have “exclusive charge” of operations or something similar. 2015 AAPL Form 610 art. V.A (“shall conduct and direct and have full control of all operations”); AAPL Form 710 art. 5.1 (“exclusive right and duty to conduct operations”); AAPL Form 810 (“the exclusive right and duty to conduct (or cause to be conducted) all activities or operations”); 2012 AIPN art. 4.2.A (“exclusive charge”); UKCS cl. 6.1.1 (“the Operator has the right and is obliged to conduct the Joint Operations”).

example. Article V.A, states that the Operator “shall conduct and direct . . . all operations conducted under this agreement.”³¹ Similar or identical language is contained in the earlier versions of AAPL Form 610³² and in other model forms.³³

Joint operating agreements do not specify the particular operations that the Operator must perform. This lack of detail is unavoidable. Because of the uncertainties involved in the exploration, development, and production processes, it is not possible to spell out in detail the particular wells to be drilled or reworked, the specific depth to which wells should be drilled, and so forth. For this reason, many disputes regarding the Operator’s conduct of operations will turn on whether the Operator has complied with certain standards of conduct which are set forth in the JOA (those standards are discussed in Section III of this Article), rather than whether the Operator breached a specific duty.

Nevertheless, some operating agreements specify certain operational duties in slightly more detail. As noted below, these include (1) duties relating to testing, and (2) duties relating to drilling horizontal wells for the distance and to the stratum that was proposed.

1. Duty to Test

Some model forms impose additional, somewhat more specific operational duties. For example, Article V.D of the 2015 Form 610 (entitled “Rights and Duties of Operator”) imposes at least two additional operating duties. Article V.D.7(c) requires the Operator to “adequately test all Zones encountered within the Contract Area which may reasonably be expected to be capable of production of oil and gas in paying quantities as a result of examination of the electric log or any other logs or cores or tests conducted hereunder.”³⁴ This testing requirement is essentially identical to the testing requirement contained in the 1989, 1982, 1977, and 1956

31. Article V of the 2015 AAPL Form is entitled “Designation and Responsibilities of Operator.”

32. 1989 AAPL art. V.A; 1982 AAPL art. V.A; 1977 AAPL art. V.A; 1956 AAPL art. 5.

33. AAPL Form 710 art. 5.1 (“duty to conduct operations”); AAPL Form 810 (“duty to conduct . . . all activities or operations”); 2012 AIPN art. 4.2.A (“shall operate”); UKCS cl. 6.1.1 (“Operator . . . is obliged to conduct the Joint Operations”).

34. “Zones” is defined to mean “a stratum of earth containing or thought to contain a common accumulation of Oil and Gas separately producible from any other common accumulation of Oil and Gas.” 2015 Form art. I.CC.

Forms.³⁵ The CAPL Form also imposes a duty to conduct tests.³⁶ Other forms seem to assume tests will be conducted without expressly mandating a duty to test.³⁷

The model forms that require the Operator to conduct tests do not state with great specificity what tests must be conducted—and any attempt to do so generally would be impractical.³⁸ Accordingly, the resolution of any dispute concerning an Operator's failure to conduct a particular test likely would depend on whether the failure constituted a breach of the standard of care imposed upon the Operator, a breach of an agreement of the parties relating to the testing of a particular well, or the breach of a binding drilling plan.

Disputes can also arise if the Operator conducts a test, but a Non-Operator asserts that the test should not have been conducted or that the test was not done properly. For instance, sometimes Non-Operators object to testing that they think is unnecessary because of concerns over costs or the possibility that testing will damage the wellbore.³⁹ If one or more Non-Operators assert that the Operator incurred excessive expenses by performing a test that was unnecessary or that the Operator performed a necessary test in an improper manner, the dispute would be resolved based on application of the standards of care imposed by the operating agreement (the standard of care imposed by a JOA is discussed in Section III of this Article).

35. The 1989 Form addressed this duty in Art. V.D.7. The 1982 and 1977 Forms addressed testing in Article VI, entitled "Drilling and Development," rather than in Article V. In Article VI.A, the 1982 and 1977 Forms stated: "Operator shall make reasonable tests of all formations encountered during drilling which give indication of containing oil and gas in quantities sufficient to test, unless this agreement shall be limited in its application to a specific formation or formations, in which event Operator shall be required to test only the formation or formations to which this agreement may apply." The 1956 Form addressed the issue in Article 7.

36. CAPL cl. 7.03.

37. See, e.g., AMPLA cls. 1.1 (definition of "Good Australian Oilfield Practice"), 9.1 (discussion of well completion).

38. The CAPL Form, which may contain the most detail regarding testing, states that the Operator must "run agreed log surveys," "test in accordance with the approved program," conduct "such further tests as are warranted of any formations with showings of Petroleum Substances," and "take such mud and drillstem test fluid samples as are appropriate to obtain accurate resistivity, mud filtrate and formation water readings." CAPL cl. 7.03.

39. Andrew B. Derman, *The New and Improved 1989 Joint Operating Agreement: A Working Manual*, 31 (this is No. 15 in the American Bar Association's "Natural Resources, Energy, and Environmental Law Section Monograph Series").

2. Duty to Drill to Objective Zones and to the Proposed Displacement

Article V.D.7(d) of the AAPL Form 610 specifies an additional operating duty:

For any Horizontal Well drilled under this agreement, Operator shall drill such well to the objective Zone(s) and drill the Lateral in the Zone(s) to the proposed Displacement unless drilling operations are terminated pursuant to Article VI.G [relating to circumstances in which drilling operations encounter granite or other practically impenetrable substance or other difficulties] or Operator deems further drilling is neither justified nor required.⁴⁰

In earlier versions of AAPL Form 610, Article V (the Article that contains most of the provisions relating to the Operator, including a specification of the Operator's duties) does not contain any similar language, but the addition of this language to Article V in the 2015 Form may be less of a change than first appears. In some earlier versions of AAPL Form 610, Article VI (which governs provisions relating to drilling operations), the model form stated that the Operator must continue drilling certain wells to the planned depth except in certain circumstances, such as when the drilling encounters impenetrable substances or other problems.⁴¹ Similarly, AAPL 710 provides that the "Operator shall diligently conduct the operation . . . until the Objective Depth, unless the well encounters, at a lesser depth, impenetrable conditions or mechanical difficulties that cannot be overcome by reasonable and prudent operations."⁴² The 2012 AIPN Form contains a very similar provision,⁴³ and the CAPL form places

40. "Lateral" is defined as meaning "that portion of a wellbore of a Horizontal Well between the point at which the wellbore initially penetrates the objective Zone and the Terminus." 2015 Form art. I. "Displacement" is defined having "the same meaning as the term defined by the state regulatory agency having jurisdiction over the Contract Area, in the absence of which the term shall otherwise mean the length of a Lateral." *Id.*

41. 1989 AAPL Form art. 610 art. VI.F; 1982 AAPL Form 610 art. VI.A; 1977 AAPL Form 610 art. VI.A; 1956 AAPL Form 610 art. 7.

42. AAPL Form 710 art. 10.7. In article 2.25, Form 710 defines "Objective Depth" as, "A depth sufficient to test the lesser of the Objective Horizon or the specific footage depth stated in the AFE and approved by the Participating Parties." Form 710's article 2.26 defines "Objective Horizon" as "The interval consisting of the deepest zone, formation, or horizon to be tested in an Exploratory Well, Development Well, Deepening operation, or Sidetracking operation, as stated in the AFE and approved by the Participating Parties." *See also* AAPL Form 810 art. 10.1.4).(b).

43. 2012 AIPN art. 5.13.D.1.

restrictions on an Operator's deviation from the plan approved by the parties for a horizontal well.⁴⁴

B. Financial Duties

Many operating agreements impose upon the Operator various financial duties that are important for purposes of managing the "joint account." Often, operating agreements impose upon the Operator duties to:

- obtain competitive rates for goods and services,
- manage the joint account and discharge its obligations,
- protect the JOA assets against liens, and
- act as a custodian of funds.

The most recent versions of AAPL Form 610 impose each of these duties. As discussed in more detail below, other model forms, used in the United States and elsewhere, impose similar sets of financial duties.

1. Duties to Obtain Competitive Rates

Because the Operator conducts all operations, the Operator typically is the only party to the JOA that enters contracts for the performance of work or for the provision of materials necessary to complete operations. However, all parties to the JOA are responsible for paying their proportionate share of the costs. Accordingly, JOAs typically impose upon the Operator various duties relating to costs.

For example, the 2015 and 1989 versions of AAPL Form 610 require the Operator to ensure that all wells are drilled "on a competitive contract basis at the usual rates prevailing in the area."⁴⁵ Other forms used in the United States⁴⁶ and elsewhere impose similar duties. For instance, the 2012 AIPN form provides parties with a couple of options for the clause

44. CAPL cl. 8.02(B).

45. 2015 Form art. V.D.1; 1989 Form art. V.D.1.

46. AAPL Form 710 art. 5.7 states in part:

Insofar as possible, Operator shall use competitive bidding to procure good and services for the benefit of the parties. All drilling operations . . . shall be conducted by properly qualified and responsible drilling contractors under current competitive contracts. A drilling contract will be deemed to be a current competitive if it (a) was made within_()months before the commencement of the well and (b) contains terms, rates, and provisions that, when the contract was made, did not exceed those generally prevailing in the area for operations involving substantially equivalent rigs that are capable of conducting the drilling operations.

See also AAPL Form 810 art. 5.3; Rocky Mountain Form 3 art. 4(9).

to deal with this issue: Both options require the Operator to choose the “best qualified contractor” based on a combination of cost, quality, and ability, while one of the options would require the Operator to obtain competitive bids for contracts above a certain monetary value.⁴⁷ The AMPLA Form requires the Operator to “obtain, evaluate and accept competitive quotes” for contracts.⁴⁸ The CAPL form states that the Operator “will normally award contracts on a competitive basis” and the UKCS form generally requires the Operator to award contracts on a competitive basis if the cost of the contracts exceed a specified monetary value.⁴⁹

In addition to generally requiring the Operator to secure contracts that contain competitive rates and terms, some model form joint operating agreements contain provisions that are designed to protect the Non-Operators against self-dealing by the Operator. For example, the 2015 and 1989 versions of AAPL Form 610 state that the Operator may use its own tools and equipment in the drilling of wells, but if it does so, the Operator must: (1) charge rates that do not exceed the rates prevailing in the area, (2) obtain the other parties’ written consent to its rates before commencing drilling operations, and (3) perform the work under the same terms and conditions as are customary and usual for that geographic area in contracts of independent contractors.⁵⁰ The 1982 and 1977 Forms impose similar requirements relating to competitive rates and the Operator’s use of its own equipment.⁵¹ The offshore AAPL forms likewise contain such requirements.⁵²

Further, model form joint operating agreements often contain provisions to regulate the costs, as well as other terms and conditions, of any contract that an Operator enters with one of its corporate affiliates.⁵³

47. 2012 AIPN art. 6.7.

48. AMPLA cl. 7.2(c).

49. CAPL cl. 3.03(B); *see generally* UKCS cls. 6.5.4, 6.5.5.

50. 2015 AAPL Form 610 art. V.D.1.

51. 1982 AAPL Form 610 art. V.D.1; 1977 Form art. V.D.1.

52. *See* 2002 AAPL Form 710 art. 5.7; *see also* 2007 AAPL Form 810 art. 5(3).

53. The 2015 and 1989 versions of AAPL Form 610 do not expressly give the Operator the right to use one of its own corporate affiliates to perform work or supply materials, but the forms implicitly suggest that the Operator may do so. Those forms state that “[a]ll work performed or materials supplied by an Affiliate of Operator” must meet certain requirements, but the consent of the other parties to the JOA does not appear to be a requirement. The forms state that all such work performed, or materials supplied by an affiliate of the Operator must be done “pursuant to written agreement.” One could argue that this provision means that the Operator must obtain the written consent of the parties to the JOA, but in context the provision appears to mean that anytime the Operator uses one of its affiliates the Operator must do so pursuant to a written contract with the affiliate.

The 2015 version of AAPL Form 610 illustrates this point. To the extent that work is to be performed or materials supplied by an “Affiliate”⁵⁴ of the Operator, the 2015 Form provides that this must be done “at competitive rates, pursuant to written agreement, and in accordance with customs and standards prevailing in the industry.”⁵⁵ This represents a minor change from the 1989 Form. The 1989 Form imposes the substance of this requirement, but it does so with respect to “affiliates or related parties of Operator,” and neither “affiliates” nor “related parties” are defined terms.⁵⁶

The 2012 AIPN Form includes an optional provision which states that “before entering into contracts with Affiliates of Operator exceeding” a specified dollar value, the Operator must obtain the consent of the Operating Committee.⁵⁷ The UKCS Form similarly requires the Operator to obtain the consent of other parties before providing materials or services from its own resources or those of an affiliate, if the costs will exceed a

In contrast to the AAPL Form 610, the 2012 AIPN expressly authorizes the Operator to hire its own affiliates. Article 4.2.A authorize the Operator to “employ independent contractors and agents, including Affiliates of Operator, Non-Operators, or Affiliates of a Non-Operator.” *See also* AMPLA cl. 7.7; *but see* AMPLA cl. 7.10.

54. “Affiliate” is defined to mean:

for a person, another person that controls, is controlled by, or is under common control with that person. For purposes of this definition, “control” means the ownership by one person, directly or indirectly, of more than fifty percent (50%) of the voting securities of a corporation or, for other persons, the equivalent ownership interest (such as a partnership interest), and “person” means an individual, corporation, partnership, trust, estate, unincorporated organization, association, or legal entity.

2015 AAPL Form 610 art. I.

55. 2015 AAPL Form art. V.D.1.

56. 1989 AAPL Form art. V.D.1. Other than the 2015 Agreement’s providing using the defined term “Affiliate” in Article V(D)(1), instead of using “affiliates or related parties,” the financial duties imposed on the Operator by the 2015 Form are the same as those imposed by the 1989 Form. Over time, however, there have been some changes in the COPAS Form that is commonly attached as Exhibit C to the APPL-610 joint operating agreements. This Article does not attempt to address COPAS in detail, much less the changes that have occurred in the COPAS Form over time. Further, any such changes do not change the basic nature of the Operator’s financial duties.

The 1982 and 1977 versions of AAPL Form 610 do not expressly address the use of affiliates of the Operator.

57. 2012 AIPN art. 6.7. The alternative that includes this requirement contains a blank that the parties to the joint operating agreement should fill-in to specify the dollar value that will trigger the consent requirement.

value specified in the JOA.⁵⁸ The AMPLA form states that the Operator may not contract with one of its affiliates (or with a Non-Operator or an affiliate of a Non-Operator) to provide goods or services for joint operations *unless* the contract is on “terms and conditions no less favorable to the [parties to the JOA] than an arm’s length commercial agreement with a Third Party supplier, and the proposed agreement has been approved by the Operating Committee.”⁵⁹

2. Management of Joint Account

Under the 2015 and 1989 versions of AAPL Form 610, the Operator must promptly pay “expenses incurred in the development and operation of the Contract Area pursuant to the agreement,” and charge each of the parties with their respective proportionate shares upon the expense basis set forth in the JOA’s Exhibit C—the standard COPAS provisions.⁶⁰ The Operator must also keep an account record of the joint account, “showing expenses incurred and charges and credits made and received.”⁶¹ In the 1982 and 1977 Forms, financial duties are not addressed in Article V, but Article VI.C requires the Operator to promptly pay costs. The AAPL offshore forms contain similar requirements.⁶²

As with many other issues, Forms used outside the U.S. impose duties similar to those imposed by the AAPL Forms. For example, the 2012 AIPN Form requires the Operator to “timely pay and discharge all costs and liabilities incurred in connection with Joint Operations,” to “exercise

58. UKCS cl. 6.5.2(b). The UKCS Form contains a blank for the parties to fill-in to specify the monetary value of a contract that triggers the requirement to obtain consent from the other parties. *Id.*

59. AMPLA cl. 7.10. The quoted provision refers to the “Operating Committee.” JOA forms used outside the United States often provide for the creation of an operating committee that contains representatives of each party. *See* 2012 AIPN art. 5; AMPLA cl. 5; UKCS cl. 9 (“Joint Operating Committee”). The operating committee typically exercises some authority over budgets and other matters. *See, e.g.,* AIPN art. VI.1.D; AMPLA cl. 8.2; UKCS cl. 10.1.2. Necessarily, the Operator still controls day-to-day matters, but the use of an operating committee may give the Non-Operators more oversight than they have under the various versions of AAPL Form 610, which do not provide for an operating committee.

60. 2015 AAPL 610 art. V.D.2; 1989 AAPL 610 art. V(D)(2). (“COPAS” is an acronym for Council of Petroleum Accounting Societies).

61. 2015 AAPL 610 art. V.D.2; 1989 AAPL 610 art. V.D.2.

62. Each of the two offshore forms requires the Operator to keep accurate books and records. *See* 2007 AAPL Form 710 art. 5.5; *see also* 2002 AAPL Form 810 art. 5.5. Also, by requiring the Operators to seek to keep the contract area free of liens, *see* 2007 AAPL Form 710 art. 5.3; *see also* 2002 AAPL Form 810 art. 5.4, the model forms implicitly require the Operator to promptly pay most expenses.

due care with respect to the receipt, payment and accounting of funds,” and to charge all costs to the Joint Account in accordance with the “Accounting Procedure.”⁶³ The Accounting Procedure, a separate document that is designed to be an exhibit to the JOA, requires the Operator to keep accurate books and records.⁶⁴ Other model Forms used outside the U.S. contain analogous provisions.⁶⁵

3. Protecting JOA Assets Against Liens

Many jurisdictions provide that if a contractor is not paid for its work relating to certain property, such as oil and gas wells or production facilities, the contractor may record a lien giving the contractor a security interest in those facilities.⁶⁶ Individual workers and suppliers of equipment may be entitled to the same or similar protections.⁶⁷ Many joint operating agreements require the Operator to protect the jointly-owned assets against such liens.

For example, under both the 2015 Form and the 1989 Form, the Operator is required: to pay or cause payment of all accounts of contractors and suppliers, as well as all wages and salaries, for all services and materials provided for work under the parties’ agreement; and to keep the area free of liens and encumbrances, except for any which arise from a bona fide dispute as to the services or supplies.⁶⁸ AAPL Forms 710 and 810 impose a similar requirement.⁶⁹

As previously noted, in the 1982 and 1977 Forms, Article V did not address financial duties of the Operator, but Article VI.C generally required the Operator to promptly pay expenses. The 1982 and 1977 Forms did not expressly address protection against liens, except to provide that, with respect to operations by less than all the parties, the Consenting Parties would keep the operations free from liens.⁷⁰

63. 2012 AIPN art. 4.2.B.9; 2012 AIPN art. 4.2.B.3; 2012 AIPN art. 4.2.B.4.

64. 2012 AIPN Model Form International Accounting Procedure § 1.4.1: Operator shall at all times maintain and keep true and correct records of the production and disposition of all Hydrocarbons, of all costs and expenditures under the Agreement, and of other data necessary or proper for the settlement of accounts between the Parties in connection with their rights and obligations under the Agreement to enable Parties to comply with their income tax and other legal and contractual obligations.

65. *See, e.g.*, AMPLA cls. 7.5, 10; UKCS cl. 6.7; CAPL cl. 3.07.

66. *See, e.g.*, Louisiana Oil Well Lien Act, LA. REV. STAT. 9:4861-4873 (2018); N.D. CENT. CODE § 35-24-02 (2017); Oil and Gas Lien Act, N.M. STAT. §§ 70-4-1 to -14 (2018); TEX. PROP. CODE §§ 56.001-56.006 (2017).

67. *See, e.g.*, LA. REV. STAT. § 9:4862(A)(3), (6) (2018).

68. 2015 AAPL 610 art. V.D.3; 1989 AAPL 610 art. V.D.3.

69. 2002 AAPL 710 art. 5.3; 2007 AAPL 810 art. 5.4.

70. 1982 AAPL 610 art. VI.B.2; 1977 AAPL 610 art. VI.B.2.

Various standard forms used outside the United States impose similar duties.⁷¹ Article 4.2.B.9 of the 2012 AIPN form is illustrative. It requires that the Operator “timely pay and discharge all costs and liabilities incurred in connection with Joint Operations and use its reasonable endeavors to keep the Joint Property free from all liens, charges, and encumbrances arising out of Joint Operations.” The standard AMPLA form requires the Operator to “keep the Joint Venture Property free and clear of all Encumbrances, except for those Encumbrances specifically permitted under [the] agreement.”⁷²

4. *Acting as Custodian of Funds*

Article V.D.4 of the 2015 AAPL Form 610 requires the Operator to hold, for the account of the Non-Operators, any money that is paid to the Operator by the Non-Operators or from sales of product from the Contract Area, until such funds are (1) used for their intended purpose, (2) delivered to the Non-Operators, or (3) applied toward debts as allowed under Article VII.B of the agreement.⁷³ (Article VII.B provides that the parties grant liens to one another, and it governs those liens). Until the funds are used or delivered to the Non-Operators, the funds being held by the Operator continue to belong to the Non-Operator on whose behalf the funds were paid or advanced, but the Operator is not required to maintain separate accounts for such funds unless the parties have agreed otherwise.⁷⁴ (Other AAPL forms that address the issue also state that the Operator need not establish a separate account.⁷⁵)

Notably, Article V.D.4 of the 2015 Form suggests that the Operator has a fiduciary duty with respect to any funds that it holds. The provision states: “Nothing in this paragraph shall be construed to establish a fiduciary relationship between Operator and Non-Operators for any purpose other than to account for Non-Operator funds as herein specifically provided.” This suggests that the Operator has a fiduciary duty for the limited purpose of accounting for funds, and by implication this provision reinforces the rule that the Operator does not have a fiduciary duty for most purposes. The 1989 version of AAPL Form 610 has a similar provision.⁷⁶

71. See, e.g., 2012 AIPN art. 4.2.B.9; AMPLA cl. 7.2(o); CAPL cl. 3.06; UKCS cl. 6.3.

72. AMPLA cl. 7.2(o).

73. 2015 AAPL 610 art. V.D.4; 1989 AAPL 610 art. V.D.4.

74. 2015 AAPL 610 art. V.D.4; 1989 AAPL 610 art. V.D.4.

75. 1989 AAPL 610 art. V.D.4; 2002 AAPL 710 art. 8.5; 2007 AAPL 810 art. 6.1.

76. 1989 AAPL 610 art. V.D.4.

The 2012 AIPN form contains an optional provision by which parties can prohibit the Operator from commingling funds it receives from the Non-Operators with the Operator's own funds—thus, effectively requiring the Operator to establish a separate account.⁷⁷ The AMPLA Form requires the Operator to pay costs and expenses incurred by the Operator in operations, and for “such purpose to open, maintain and operate one or more separate bank accounts (with which its own funds are not commingled) on behalf of” the parties to the operating agreement.⁷⁸ The CAPL Form expressly authorizes the Operator to commingle funds, unless parties holding a majority of the Non-Operator ownership interests request otherwise, but the Form apparently anticipates that the Operator will have fiduciary duties with respect to the funds that it holds.⁷⁹

C. Informational and Reporting Duties

Under joint operating agreements, Operators generally have duties to provide various information to regulators and the Non-Operators.

1. Reporting to Regulators

Often, statutes or regulations will require that certain information regarding operations be reported to a government agency. Typically, it would be inefficient and unnecessary for multiple parties to report the same information to regulators, but the parties must ensure that someone submits the information. Further, the Operator often will be in the best position to prepare reports and submit information because the Operator is the party that is handling day-to-day operations. Accordingly, model form joint operating agreements often require the Operator to submit any reports required by law. For example, Article V.D.6 of AAPL's 2015 Form 610 states that the “Operator will file . . . all operational notices, reports or applications required to be filed by local, State, Federal or Indian agencies or authorities having jurisdiction over operations hereunder.” Prior versions of Form 610 imposed a similar duty.⁸⁰

77. 2012 AIPN art. 4.8.A.

78. AMPLA cl. 7.2(e).

79. CAPL cl. 5.07; CAPL cl. 1.05.

80. Article V.D.6 of the 1989 Form expressly imposes such a duty, using language essentially identical to that in the 2015 Form. The 1982 Form does not expressly impose such a duty, but it seems to assume that the Operator will file such forms. Article VI.D of the 1982 and 1977 AAPL Forms describe the extent of the Operator's duty to furnish the Non-Operators with copies of “forms or reports filed with governmental agencies,” thus implying that the Operator will have copies of those forms or reports because the Operator has prepared and filed them.

A difference between the 1989 and 2015 Form is that the 2015 Form expressly designates the Operator as the agent of the Non-Operators:

for the sole purpose of executing, filing for approval by a governmental agency as required under applicable law or regulation, and recording a declaration of pooling or communitization agreement to effectuate the pooling or communitization of the [oil and gas leases subject to the JOA] (to the extent legally allowed under their respective terms and conditions) to conform with a spacing order of a governmental agency having jurisdiction over any portion of the Contract Area. However, such agency shall only be exercised by Operator after providing written notice including a copy of the proposed pooling declaration or communitization agreement to Non-Operators, and shall be binding upon any Non-Operator failing to produce to Operator a written objection with ten (10) days after such notice.⁸¹

Similar to AAPL Form 610, the 2012 AIPN form requires the Operator to provide all records, information, and reports that the granting instrument requires of the parties.⁸² The AMPLA form generally requires the Operator to “prepare, file and lodge all statutory reports as and when required” by law.⁸³ Most other model forms also impose such duties on the Operator.⁸⁴

2. Providing Information to Non-Operators

Because the Operator conducts day-to-day operations, it typically will possess all, or virtually all, information that exists regarding joint operations and will have daily access to physical facilities involved in operations. Non-Operators do not have this advantage, but within the oil and gas industry, the prevailing view is that Non-Operators should have a right to information and access. Accordingly, most operating agreements expressly require the operator to provide information to Non-Operators. But not all information is equally important, and it could be burdensome for the Operator to collect and provide some types of information.

81. 2015 AAPL 610 art. V.A.

82. 2012 AIPN art. 4.2.B.11.

83. 2011 AMPLA cl. 7.2(k).

84. AAPL Form 710 requires the Operator to “make reports to governmental authorities it has a duty to make as Operator.” 2002 AAPL 710 art. 5.8. The intent of this provision probably is that the operator must submit all reports, other than any reports that the law might require each working interest owner to submit (such as income for purposes of income tax reporting). AAPL Form 810, section 5.6 contains a similarly-worded requirement. *See also* 2011 AMPLA cl. 7.2(k); UKCS cl. 6.2.1(g).

Therefore, JOAs typically specify the types of information that the Operator must provide. Similarly, joint operating agreements typically give Non-Operators a right of access to physical facilities to view and inspect them, while imposing some reasonable restrictions or conditions on such access in order to prevent undue interference with operations. Also, it is notable that some JOAs give non-participating parties the right to a narrow set of information and access rights than other parties to the JOA.⁸⁵

The 2015 version of AAPL 610 Form provides that the Operator must:

- notify Non-Operators of the date on which drilling operations are commenced,
- send to Consenting Parties⁸⁶ copies of all test results and reports that they reasonably request,
- permit other parties—either each Non-Operator or each Consenting Party (depending on the particular JOA)—full access to all operations,
- provide other parties—either each Non-Operator or each Consenting Party (depending on the particular JOA)—access to operating records and other books and records relating to each operation, and
- file with regulators all required notices, applications, and reports, and upon request, furnish copies of such filings to Non-Operators.⁸⁷

85. Under most operating agreements, certain operations can proceed without the unanimous consent of the parties. In such situations, each party typically will be given the chance to participate in the project by agreeing in advance to pay its share of costs or to “go non-consent,” and thereby not participate in the costs. When a party elects not to participate and therefore not pay its share of costs, that party generally is required to forego any share to the revenue from that operation—either permanently or until (and unless) the operation is so successful that revenue from the operation exceeds costs of the operation by a specified factor. Typically, non-participating parties do not forfeit all rights to information because they may have a right to share in revenue from the operation eventually, assuming the operation’s revenue exceeds its costs by a sufficient margin, and because the operation in which the party is not participating sometimes may affect other operations under the JOA.

86. A “Consenting Party” is “a party who agrees to join in and pay its share of the cost of any operation conducted under the provisions of this agreement.” 2015 AAPL art. I.D.

87. Article 5.1.F of Rocky Mountain Form 3 requires the Operator to supply a similar set of information.

It also requires the Operator to give the Non-Operators access to physical facilities so that they can observe operations.⁸⁸

A significant change between the 1989 and 2015 versions of AAPL Form 610 is that under the 2015 Form, only Consenting Parties have the right to access well locations and to receive test results, logs, operating records, and most books and records relating to Operations.⁸⁹ In contrast, under the 1989 Form, all Non-Operators were entitled to such access and information.⁹⁰ Even under the 2015 Form, however, Non-Consenting Parties are entitled to production amounts and, if they request an audit, the information necessary to audit “the payout account.”⁹¹ Like the 2015 version of AAPL Form 610, the AAPL offshore forms require the Operator to give a broad range of information to parties participating in an operation, while significantly restricting the scope of information that non-participating parties are entitled to receive.⁹²

The JOA forms used outside the United States similarly require the Operator to provide information to Non-Operators.⁹³ For example, the 2012 AIPN Form requires Operators to provide Non-Operators with: copies of all logs and surveys; the proposed well design and any revisions for each well; daily drilling reports; all tests, core data, and analysis reports; a final well recap report; plugging reports; seismic sections, and if applicable, shot point location maps; final (and if requested, intermediate) geological and geophysical maps, interpretations, and reports; engineering studies; and periodic progress reports.⁹⁴ The 2012 AIPN Form gives non-participating parties the right to some information, but also places some limits on their right to information.⁹⁵

88. 2015 AAPL 610 art. V.D.5; *see also* Rocky Mountain Form 3, art. 5.1.F (giving Non-Operators the right to physical access).

89. 2015 AAPL 610 art. V.D.5.b.

90. 1989 AAPL 610 art. V.D. Like the older versions of AAPL Form 610, the portion of Rocky Mountain Form 3 that requires the Operator to provide information to other parties does not distinguish between participating and non-participating parties. Rocky Mountain Form 3, art. 5.1.F.

91. 2015 AAPL 610 art. V.D.5.a.; 2015 AAPL 610 art. V.D.5.c.

92. 2002 AAPL 710 art. 5.9; 2007 AAPL 810, art. 5.7.; 2002 AAPL 710, art. 5.10; 2007 AAPL 810, art. 5.9.

93. *See, e.g.*, 2012 AIPN art. 4.4.A; AMPLA cl. 7.1; CAPL cl. 7.02; UKCS cl. 6.8.

94. 2012 AIPN art. 4.4.A. The form gives parties the option to specify how often the Operator should provide progress reports.

95. 2012 AIPN art. 7.4.A. The CAPL form likewise gives Non-Operators the right to information and access, CAPL cl. 7.02, but places some restrictions on the access and information rights of non-participating parties. *See* CAPL art. 10.19. The UKCS form follows a similar pattern. *See* UKCS cls. 6.8 (Operator’s duty to provide reports to other parties) and 15.2.8 (the right of parties not participating in “sole risk” operations to some, but not all of the information regarding sole risk operations).

The AMPLA Form does not contain as detailed a list of the information that the Operator must provide, but it nevertheless imposes significant duties to supply information to the other parties. It requires the Operator to submit certain information to the Operating Committee, to provide reports that include “all well and reservoir reports” to “Participants,” and to provide certain information regarding the joint account to any party upon request.⁹⁶ AIPN’s 2012 form also grants Non-Operators the right to have representatives observe operations. Article 4.2.B.8 states:

Upon receipt of reasonable advance notice, [the Operator must] permit representatives of any Party to have at all reasonable times during normal business hours and at such Party’s own risk and cost reasonable access to Joint Operations, to observe Joint Operations, to inspect Joint Property, to conduct HSE audits, and to conduct financial audits and to observe taking of inventory.

III. STANDARD OF CARE

A. The Standard Specified

Most operating agreements expressly impose a standard of care upon the Operator. The specified standard often includes multiple components, with typical components being requirements that the operator perform work as a reasonably prudent operator, in a good and workmanlike manner, consistent with good oilfield practice, and in compliance with applicable laws and regulations. Some forms add an express requirement that operations be conducted in compliance with the granting instrument.⁹⁷

The standard specified in Article V.A of the 2015 Form is typical. It requires that the Operator “conduct its activities under this agreement as a reasonably prudent operator, in a good and workmanlike manner, with due diligence and dispatch, in accordance with good oilfield practice, and in compliance with applicable law and regulations.” The 1989 Form contained an identical standard, while the earlier AAPL 610 Forms required the Operator to conduct “all such operations in a good and workmanlike manner.”⁹⁸

96. AMPLA cl. 7.1(e); AMPLA cl. 7.1(f); AMPLA cl. 7.5(b).

97. For example, Article 5.1.C of Rocky Mountain Form 3 requires the Operator to “[c]omply with the terms of the oil and gas leases [to which the JOA applies] and with all applicable laws and regulations.”

98. 1989 AAPL 610, Art. V.A.; 1982 AAPL 610, Art. V.A.; 1977 AAPL 610, Art. V.A.; 1956 AAPL 610, art. 5.

Similarly, one of the AAPL offshore forms requires the operator to “timely commence and conduct all operations in a good and workmanlike manner, as would a prudent operator under the same or similar circumstances,”⁹⁹ while the other contains the same language, except for replacing “operations” with “activities or operations.”¹⁰⁰ Both require the Operator to conduct operations in compliance with the law.¹⁰¹

Forms used outside the United States seem to impose analogous standards.¹⁰² The 2012 AIPN Form requires the Operator to conduct all joint operations “in a diligent, safe, and efficient manner in accordance with good and prudent petroleum industry practices and field conservation principles generally followed by the international petroleum industry under similar circumstances,” and in compliance with the granting instrument and “the Laws.”¹⁰³ The AMPLA form contains similar language, but also adds requirements relating to fair dealing, stating that the Operator must “conduct Joint Operations in a good, workmanlike and commercially impartial and reasonable manner in accordance with Good Australian Oilfield Practice,”¹⁰⁴ and that the Operator must “act in utmost good faith in all its dealings, as Operator, with each” of the other parties.¹⁰⁵

Of course, “good and workmanlike manner” refers to a general standard of conduct. The parties to a JOA specify a standard of conduct instead of attempting to specify exactly what the Operator must do in all future circumstances because at the time the JOA is entered, the circumstances that will arise in future operations are unknown and the range of possible circumstances is unlimited.

It is probably impossible to define the “good and workmanlike manner” standard, except in very general terms, but existing case law may shed some light on the standard and how courts have applied it. In the

99. This requirement is contained in art. 5.2 of the AAPL Form 710.

100. AAPL Form 810, art. 5.2. art. 26.4 requires all Parties to comply with “all laws, orders, rules, and regulations,” and article 5.10 requires compliance with health, safety, and environmental regulations.

101. Article 5.6 of AAPL Form 710 requires the Operator to conduct operations in compliance with the law. *See also* AAPL Form 810, art. 26.4.

102. Article 3.04 of the CAPL form requires the Operator to “conduct all Joint Operations diligently, in a good and workmanlike manner, in compliance with the Title Documents and the Regulations and in accordance with good oilfield practice.”

Clauses 6.2.2(a) and (b) of the UKCS form require the Operator to “conduct the Joint Operations in a proper and workmanlike manner in accordance with Good Oilfield Practice,” and “in compliance with the requirements of the Acts, the License, and any other applicable Legislation.”

103. AIPN art. 4.2.B.2; AIPN art. 4.2.B.1.

104. AMPLA cl. 7.1(c) (Section 1.1 of the AMPLA form provides a lengthy definition of “Good Australian Oilfield Practice.”)

105. AMPLA cl. 7.1(g).

context of a drilling contract that obligated a party to perform in a “good and workmanlike manner,” a Texas appellate court expressed approval for a definition providing that the work must be performed “as a person skilled in that business should do it—in a manner generally considered skillful by those capable of judging such work in the community of the performance.”¹⁰⁶ In a context outside the oil and gas industry, the Texas Supreme Court defined “good and workmanlike manner” as meaning “that quality of work performed by one who has the knowledge, training, or experience necessary for the successful practice of a trade or occupation and performed in a manner considered proficient by those capable of judging such work.”¹⁰⁷ Similarly, Black’s Law Dictionary defines “good and workmanlike” as meaning “[i]n a manner generally considered skillful by those capable of judging such work in the community of its performance.”¹⁰⁸

Relatively few cases address the meaning of “good and workmanlike manner” in the context of joint operating agreements. A few cases that have addressed the standard in this context seem to have equated the “good and workmanlike manner” standard with the “prudent operator” standard. In *Johnston v. American Cometra, Inc.*, non-operators brought suit against the Operator in a Texas state court, complaining in part that the Operator breached its duties by failing to bring a take-or-pay claim on behalf of the parties to the operating agreement.¹⁰⁹ The district court granted summary judgment to the Operator, dismissing the claims that were based on the failure to assert a take-or-pay claim.¹¹⁰

The appellate court affirmed in part and reversed in part. The appellate court acknowledged that the joint operating agreement contained clauses that could support the Operator’s argument that it did not owe a fiduciary duty to the non-operators.¹¹¹ But the court stated that even though the Operator might not owe fiduciary duties, the Operator owed other duties to the non-operators, including the duty to perform in a “good and workmanlike manner.”¹¹² The court concluded that this required the Operator to “perform as a reasonably prudent operator.”¹¹³

The court went on to hold that, because the summary judgment record did not preclude the possibility that a reasonably prudent operator would

106. *Westbrook v. Watts*, 268 S.W.2d 694, 698 (Tex. App. 1954).

107. *Melody Home Mfg. Co. v. Barnes*, 741 S.W.2d 349 (Tex. 1987).

108. *Good and Workmanlike*, BLACK’S LAW DICTIONARY (6th ed. 1990).

109. 837 S.W.2d 711 (Tex. App. 1992).

110. *Johnston v. American Cometra, Inc.*, 837 S.W.2d 711, 713 (Tex. App. 1992).

111. *Id.* at 716.

112. *Id.*

113. *Id.*

have asserted a take-or-pay claim on behalf of the non-operators, the portion of the summary judgment ruling that dismissed the plaintiffs' complaint as it related to that issue should be reversed.¹¹⁴ This should not be read as indicating that the prudent operator standard would require an Operator to assert a take-or-pay claim on behalf of the non-operators. Instead, the case merely stands for the proposition that this is a question of fact. Thus, the primary importance of *American Cometra* is that: (1) it equates the "good and workman manner" standard with the prudent operator standard, and (2) it illustrates that the question of whether the standard has been breached is an issue of fact.

Norman v. Apache Corp., was another appeal of a summary judgment decision.¹¹⁵ The case was a diversity jurisdiction case that arose in Texas, and the court cited *American Cometra* in support of the proposition that the "good and workmanlike manner" standard required the Operator to act as a reasonably prudent operator.¹¹⁶ Here, the Operator permanently abandoned a unit well that the Operator asserted was no longer economic. Although the well was the only well that was holding certain leases beyond the primary term,¹¹⁷ the Operator did not inform the non-operators in advance that it was abandoning the well. The leases that had been held by the well's production had cessation of production clauses¹¹⁸—some with a 60-day period and others with a 90-day period—but those periods had already lapsed by the time that the Operator informed the non-operators that the well had been abandoned.¹¹⁹ Thus, the leases were lost.

The non-operators filed suit, complaining that the Operator breached its duties by not informing them in advance that it planned to permanently abandon the wells. Based on certain portions of the operating agreement

114. *Id.* at 716, 718.

115. 19 F.3d 1017 (5th Cir. 1994).

116. *Norman v. Apache Corp.*, 19 F.3d 1017, 1019-20 (5th Cir. 1994) (case removed from state court based on diversity jurisdiction). *Id.* at 1029-30 (equating good and workman like manner standard and prudent operator standard).

117. In the United States, oil and gas leases are virtually always granted for a primary term of specified length (typically a few years) and as long thereafter as there is production of oil or gas in paying quantities. If the lease is beyond the primary term, a well that is producing oil or gas in paying quantities, and which thus is keeping the lease alive, is described as "maintaining" or "holding" the lease.

118. A cessation of production clause is a type of savings clause. Such a clause typically provides that, if a lease has been held by production after the primary term and such production ceases, the lease will not terminate if the lessee takes certain action—such as to re-establish production in the well, to commence reworking of that well, or the commence drilling operations for a new well—within some specified number of days. See Patrick H. Martin and Bruce M. Kramer, *MANUAL OF OIL AND GAS TERMS* (14th ed. 2009).

119. *Norman v. Apache Corp.*, 19 F.3d 1017, 1019 (5th Cir. 1994).

that were quoted by the court, it appears that the parties may have been using a modified version of the 1956 version of the AAPL Form-610. In any event, the United States Fifth Circuit held that the operating agreement did not expressly require the Operator to inform the non-operators in advance about the permanent abandonment of a well, but that the district court erred by granting summary judgment dismissing the plaintiff's claim that the Operator breached its duty to perform in a good and workmanlike manner. Thus, *Norman* does two relevant things here—it (1) reinforces the view that, at least under Texas law, the good and workmanlike manner standard requires an Operator to perform as a reasonably prudent operator, and (2) declares that whether this standard has been breached will be a fact issue.

As for the reasonably prudent operator standard, much of the jurisprudence relating to what it requires is found in the context of implied covenant disputes between lessors and lessees. The descriptions of the reasonably prudent operator standard found in those cases does not shed much additional light on what the standard requires. The jurisprudence merely suggests that the reasonably prudent operator standard requires an Operator to take the steps that a reasonably prudent operator would take in the same circumstances.

As a general rule, a non-operator who asserts that the Operator has breached the reasonably prudent operator standard will need expert testimony. Under certain facts, it might be clear to the average factfinder that an Operator's conduct does not satisfy this standard, but generally the average juror or judge will not know what is required of a reasonably prudent operator. For example, in *Bonn Operating Co. v. Devon Energy Production Co.*, a federal district court in Texas expressly concluded that expert testimony would be needed to establish whether the Operator failed to act as a reasonably prudent operator, thereby breaching the good and workmanlike manner standard under an operating agreement.¹²⁰ This conclusion is consistent with court decisions that a lessor-plaintiff needs expert testimony in order to establish that a lessee has breached implied covenant duties under a lease (implied covenant duties are evaluated based on a reasonably prudent operator standard).

If parties find themselves in a dispute regarding whether the Operator met the required standard of care, the parties can look to previously-decided cases for some guidance, but the circumstances faced by the parties may not be a close match to the circumstances found in the available cases. Further, the question of whether the Operator met the standard of care is a factual question, and, even if the circumstances of the

120. 2009 WL 484218 (N.D. Tex.); The parties in *Bonn Operating* used the 1956 version of the AAPL Form 610.

parties' dispute happens to be a reasonably-close match for the facts of a prior case, the factfinder in the parties' dispute could reach a different conclusion than the factfinder in the prior case.

Finally, although the discussion immediately above talks about parties disputing whether the Operator has met its obligations to conduct operations in a "good and workmanlike manner," it is noteworthy that the exculpatory clause found in many joint operating agreements will shield the Operator from liability to the Non-Operators unless the seriousness of the Operator's lapse is much more severe than a mere failure to satisfy the "good and workmanlike manner standard." A later section of this Article will discuss exculpatory clauses.

B. Attempts to Hold Operator to Fiduciary or Other Heightened Standards

Non-operators sometimes attempt to hold Operators to heightened duties, such as a fiduciary duty.¹²¹ Typically, they do this by arguing that the relationship between the parties carries with it either fiduciary duties or some heightened duty of loyalty. Because agents generally owe a fiduciary duty to their principal,¹²² the principal-agency relationship is the example of such a duty.¹²³

Another way Non-Operators can argue that the Operator owes fiduciary duties is by asserting that either the joint operating agreement, the parties' conduct, or both, establishes some relationship between all the parties such that all parties owe fiduciary duties to one another. Such an

121. A fiduciary duty is "[a] duty to act for someone else's benefit, while subordinating one's personal interest to that of the other person." *Fiduciary Duty*, BLACK'S LAW DICTIONARY (6th ed. 1990). The Rocky Mountain Mineral Law Foundation has previously published several excellent articles on joint operating agreements, including some that discuss arguments regarding whether an operator is subject to a fiduciary duty. See, e.g., Patrick H. Martin, *Gas Balancing and Split Stream Sales Under Joint Operating Agreements and Unit Operating Agreements*, ROCKY MTN. MIN. L. FDN. SPECIAL INST. ON ONSHORE POOLING AND UNITIZATION (2008).

122. RESTATEMENT (SECOND) AGENCY § 13 ("An agent is a fiduciary with respect to matters within the scope of his agency."); RESTATEMENT (THIRD) AGENCY § 8.01 ("An agent has a fiduciary duty to act loyally for the principal's benefit in all matters connected with the agency relationship."); *Johnson v. Brewer & Pritchard, P.C.*, 73 S.W.3d 193, 200 (Tex. 2002); *Basile v. H & R Block, Inc.*, 761 A.2d 1115, 1120 (Pa. 2000); *Burlington Northern and Santa Fe Ry. Co. v. Burlington Resources Oil & Gas Co.*, 590 N.W.2d 433, 437 (N.D. 1999).

123. Section IV(A) of this Article discusses issues relating to whether the Operator could be classified as an agent for purposes of all work it performs on behalf of the Non-Operators. Section IV(B) of this Article discusses whether the Operator could be classified as an agent for limited purposes.

argument, if successful, would impose the same duty on all the parties, rather than some special duty on the Operator. The existence of such a duty could be particularly significant for the Operator; as the party that conducts operations and bears certain other duties, the operator is most likely to be on the “receiving end” of a breach of fiduciary duty claim.

It is beyond the scope of this Article to provide a worldwide survey of the various laws and business relationships that can establish heightened duties between parties. Below, however, this Article gives an overview of the elements necessary to establish a partnership, mining partnership, or joint venture¹²⁴ within the United States, followed by a brief discussion of efforts by the AAPL Form 610 and other model forms to avoid the creation of such relationships. The potential existence of such entities is important because parties to those relationships often owe heightened duties to one another.

1. Elements of Partnerships, Mining Partnerships, and Joint Ventures

The elements necessary to establish a partnership, mining partnership, or joint venture have certain similarities. For each of the three, a critical element is the right of control, as can be seen by examining the elements of a partnership.

a. Elements of a Partnership

Partnership law is now governed by statute in all 50 states. It appears that all states other than Louisiana have adopted some version of the Uniform Partnership Act, and, in Louisiana, partnerships are governed by the Louisiana Civil Code.¹²⁵ But the statutes governing partnerships—like the common law that previously governed partnerships—impose high standards of conduct upon partners. As a general rule, partners owe

124. Within the United States, “joint venture” typically means a business relationship that is akin to a partnership, except that a “joint venture” generally is entered for a single business deal or a specific area or for a limited time. This Article acknowledges that, outside the U.S., some people may use “joint venture” differently.

125. *See, e.g.,* *Ingram v. Deere*, 288 S.W.3d 886, 894-5 (Tex. 2009) (stating that Uniform Partnership Act had been adopted by all states other than Louisiana and discussing, under Texas law, the change).

fiduciary duties and duties of loyalty to one another,¹²⁶ and they are agents of the partnership.¹²⁷

State law governs whether a partnership exists, but the elements or factors necessary to create a partnership tend to be similar from one state to another. The intent of the parties is an important element, but the creation of a partnership does not necessarily depend on whether the parties subjectively intended to form one.¹²⁸ The critical factor with respect to intent is whether the parties intended to create a business relationship that contains the characteristics of a partnership—a business carried on jointly for purposes of profit.¹²⁹ In some states—such as Kansas, New Mexico, and Oklahoma—statutes provide that “the association of two or more persons to carry on as co-owners a business for profit forms a partnership.”¹³⁰ In some other oil and gas states—such as Colorado, North Dakota, Ohio, Pennsylvania, and Wyoming—the statutes governing partnerships use very similar language in specifying what constitutes a partnership.¹³¹ But co-ownership of property and a sharing of profits made by use of the property alone are not sufficient to create a partnership.¹³² To constitute a partnership, each owner must have a right of control.¹³³

126. *See, e.g.*, LA. CIV. CODE art. 2809; N.M. § 54-1A-404; OHIO REV. CODE § 1776.44; 54 OKLA. STAT. § 1-404; 15 PA. CONSOL. STAT. § 8447; WYO. STAT. § 17-21-404. Under the Texas statutes governing partnerships, the duties are not explicitly called “fiduciary” duties, but there are duties of loyalty, TEX. BUS. ORG. CODE § 152.205, and of good faith, TEX. BUS. ORG. CODE § 152.204(b), and these duties generally cannot be waived, TEX. BUS. ORG. CODE § 152.002. Other states, even those that refer to the existence of “fiduciary” duties, may also provide expressly for duties of loyalty, good faith, and fair dealing that cannot be waived. *See, e.g.*, 54 OKLA. STAT. §§ 1-103 (bar on waiver of certain duties), 1-404 (duty of loyalty, good faith, and fair dealing).

127. *See, e.g.*, COLO. REV. STAT. § 7-60-109; LA. CIV. CODE art. 2809; N.M. § 54-1A-301; OHIO REV. CODE § 1776.31; 54 OKLA. ST. § 1-301; TEX. BUS. ORG. CODE § 152.301; WYO. STAT. § 17-21-301.

128. *Ziegler v. Dahl*, 691 N.W.2d 271, 275 (N.D. 2005); *Hillme v. Chastain*, 75 S.W.3d 315, 317 (Mo. App. 2002).

129. *Id.*

130. 54 OKLA. STAT. § 1-202; N.M. STAT. § 54-1A-202; KAN. STAT. § 56a-202.

131. COLO. REV. STAT. §§ 7-60-106 (definition of “partnership”), 7-60-107 (rules for determining whether a partnership exists); N.D. CENT. CODE § 45-13-01; OHIO REV. CODE § 1776.01; 15 PA. CONSOL. STAT. § 8412 (nature of partnership); TEX. BUS. ORG. CODE § 152.051; WYO. STAT. 17-21-101.

132. 54 OKLA. STAT. § 1-202; N.M. STAT. § 54-1A-202; KAN. STAT. § 56a-202.

133. *Ziegler v. Dahl*, 691 N.W.2d 271, 275 (N.D. 2005); *Al-Yassin v. Al-Yassin*, 2004 WL 625757 *7 (Cal. App. 2004); *Tarnavsky v. Tarnavsky*, 147 F.3d 674, 677-8 (8th Cir. 1998) (an element necessary for creation of a partnership is “power of control in the management of the business;” North Dakota law); *In re Stewart*, 1990 WL 10593999 *3 (Bankr. S.D. Iowa 1990); *cf. Hillme v. Chastain*, 75 S.W.3d 315, 317 (Mo. App. 2002) (“A voice in the management of the partnership enterprise . . . [is an] indication[] of a partnership”).

Under Texas law, courts consider a list of five factors—none of which are determinative—in evaluating whether a partnership exists.¹³⁴ Factors that weigh in favor of concluding that persons have created a partnership include the fact they have: (1) received or have the right to share in the profits of a business; (2) expressed an intent to be partners; (3) participated or have the right to participate in control of the business; (4) have shared or agreed to share losses and liabilities; and (5) contributed or agreed to contribute money or profit into the business.¹³⁵ Texas statutory law specifically states that the mere fact that a mineral interest is governed by a joint operating agreement will not establish a partnership.¹³⁶

Louisiana law provides that “[a] partnership is a juridical person, distinct from its partners, created by a contract between two or more persons to combine their efforts or resources in determined proportions and to collaborate at mutual risk for their common profit or commercial benefit.”¹³⁷ The terms of most joint operating agreements would satisfy the majority of terms included within that definition, but Louisiana law expressly provides that an oil and gas joint operating agreement “does not create a partnership unless the contract expressly so provides.”¹³⁸

In many jurisdictions, a disclaimer of partnership will not necessarily be determinative, but it should be helpful in preventing parties from being deemed partners when they do not wish to be. This is particularly true with respect to the duties the parties owe one another. If the parties do not wish to be partners, there is no reason that the law should impose upon them partnership duties vis-à-vis one another. Further, the level of control that most joint operating agreements give to the Operator may preclude the joint right of management that is necessary for the existence of a partnership.

134. *Ingram*, 288 S.W.3d at 895.

135. TEX. BUS. ORG. CODE § 152.052.

136. TEX. BUS. ORG. CODE § 152.052(b)(4).

137. LA. CIV. CODE art. 2801. Louisiana is largely a civil law or mixed jurisdiction, even though it is part of the United States, where the common law has predominated historically. The civil law has been more receptive to treating partnerships as an entity. Harry G. Henn and John R. Alexander, *LAW OF CORPORATIONS* § 9 at pp. 16-19 (West Publishing 3rd ed. 1983). The common law applied the “aggregate” theory to partnerships. *Id.* Under that theory, a partnership created a relationship between individuals—a relationship that had certain consequences—but a partnership was not a separate juridical entity. But now, all 49 states other than Louisiana have adopted some version of the Uniform Partnership Act, and that Act largely treats partnerships as entities.

138. LA. REV. STAT. § 31:215. Depending on the meaning of “collaborate” and the terms of a particular joint operating agreement, the “collaborat[ion]” element might not be satisfied. Thus, even without LA. REV. STAT. § 31:215, the parties to a joint operating agreement would not necessarily have a partnership.

a. Elements of a Mining Partnership

Members of a mining partnership generally owe fiduciary duties to one another.¹³⁹ Whether a mining partnership exists is an issue of fact, but the elements or factors necessary to establish a mining partnership are a matter of state law.¹⁴⁰ In Oklahoma, there are three elements of a mining partnership: (1) a joint interest in the property; (2) an express or implied agreement to share in profits and losses; and (3) cooperation in the project.¹⁴¹ Under Oklahoma law, “cooperation in the project” means “actively joining in the promotion, conduct or management” of a project.¹⁴² The mere fact that an interest is governed by a joint operating agreement is not sufficient to create a mining partnership.¹⁴³ Such actions as “[r]eceiving reports, questioning bills, and hiring a pumper to evaluate [a] well in contemplation of taking over as operator” do not constitute “cooperation in the project.”¹⁴⁴

Much of the jurisprudence relating to whether a mining partnership exists is brought by third persons who seek to have all the co-owners held liable for the torts or contracts of one of the co-owners (usually the operator), opposed to being cases brought by a co-owner seeking to hold the Operator liable as a fiduciary. Often, the existence or non-existence of a mining partnership turns on whether all of the co-owners had a right to control operations. In the absence of such a right, a court generally will find that a mining partnership does not exist. And often courts have found that a mining partnership does not exist because non-operators lacked the right to control operations.

b. Elements of a Joint Venture

A joint venture is similar to a partnership. The primary distinction between a partnership and a joint venture “is that, while a [partnership] is ordinarily formed for the transaction of a general business of a particular kind, a joint venture is usually, but not necessarily, limited to a single transaction, although the business of conducting it to a successful

139. *Bufalini v. De Michelis*, 288 P.2d 934, 937 (Cal. Ct. App. 1955); *Smith v. Bolin*, 261 S.W.2d 352, 363 (Tex. App. 1953), *aff'd in part and rev'd in part*, 271 S.W.2d 93 (Tex. 1954).

140. *Spark Bros. Drilling Co. v. Texas Moran Exploration Co.*, 829 P.2d 951, 953 (Okla. 1991).

141. *Id.*

142. *Id.*; *see also Jenkins v. Pappas*, 383 P.2d 645, 647 (Okla. 1963).

143. *See Spark Bros. Drilling Co.*, 829 P.2d 951 at 953.

144. *Id.* at 954.

termination may continue for a number of years.”¹⁴⁵ Because joint ventures are essentially partnerships for a limited purpose, joint ventures generally are governed by the same rules that govern partnerships.¹⁴⁶ Accordingly, parties to a joint venture owe each other fiduciary duties, just as partners owe each other fiduciary duties.¹⁴⁷

The mere facts that parties co-own an oil and gas lease and that they have agreed that one co-owner will operate the lease on the parties’ behalf are not sufficient to create a joint venture.¹⁴⁸ On the other hand, the existence of a joint operating agreement will not automatically preclude the existence of a joint venture. In some cases, courts have found that a joint venture existed.¹⁴⁹ In other cases, courts have determined that a joint

145. *Daily States Publishing Co. v. Uhalt*, 126 So. 228, 231 (La. 1930). *See also* *Ben Fitzgerald Realty Co. v. Muller*, 846 S.W.2d 110, 120 (Tex. App. – Tyler 1993) (“The principle distinction between a joint venture and a partnership is that a joint venture is usually limited to one particular enterprise.”); *Texas Oil & Gas Corp. v. Hawkins Oil & Gas, Inc.*, 668 S.W.2d 16, 16 (Ark. 1984) (“[A] joint venture is ‘in the nature of a partnership of a limited character.’”) (quoting *Johnson v. Lion Oil Company*, 216 Ark. 736, 739 (Ark. 1950)); *Boles v. Akers*, 244 P. 182, 184 (Okla. 1925) (“A joint venture generally relates to a single transaction.”); *Bebo Const. Co. v. Mattox & O’Brien, P.C.*, 998 P.2d 475, 477 (Colo. App. 2000) (“A joint venture is a partnership formed for a limited purpose”); *SPW Assocs., LLP v. Anderson*, 718 N.W. 2d 580, 583 (N.D. 2006) (“A joint venture is generally considered akin to a partnership, although more limited in scope and duration. . . .”); *Lightsey v. Marshall*, 128 N.M. 353, 357, 992 P.2d 904, 908 (N.M. App. 1999) (“a joint venture ‘is generally considered to be a partnership for a single transaction’”); *Madrid v. Norton*, 596 P.2d 1108, 1118 (Wyo. 1979) (“The principal distinction between a joint venture and a partnership is that a joint venture usually relates to a single transaction.”); *see also* *Henn, supra* note 137, § 49 at 105.

146. *SPW Assocs., LLP v. Anderson*, 718 N.W.2d 580, 583 (N.D. 2006); *Ben Fitzgerald Realty Co. v. Muller*, 846 S.W.2d 110, 120 (Tex. App. 1993); *Cajun Elec. Power Co-Op, Inc. v. McNamara*, 452 So. 2d 212, 215 (La. App. 1984); *Boles v. Akers*, 244 P. 182, 184 (Okla. 1925); *Madrid v. Norton*, 596 P.2d 1108, 1118 (Wyo. 1979); *see also* *Henn, supra* note 137, § 49 at 107.

147. *Texas Oil & Gas Corp. v. Hawkins Oil & Gas, Inc.*, 668 S.W.2d 16, 17 (Ark. 1984); *Rankin v. Naftalis*, 557 S.W.2d 940, 944 (Tex. 1977); *Madrid v. Norton*, 596 P.2d 1108, 1118 (Wyo. 1979); *see also* *Henn, supra* note 137, § 49 at p. 107.

148. *Hamilton v. Texas Oil & Gas Corp.*, 648 S.W.2d 316, 320 (Tex. App. 1982) (“Joint owners of an oil and gas lease, may contract for the operation of leases by one of them and for the operator, in the event of success, to pay to the other joint owners one-half of the proceeds of the sale of the oil and gas less the expenses of finding it, without creating a joint venture or a mining partnership.”).

149. *Rankin v. Naftalis*, 557 S.W.2d 940, 944 (Tex. 1977) (parties were “joint venturers for the development of a particular oil and gas lease;” nevertheless, plaintiffs were denied recovery because joint venture did not extend to the property that was at issue in the litigation). As one commentator noted, “the mere existence of an agreement between an operator and non-operator is not sufficient to avoid [the existence of a fiduciary] duty.” Christopher S. Kulander, *Old Faves and New Raves: How Case Law Has Affected Form Joint Operating Agreements—*

venture did not exist.¹⁵⁰ State law determines the elements necessary to create a joint venture, but whether a joint venture exists in any particular case will be a fact issue that depends on the terms of the parties' agreement and perhaps on their conduct.¹⁵¹

In Texas, four elements are necessary for the existence of a joint venture: (1) a community of interest in the venture; (2) an agreement to share profits; (3) an agreement to share losses; and (4) a mutual right of control or management of the enterprise.¹⁵² A community of interest is defined under Texas law as "a commonly shared incentive between the parties as to the progress and goals of the joint venturers."¹⁵³ Under most joint operating agreements, at least three of the four elements of a joint venture will exist—a community of interest, an agreement to share profits, and an agreement to share losses. Accordingly, if parties dispute whether a joint venture exists, the determining issue often will be whether the parties have a mutual right of control and management.¹⁵⁴ A mere right to receive information or to visit the drill site is not sufficient control to support the existence of a joint venture.¹⁵⁵

In Oklahoma, three elements are needed to establish a joint venture: "1) A joint interest in property (the contributions need not be equal or of the same character), 2) An express or implied agreement to share profits and losses of the venture, 3) Action or conduct showing cooperation in the venture."¹⁵⁶ Under Colorado law, the elements necessary to establish a

Problems and Solutions (Part One), 1 OIL AND GAS, NAT. RES., AND ENERGY J. 1, 11 (2015). Instead, courts will consider whether the terms of the agreement "create[] a partnership, joint venture, or agency relationship that may trigger a fiduciary duty." *Id.*

150. *Ayco Development Corp. v. G.E.T. Service Co.*, 616 S.W.2d 184, 186 (Tex. 1981); *Hamilton v. Texas Oil & Gas Corp.*, 648 S.W.2d 316, 321 (Tex. App. El Paso 1982).

151. *Grand Isle Campsites, Inc. v. Cheek*, 262 So. 2d 350 (La. 1972); *Cajun Elec. Power Co-Op, Inc. v. McNamara*, 452 So. 2d 212, 216 (La. App. 1984); *see also Price v. Howard*, 236 P.3d 82, 91 (Okla. 2010) (existence is a question of fact); *Madrid v. Norton*, 596 P.2d 1108, 1118 (Wyo. 1979) (question of fact). The agreement that supports the existence of a joint venture can be either express or implied. *Pillsbury Mills, Inc. v. Chehardy*, 90 So. 2d 797, 801 (La. 1956).

152. *Ayco Development Corp. v. G.E.T. Service Co.*, 616 S.W.2d 184, 186 (Tex. 1981); *Hamilton v. Texas Oil & Gas Corp.*, 648 S.W.2d 316, 321 (Tex. App. 1982).

153. *Metroplexcore, L.L.C. v. Parsons Transp., Inc.*, 743 F.3d 964, 973 (5th Cir. 2014) (*quoting* *Ballard v. United States*, 17 F.3d 116, 118 (5th Cir. 1994)).

154. This has been the decisive issue in several cases. *See, e.g., Ayco Development Corp. v. G.E.T. Service Co.*, 616 S.W.2d 184, 186 (Tex. 1981); *Hamilton v. Texas Oil & Gas Corp.*, 648 S.W.2d 316, 321 (Tex. App. 1982) (no joint venture because operator "had full control of all operations").

155. *Ayco Development Corp. v. G.E.T. Service Co.*, 616 S.W.2d 184, 186 (Tex. 1981).

156. *McGee v. Alexander*. 37 P.3d 800, 806-7 (Okla. 2001).

joint venture are essentially the same. Courts have stated that a party must prove the existence of three elements in order to show that a joint venture exists—“(1) A joint interest in the property; (2) an agreement, express or implied, to share in the losses or profits of the venture; and (3) actions or conduct showing cooperation in the project. No one of these elements alone is sufficient.”¹⁵⁷ The law is very similar in most other states.¹⁵⁸ Thus, whether or not the non-operators have a right of control tends to be the deciding issue in disputes regarding whether a joint venture exists.

Based on the non-operator’s lack of control, courts often have found that a joint venture did not exist, but, in some cases, courts have found that the parties’ relationship constituted a joint venture. If a joint venture exists, one of the consequences of the fiduciary duty or duty of loyalty owed by each co-owner could be a duty not to compete with the joint venture. In *Texas Oil & Gas Corp. v. Hawkins Oil & Gas, Inc.*, the heirs of Alexander B. Hamilton granted oil and gas leases to Hawkins Oil & Gas, Inc. (“Hawkins”) covering certain areas in “Section 6” that had been owned by Hamilton.¹⁵⁹ Later, Hawkins entered a joint operating agreement with Texas Oil & Gas Corp. (“Texas”). Texas also held leases covering land in Section 6, and it became Operator. Later, Texas discovered that the Hamilton heirs did not own the minerals in the land covered by the lease they had granted to Hawkins. Instead, Hamilton’s widow owned the minerals. Without telling Hawkins that its lessors lacked title to the minerals purportedly leased to Hawkins, Texas acquired leases from the heirs of Hamilton’s widow.

After discovering what Texas had done, Hawkins filed suit in Arkansas asserting that the parties’ joint operating agreement created a

157. *Breckenridge Co. v. Swales Management Corp.*, 522 P.2d 737, 739 (Colo. 1974).

158. Under North Dakota law, four elements must be present to form a joint venture, namely “(1) contribution by the parties of money, property, time, or skill in some common undertaking, but the contributions need not be equal or of the same nature; (2) a proprietary interest and right of mutual control over the engaged property; (3) an express or implied agreement for the sharing of profits, and usually, but not necessarily, of losses; and (4) an express or implied contract showing a joint venture was formed.” *SPW Assocs., LLP v. Anderson*, 718 N.S.2d 580, 583 (N.D. 2006).

In New Mexico, a joint adventure is formed when parties enter an agreement that they will (1) combine their resources into a particular business deal, (2) share profits, (3) share losses, and (4) have the mutual right of control over the subject matter of the enterprise. *Fullerton v. Kaune*, 382 P.2d 529, 532 (N.M. 1963).

One treatise states that most authorities would agree on four elements that are necessary to create a joint venture: (1) an agreement, express or inferred; (2) a joint interest (contribution); (3) a sharing of profits and usually of losses, with unlimited liability; and (4) a mutual right of control. *See Henn, supra* note 137 § 49 at p. 17.

159. 668 S.W.2d 16 (Ark. 1984).

joint venture, that joint venturers owe fiduciary duties to one another, and that Texas had breached its duty when it purchased for itself alone an interest in the subject matter of the joint venture. Accordingly, the Arkansas Supreme Court held that Hawkins was entitled to a one-half interest in the leases Texas acquired from the widow's heirs.¹⁶⁰

2. Model Form Efforts to Avoid Partnership, Mining Partnership, or Joint Venture

Parties typically want their joint operating agreement to govern their obligations with respect to one another. They wish to avoid having the law impose the sort of heightened standards of conduct associated with partnerships, fiduciary relationships, and principal-agent relationships. Similarly, they do not want to be directly liable to third persons for the acts of other parties to the joint operating agreement, and the existence of a partnership could result in direct liability to third persons.

Accordingly, the 2015 and 1989 versions of AAPL Form 610 expressly disclaim any intent to create a partnership, mining partnership, or joint venture.¹⁶¹ The 1982 and 1977 Forms expressly disclaim any intent to create a "mining or other partnership or association."¹⁶² The 1982 and 1977 Forms do not expressly refer to joint ventures, but the Forms' disclaimer should be interpreted as effectively disclaiming any intent to create a joint venture given the fact that a joint venture is essentially a partnership for a limited purpose (as noted above), and given those Forms' disclaimer of an intent to create a partnership or other "association." The AAPL Offshore Forms contain similar provisions, as does Rocky Mountain Form 3, which similarly disclaims any intent to form a partnership, mining partnership, or joint venture.¹⁶³

Model forms used outside the United States contain similar provisions. The 2012 AIPN Form states that the parties' relationship is "contractual only and shall not be construed as creating a partnership or other recognized association."¹⁶⁴ AMPLA disclaims any intent to create a partnership,¹⁶⁵ and the CAPL Form states that the parties are not creating a "partnership or association of any kind," and instead hold their interests as "tenants in common, subject to those modifications expressly provided under this Agreement," and that they are not intending to create

160. *Id.*

161. 2015 AAPL 610 art. VII.A; 1989 AAPL 610 art. VII.A.

162. 1982 AAPL 610 art. VII.A; 1977 AAPL 610 art. VII.A.

163. AAPL 710 art. 19.1; AAPL 810 art. 22.1; Rocky Mountain Form 3 art. 16.1.

164. 2012 AIPN art. 9.3.B.8.

165. AMPLA cl. 3.3(f).

partnership duties or fiduciary duties, except for duties relating to commingling of funds and maintaining confidential information.¹⁶⁶ The UKCS Form states that the parties are not creating “any mining partnership, commercial partnership or other partnership.”¹⁶⁷

Under the law of some jurisdictions, a disclaimer of any intent to create a particular relationship may not be sufficient to avoid creating such a relationship if the facts and circumstances satisfy the elements needed to create such a relationship,¹⁶⁸ but the parties’ express disclaimer should be given some weight, particularly with respect to their rights and duties vis-à-vis one another. Further, as discussed in more detail in the section of this Article that discusses the relationship of the Operator to the Non-Operators, the AAPL Forms vest in the Operator the right and duty to conduct all operations, and provide that the Operator is not subject to the direction or control of the Non-Operators. In most cases, the Non-Operators’ lack of the right to control operations likely will prevent the creation of a partnership, mining partnership, or joint venture.¹⁶⁹

IV. RELATIONSHIP OF OPERATOR TO NON-OPERATORS

As already noted, joint operating agreements typically attempt to avoid the creation of a partnership or joint venture between the parties. Many joint operating agreements also attempt to control the legal nature of the *relationship* between the Operator and the Non-Operators. The agreements do so in two major ways. First, they attempt to ensure that the Operator will be classified as an independent contractor, rather than as an agent of the parties. Second, they seek to ensure that the Operator serves on a no-gain and no-loss basis.

A. Independent Contractor Status and Avoiding Principal-Agency Relationship

Most operating agreements used in North America attempt to classify the Operator as an independent contractor, rather than as an agent of the Non-Operators. Some other operating agreements characterize the Operator as the agent of the Non-Operators.

166. CAPL cl. 1.05(A).

167. UKCS cl. 22.2.1.

168. This is certainly true in the United States. *See infra* note 177. Further, it may be true outside the U.S. as well. CAPL cl. 1.05 states that “the Parties recognize [their contractual clause disclaiming any partnership, trust relationship, or fiduciary relationship] might not prevent such a trust, trust duty or fiduciary relationship being imposed at law or in equity.”

169. *See, e.g., Burlington Resources, Inc. v. United National Ins. Co.*, 481 F.Supp. 2d 567, 574 (E.D. La. 2007).

1. *The North American Forms—AAPL and CAPL*

Most of the operating agreements used in North America contain provisions that attempt to ensure that the Operator will be classified as an independent contractor of the Non-Operators, not an agent of the Non-Operators, for purposes of the work that the Operator performs. Avoiding a principal-agency relationship serves two purposes. First, it helps protect the Non-Operators from direct liability to third persons for the contracts and torts of the Operator. As a general rule, a principal is liable to third persons for the torts committed¹⁷⁰ and the contracts entered by¹⁷¹ an agent within the scope of his agency, but a person generally is not liable to third persons for the acts of an independent contractor, provided that the person has not maintained direction and control over the contractor's work.¹⁷²

Second, avoiding a principal-agency relationship can help ensure that the Operator's obligations are generally governed by the terms of the operating agreement, rather than by rules that might be imposed as a matter of law if the Operator were considered an agent. For example, an agent generally owes a fiduciary duty to its principal.¹⁷³ A fiduciary duty generally has "[a] duty to act for someone else's benefit, while subordinating one's personal interest to that of the other person," and such a high level of duty is generally not consistent with the intent of the parties to a joint operating agreement.¹⁷⁴ In contrast to an agent, an independent contractor generally does not owe fiduciary duties.¹⁷⁵

There are at least three ways in which a joint operating agreement can seek to have an Operator classified as an independent contractor of the Non-Operators, rather than as an agent. Namely, the agreement can: (1) expressly characterize the Operator as an "independent contractor"; (2) expressly disclaim the existence of a principal-agent relation; and (3) give the Operator a degree of control over operations that is characteristic of an

170. RESTATEMENT (THIRD) AGENCY § 7.04; *Travelers Cas. & Sur. Co. v. Castagnaro*, 772 A.2d 456, 460 (Pa. 2001); *Marron v. Helmecke*, 67 P.2d 1034, 1035 (Colo. 1937).

171. RESTATEMENT (THIRD) AGENCY §§ 6.01-6.03.

172. RESTATEMENT (SECOND) TORTS §§ 409, 414; *Fleck v. ANG Coal Gasification Co.* 522 N.W.2d 445, 447 (N.D. 1994).

173. RESTATEMENT (SECOND) AGENCY § 13 ("An agent is a fiduciary with respect to matters within the scope of his agency."); RESTATEMENT (THIRD) AGENCY § 8.01 ("An agent has a fiduciary duty to act loyally for the principal's benefit in all matters connected with the agency relationship."); *Johnson v. Brewer & Pritchard, P.C.*, 73 S.W.3d 193, 200 (Tex. 2002); *Basile v. H & R Block, Inc.* 761 A.2d 1115, 1120 (Pa. 2000); *Burlington Northern and Santa Fe Ry. Co. v. Burlington Resources Oil & Gas Co.*, 590 N.W.2d 433, 437 (N.D. 1999).

174. BLACK'S LAW DICTIONARY (6th edition 1990).

175. *Horwitz v. Holabair & Root*, 816 N.E.2d 272, 285-6 (Ill. 2004).

independent contractor, rather than an agent. The two most recent versions of the AAPL Form 610 do each of these three things.

First, Articles V.A of the 2015 and 1989 Forms state, “In its performance of services hereunder for the Non-Operators, Operator shall be an independent contractor ” Readers should note, however, that merely declaring in an agreement that one party is an independent contractor, rather than an agent, will not necessarily be determinative of the nature of the parties’ relationship. Courts sometimes will consider the parties’ intent regarding the nature of their relationship,¹⁷⁶ but courts often will look to the substantive terms of a contract’s terms to determine whether those terms satisfy the elements of a principal-agency relationship, rather than simply accepting the characterization that the parties choose to adopt.¹⁷⁷

Further, the same sentence expressly characterizing the Operator as an independent contractor also gives the Operator a degree of control that is characteristic of an independent contractor. The full sentence reads: “In its performance of services hereunder for the Non-Operators, Operator shall be an independent contractor not subject to the control or direction of the Non-Operators except as to the type of operation to be undertaken in accordance with the election procedures contained in this agreement.” The major distinction between an independent contractor and an agent is that

176. For example, in *In re Great Western Drilling, Ltd.*, 211 S.W.3d 828, 841 (Tex. App. – Eastland 2006), the court stated: “The JOAs gave Great Western full control of all operations in the contract area *and recognized that it was an independent contractor* not subject to the control or direction of the working interest owners.” Thus, the court seemed to give some weight to the parties’ characterization of the relationship. This may contrast with *Burlington Resources, Inc. v. United National Ins. Co.*, 481 F. Supp. 2d 567, 574 (E.D. La. 2007). In *Burlington Resources*, the court quoted language stating: Operator “shall *conduct and direct and have full control of all operations* on the Contract Area as permitted and required by, and within the limits of this agreement. In its performance of services hereunder for the Non-Operators [Burlington], Operator shall be an independent contractor *not subject to the control or direction of the Non-Operators* except as to the type of operation to be undertaken ” (emphasis in original). Thus, the court deliberately chose to emphasize the provisions relating to direction and control, while not emphasizing the parties’ characterization of their relationship.

177. One oil and gas professor said: “[I]t is not possible to make what is in fact a ‘cat’ into a ‘dog’ by merely labeling it a ‘dog.’ If the factual attributes point towards ‘cat,’ we have a ‘cat,’ not a ‘dog.’” David E. Pierce, *Evolution of Joint Operations in the oil and Gas Industry*, RCKY. MTN. MIN. L. FOUND. *2-19 Special Inst. On Joint Operation and the New AAPL Form 610-2015 Model Form Operating Agreement (2017); see also RESTATEMENT (THIRD) AGENCY § 1.01 (“An agency relationship arises only when the elements stated in § 1.01 are present. Whether a relationship is characterized as agency in an agreement between parties or in the context of industry or popular usage is not controlling.”) & § 101 cmt. (c).

an agent is subject to the principal's direction and control, whereas an independent contractor generally is not.¹⁷⁸

The next sentence of Article V.A goes on to state that the "Operator shall not be deemed, or hold itself out as, the agent of the Non-Operators with authority to bind them to any obligation or liability assumed or incurred by Operator to any third party."¹⁷⁹ The Offshore AAPL Forms and CAPL Form contain similar provisions.¹⁸⁰

The older versions of the AAPL Form 610 do not expressly refer to the Operator as an independent contractor, but those forms provide that the Operator will "conduct and direct and have full control of all operations."¹⁸¹ Such freedom from direction and control by a principal is characteristic of an independent contractor. The two AAPL Forms designed to be offshore operating agreements expressly provide that the Operator is an "independent contractor, not subject to the control or direction of Non-Operating Parties."¹⁸² The CAPL Form, which often is used in Canada, also characterizes the Operator as an independent contractor.¹⁸³

As a general rule, parties to joint operating agreements seem to be successful in avoiding having the Operator classified as an agent of the non-operators.¹⁸⁴ Indeed, there seem to be relatively few cases in which

178. *Enterprise Mgt. Consultants, Inc. v. State*, 768 P.2d 359, 362 n.13 (Okla. 1988); RESTATEMENT (SECOND) AGENCY § 1. Of course, the person who hires an independent contractor does choose the job that will be done.

179. Article V.A. The 1989 Agreement has language identical to that quoted above. However, in the 2015 Form, Article V.A. goes on to provide a narrow exception to this rule. Namely, the Non-Operators appoint the Operator as their agent for purposes of executing or filing documents relating to pooling or unitization. This exception is not listed in the 1989 Form. *See also* AAPL 710 art. 5.1; AAPL 810 art. 5.1 ("The Operator is not the agent or fiduciary of the Non-Operator Parties."); CAPL cl. 1.05(A) (excluding both agency relationships between parties and existence of fiduciary duties, except for limited purposes).

180. AAPL 710 art. 5.1 ("No Party shall be deemed to be, or hold itself out as, the agent or fiduciary of another Party."); AAPL 810 art. 5.1 ("The Operator is not the agent or fiduciary of the Non-Operator Parties."); CAPL cl. 1.05(A) (excluding both agency relationships between parties and existence of fiduciary duties, except for limited purposes).

181. AAPL-610 (1982) art. V.A; AAPL-610 (1977) art. V.A; AAPL-610 (1956) art. 5.

182. AAPL 710 (2002) art. 5.1; AAPL 810 (2007) art. 5.1 ("Operator is an independent contractor, not subject to the control or direction of Non-Operating Parties.").

183. CAPL cl. 3.03.

184. *In re Oil Spill by the Oil Rig Deepwater Horizon in the Gulf of Mexico*, on April 20, 2010, 808 F. Supp. 2d 943, 963 (E.D. La. 2011); *In re Great Western Drilling, Ltd.*, 211 S.W.3d 828, 841 (Tex. App. Eastland 2006); *Burlington Resources, Inc. v. United National Ins. Co.*, 481 F. Supp. 2d 567, 574 (E.D. La. 2007).

someone argues that, because the Operator conducts all operations, the Operator is an agent of the parties to the joint operating agreement. Sometimes a third person argues that the non-operators are directly liable for torts or contracts of the Operator, but such arguments are typically based on an assertion that the joint operating agreement creates a joint venture, rather than on an assertion the Operator is an agent because it conducts all operations. Further, non-operators sometimes argue that the Operator owes them fiduciary duties or heightened duties of loyalty, but often such arguments are based on an assertion that the joint operating agreement creates a joint venture or that the Operator is an agent for some limited purpose, such as selling a non-operator's share of production, rather than on an assertion that an Operator is a third party for all purposes.

2. Forms Used Outside North America

In contrast to the approach taken by most forms used in North America, the AMPLA Form refers to the Operator as being the “agent of the [Non-Operators] for purposes of this agreement.”¹⁸⁵ The UKCS Form provides that the Operator will serve as the agent of the other parties in dealing with contractors.¹⁸⁶ In contrast, however, AIPN Form 2012 states that the agreement “shall not be deemed or construed to authorize any Party to act as an agent . . . for any other Party for any purpose whatsoever except as explicitly set forth in this Agreement,” and that “the Parties shall not be considered fiduciaries except as expressly provided.”¹⁸⁷

B. Agency Status for Limited Purposes Under Certain Model Forms

Even model forms that disclaim the existence of an agency relationship or fiduciary relationship in general may create such a relationship for limited purposes. For example, as noted earlier this Article, the 2015 version of AAPL Form 610 expressly designates the Operator as an agent for the limited purpose of executing, filing, and recording certain instruments relating to communitization or unitization.¹⁸⁸ In addition, as previously noted, various versions of Form 610 recognize that the Operator has a duty to serve as custody of funds that Non-

185. AMPLA cl. 6.1; *see also* AMPLA cl. 7.1(a) (Operator is required to exercise its powers “as agent for and on behalf of” the Non-Operators).

186. UKCS cl. 6.5.8.

187. 2012 AIPN art. 14.1.

188. “Unitization” refers to “the joint operation of all or some portion of a producing reservoir,” *see* Patrick H. Martin and Bruce M. Kramer, *MANUAL OF OIL AND GAS TERMS*. The joint operation may come about by agreement or by order of an oil and gas regulator.” “Communitization” refers to the same concept, but “communitization” often is used when federal lands are involved.

Operators advance to the Operator, and that the Operator may have fiduciary duties with respect to those funds.¹⁸⁹

Further, an agency relationship might be created if an Operator exercises its rights under a clause relating to the sale of product. The general rule under joint operating agreements is that each party has an obligation to take its share of production in kind and to arrange its sale or other disposition.¹⁹⁰ The AAPL Forms generally provide, however, that if a Non-Operator fails to take its share or production in kind or to make its own arrangements to sell the product, the Operator has the right, though not the duty, to sell the product for the account of that Non-Operator.¹⁹¹ Some courts have concluded that, if the Operator sells products on behalf of a non-operator, then, in doing so, it serves as an agent of that non-operator.¹⁹²

C. *Serving on a No-Gain, No-Loss Basis*

The worldwide consensus view is that the Operator generally should neither gain a profit nor incur a loss because of its role as Operator.¹⁹³ For

189. 2015 AAPL 610 art. V.D.4; 1989 AAPL 610 art. V.D.4.

190. 2015 AAPL 610 art. VI.G; 1989 AAPL 610 art. VI.G; 1982 AAPL art. VI.C; AAPL 710 art. 22.2; AAPL 810 art. 15.1; 2012 AIPN art. 9.1; AMPLA cl. 4.3(a)(iii); CAPL cl. 6.01(A); UKCS cl. 18(b).

191. *See, e.g.*, 2015 AAPL 610 art. VI.H; 1989 AAPL art. VI.G; 1982 AAPL art. VI.C; 1977 AAPL art. VI.C; AAPL 710 art. 22.3; AAPL 810 art. 15.3.

192. *Atl. Richfield Co. v. The Long Trusts*, 860 S.W.2d 439, 445 (Tex. App. Texarkana 1993).

193. This is made explicit in some international JOA forms. Article 4.2.B.5 of the AIPN 2012 Form provides that, subject to exceptions provided in the JOA's accounting procedures or provisions for potential operator liability in the event of gross negligence or willful misconduct, the Operator should "neither gain a profit nor suffer a loss as a result of being the Operator."

AMPLA cl. 6.3(a) provides that the Operator may charge the parties for certain "Operator Overhead" as specified by the parties in a Schedule 1, but Schedule 1 states that this amount is designed to "reimburse without profit" the overhead expenses of the Operator. Further, clause 6.3(c) of the AMPLA Form states: "It is intended that the Operator will neither gain nor, except where it has committed fraud or willful misconduct, suffer a loss as a result of acting as Operator in the conduct of Joint Operations."

Similarly, clause 6.2.2(d) of the UKCS Form states that, except in the case of willful misconduct, the Operator should "neither gain nor suffer a loss in such capacity as a result of acting as Operator in the conduct of Joint Operations."

The no gain/no loss principle is not explicitly stated in the joint operating agreement forms commonly used in the U.S., but the AAPL forms implicitly incorporate this principle by providing that the parties to the JOA will generally share revenue and costs in proportion to their ownership fraction in the venture, the provisions in the AAPL forms that protect the Non-Operators against any self-dealing by the Operator, and provisions in the accounting rules commonly used

this reason, the Operator is not compensated for its service as Operator. It is only entitled to reimbursement of its expenses, which may include a reasonable overhead, but otherwise it works “gratuitously for the benefit of all members of the JOA.”¹⁹⁴ Further, certain provisions in the joint operating agreement that are designed to ensure that the Operator secures goods and services at a reasonable cost (these are discussed in Section II(B)(1) of this Article) include extra safeguards that apply if the Operator wishes to use its own materials and charge the joint account, or if it wishes to purchase services or materials from an affiliate. These measures seek to ensure that the Operator does not make money based on its service as Operator. This helps ensure that parties do not overpay for goods and services.

In addition, these measures help ensure that the Operator will make decisions based on what is best to ensure profitability of operations for all owners. If the Operator were allowed to make a profit on its work as Operator, there might be a conflict of interest between what is best for the parties as owners and what would produce the most profit for the Operator’s work.

The corollary of the no-gain concept is the no-loss concept. The Operator should be entitled to reimbursement for its costs, including a reasonable reimbursement for overhead. Further, as between the parties, the Operator should be protected from losses and liabilities arising from the Operator’s work as Operator. The AAPL joint operating agreement Forms typically provide such protection by providing a general rule that parties bear costs in proportion to their ownership interest, and that the parties’ liabilities are several, not joint or collective.¹⁹⁵ In addition, the AAPL Forms each contain exculpatory clauses which provide that the Operator, in its role “as Operator,” generally will not be liable to the other parties for losses sustained or liabilities incurred.¹⁹⁶ Forms used outside the United States also tend to contain exculpatory clauses.¹⁹⁷

by JOA parties in the U.S., which allow the Operator to charge for overhead, but only to a defined extent. See 2005 COPAS Accounting Procedure, Section III.

194. Scott C. Styles, *Joint Operating Agreements* 375, found in *OIL AND GAS LAW—CURRENT PRACTICE AND EMERGING TRENDS* (Greg Gordon et al. eds., 2d ed. 2011).

195. See, e.g., art. VII.A in the 2015, 1989, 1982, and 1977 versions of AAPL Form 610. See also AAPL 710 arts. 8.1 and 19.1; AAPL 810 arts. 6.1 and 22.1.

196. The exculpatory clause is contained in art. V.A of the 2015, 1989, 1982, and 1977 versions of the AAPL Form 610, and in art. 5 of the 1956 Form. It is contained in art. 5.2 in both the AAPL Form 710 (2002) and the AAPL Form 810 (2007).

197. See, e.g., AIPN art. 4.6; see also CAPL cl. 4.01 and 4.02; UKCS cl. 6.2.4; AMPLA cl. 6.5.

As a general rule, the exculpatory protection provided to the Operator is not absolute. Common exceptions include liability relating to losses sustained or liability incurred when the loss or liability arises from gross negligence, willful misconduct, or a breach of specific terms of the joint operating agreement.

D. Exculpatory Clauses

Joint operating agreements establish a general rule that each party bears a share of the expenses that arise from operations, with each party's share being in proportion to their ownership interest.¹⁹⁸ That expense-sharing scheme would be disrupted if a party to the agreement was liable to the other parties for some loss or expense arising from joint operations. The scheme also would be disrupted if one party incurred direct liability to third persons for some expense or loss arising from joint operations, and the other parties did not share direct liability, and they were excused, as between the parties, from paying their proportionate share of that expense. Because the Operator is the party that performs almost all activities necessary for joint operations, it is the Operator that has the greatest risk of incurring additional liability.

To help preserve the general rule of proportionate liability, most joint operating agreements contain an "exculpatory clause" that protects the Operator from liability "as Operator" to the Non-Operators for either losses sustained by the parties or liabilities incurred to third persons in connection with joint operations. This exculpatory protection has three notable limitations. First, although the exculpatory clause protects the Operator from liability as between the parties for liabilities incurred to third persons, the exculpatory clause of course does not affect the Operator's direct liability to third persons. Second, although the exculpatory clause protects the Operator from liability as Operator, the Operator still bears its proportionate share of liability in its role as one of the parties to the operating agreement.

Finally, and perhaps most significantly, exculpatory clauses typically do not give the Operator unconditional protection. For example, exculpatory clauses typically do not protect the Operator from liability arising from the Operator's gross negligence or willful misconduct.

The fact that the exculpatory clause does not provide unconditional protection creates the potential for disputes between the Operator and Non-Operators. One type of conflict involves factual disputes regarding whether particular action or inaction constituted gross negligence or

198. See, for example, art. VII.A of the 2015, 1989, 1982, and 1977 versions of the AAPL Form 610.

willful misconduct. But an issue that recently attracted more attention is whether the exculpatory clause's protections apply to liabilities arising from activities that are not part of operations and to liabilities arising from the Operator's alleged breach of some express duty.¹⁹⁹ Different courts have reached different conclusions. The different conclusions have come about partly because different exculpatory clauses have different wording, but sometimes different courts have reached different conclusions even when considering the same language.

1. Model Forms Used in the U.S.

The language of the exculpatory clause in the AAPL Form 610 has changed multiple times. In the 1956 version, the exculpatory clause was part of the same sentence that established a standard of care. The sentence provided: “[The Operator] shall conduct all such operations in a good and workmanlike manner, but it shall have no liability as Operator to the other parties for losses sustained, or liabilities incurred, except such as may result from gross negligence or from breach of the provisions of this agreement.”²⁰⁰ This clearly seems to create two exceptions to the protection provided by the exculpatory clauses—one for liabilities arising from gross negligence and a second for liabilities arising from a breach of the operating agreement.²⁰¹

When the 1977 version of the AAPL Model 610 was drafted, the exculpatory clause was again included in the same sentence that established a standard of conduct. But the 1977 exculpatory clause contains language different than that in the 1956 Form. In the 1977 Form, the relevant sentence provides: “[The Operator] shall conduct all such operations in a good and workmanlike manner, but it shall have no liability as Operator to the other parties for losses sustained or liabilities incurred, except such as may result from gross negligence or willful misconduct.”²⁰² The revision eliminated the express reference to an exception to the Operator's exculpation from liability for “a breach of the operating agreement,” but it added a “willful misconduct” exception. The exculpatory clause remained the same in the 1982 version of the Form 610.

199. See, e.g., Jonathan A. Hunter & Cheryl M. Kornick, *Operator Liability in the 21st Century: Is Being in Charge Still Worth It?*, 51 ROCKY MT. MIN. L. INST. 15-1 (2005).

200. 1956 AAPL 610 art. 5.

201. Ernest E. Smith & John S. Lowe, *The Operator: Liability to Non-Operators, Resignation, Removal and Selection of a Successor*, ROCKY MTN. MIN. L. FOUND. 2 (2008).

202. 1977 AAPL 610 art. V.A.

The 1977 and 1982 exculpatory clauses could be interpreted as expanding the Operator's protection by eliminating the exception for breach of the agreement. Under such an interpretation, the Operator could still be held liable as Operator for a breach of the agreement if the breach also constituted an example of gross negligence or willful misconduct. Such an interpretation received some support in commentary. For example, Professor Ernest E. Smith concluded, "[t]he history of the language used in the model form suggests that" the 1977 and 1982 exculpatory clauses protect the Operator even against liability for breaches of specific clauses of the joint operating agreement, provided that the breaches do not rise to the level of gross negligence or willful misconduct.²⁰³

This interpretation also received some support in case law. The leading case following this view is *Stine v. Marathon Oil Co.*,²⁰⁴ a diversity case from Texas. In *Stine*, the non-operator asserted that the Operator breached specific provisions of the parties' joint operating agreement by plugging and abandoning two wells without first informing the non-operator and giving him a chance to take over the wells, and also by failing to deliver certain information to the non-operators. The jury returned a verdict for the non-operator and the trial court entered a money judgment based on the verdict. The Operator appealed, arguing that it was protected by the exculpatory clause in the parties' agreement, which used the same language as is found in the exculpatory clauses found in the 1977 and 1982 Forms. The United States Fifth Circuit agreed with the Operator and reversed (in part). The Fifth Circuit held that the exculpatory language used in the 1977 and 1982 AAPL Form 610 agreements protects the Operator from liability, absent gross negligence or willful misconduct, for any action that the Operator takes in the capacity as Operator, even if the action constitutes a breach of the agreement.²⁰⁵

Alternatively, someone could argue—particularly that the 1977 and 1982 exculpatory clauses appear in the same sentence as a clause establishing a standard of conduct for "operations"—that the clauses have no application for liabilities arising from the Operator's breach of particular duties that are expressly imposed by the agreement, particularly if the duties are not part of "operations." This view also received some

203. Ernest E. Smith, *Duties and Obligations Owed by an Operator to Nonoperators, Investors, and Other Interest Owners*, 32 ROCKY MTN. MIN. L. INST. 12-30 (1986). For an interesting discussion of the meaning of "gross negligence" and "willful misconduct," with a focus on the context of the use of those terms in the Oil Pollution Act, see Patrick H. Martin, *The BP Spill and the Meaning of "Gross Negligence or Willful Misconduct,"* 71 LA. L. REV. 957 (2011).

204. 976 F.2d 254 (5th Cir. 1992).

205. *Stine*, 976 F.2d at 261.

support in commentary, as well as in the courts.²⁰⁶ For example, in contrast to *Stine's Erie-guess* that Texas law would apply the 1977 and 1982 exculpatory clause to all conduct by the Operator even if it involved breach of an express provision of the joint operating agreement, some Texas state appellate courts concluded that the clause would not apply to such breaches.²⁰⁷

Similarly, the United States Tenth Circuit concluded that exculpatory clauses based on the 1977 and 1982 language would not apply to breaches of express clauses of the agreement. In *Shell v. Rocky Mountain Production, LLC v. v. Ultra Resources, Inc.*, a non-operator claimed that the Operator breached the operating agreement's clauses regarding obtaining competitive prices for drilling.²⁰⁸ The Operator argued that the exculpatory clause applied and that the non-operator could not recover unless it proved that the Operator had engaged in gross negligence or willful misconduct. The United States Tenth Circuit disagreed, holding that the clause did not protect the Operator against liability for breaches of duties expressly imposed by the joint operating agreement.²⁰⁹ Thus, *Ultra Resources* and *Stine* reached opposing views on the scope of the 1977 and 1982 exculpatory clauses.

The exculpatory clause was changed in the 1989 version of the AAPL Form 610. Like the prior Forms, the 1989 Form included both the exculpatory clause and the clause that establishes a standard of conduct in a single sentence. In the 1989 Form, however, both of those clauses have different language than in earlier drafts of the Form. In the 1989 Form, the sentence reads:

Operator shall conduct its activities under this agreement as a reasonable prudent operator, in a good and workmanlike manner, with due diligence and dispatch, in accordance with good oilfield practice, and in compliance with applicable law and regulation, but in no event shall it have any liability as Operator to the other parties for losses sustained or liabilities incurred except such as may result from gross negligence or willful misconduct.

The Texas Supreme Court addressed the scope of the 1989 protection in *Reeder v. Wood County Energy, LLC*.²¹⁰ In that case, non-operators

206. Gary Conine, *The Prudent Operator Standard: Applications Beyond the Oil and Gas Lease*, 41 NATURAL RES. J. 23 (2001).

207. See, e.g., *Castle Tex. Prod. Ltd. P'ship v. Long Trusts*, 134 S.W.3d 267, 283 (Tex. App. Tyler 2003); *Abraxus Petroleum Corp. v. Hornburg*, 20 S.W.3d 741 (Tex. App. El Paso 2000).

208. 415 F.3d 1158 (10th Cir. 2005).

209. *Id.*

210. 395 S.W.3d 789 (Tex. 2013).

asserted that the Operator committed various breaches of the joint operating agreement. The Texas Supreme Court opened its discussion of the issues by stating that it needed to decide “whether the exculpatory clause in the JOA sets the standard to adjudicate the breach of contract claims against [the Operator].”²¹¹ Ultimately, the court decided that the 1989 clause would apply. The court noted that the sentence containing the exculpatory clause had been changed to provide that the Operator must conduct its “activities” as a reasonably prudent operator, whereas the 1982 and 1977 versions of the clause had applied to operations. Thus, the change seemed to broaden the prudent operator standard from just operational activities to all activities. The court reasoned that the change in language similarly had the effect of expanding the scope of liability protection from operational activities to all activities.²¹² Thus, *Reeder* gave a broad interpretation of the 1989 exculpatory language, concluding that it provides protection for all activities of the Operator, unless the conduct involves gross negligence or willful misconduct.²¹³ The scope of the 1982 and 1977 exculpatory clauses was not before the court, and it did not opine on the scope of those clauses, but the court’s emphasis on the significance of the change in language from “operations” to “activities” could be read as implying that the 1982 and 1977 language might not apply to breaches of duties expressly imposed by the joint operating agreement.

The language of the exculpatory clause was revised again in the 2015 version of the AAPL Form 610. The revision seems to be a response to *Reeder*. Like the 1989 Form, the 2015 Form uses broad language when it imposes a standard of conduct—applying the standard to all of the Operator’s “activities,” not just to operations. But the portion of the language that contains the exculpatory language now refers only to operations. In particular, the language reads:

Operator shall conduct its activities under this agreement as a reasonably prudent operator, in a good and workmanlike manner, with due diligence and dispatch, in accordance with good oilfield practice, and in compliance with applicable law and regulation. However, in no event shall it have any liability as Operator to the other parties for losses sustained or liabilities incurred in connection with authorized or approved operations under this agreement except such as may result from gross negligence or willful misconduct.²¹⁴

211. *Reeder*, 395 S.W.3d at 792.

212. *Id.*

213. *Id.* at 795.

214. 2015 AAPL 610 art. V.A.

There is still potential for a court to interpret the exculpatory clause broadly. The new language does not go back to the 1956 language, which expressly put liabilities arising from a breach of the agreement outside the scope of the exculpatory clause. Further, a court could interpret “in connection with” broadly. But given the history of the changes to the clause and the cases interpreting the exculpatory clause, it seems likely that a court will conclude that the 2015 exculpatory clause has a narrower scope than that of the 1989 clause as it is interpreted in *Reeder*.

AAPL Form 710 states in capital letters, “OPERATOR SHALL NOT BE LIABLE TO NON-OPERATORS FOR LOSSES SUSTAINED OR LIABILITIES INCURRED, EXCEPT AS MAY RESULT FROM OPERATOR’S GROSS NEGLIGENCE OR WILLFUL MISCONDUCT.”²¹⁵ This sentence does not expressly restrict application of the exculpatory clause to any particular sort of activity. Thus, the exculpation clause arguably applies to any sort of activity, even administrative tasks, and it arguably applies even if the Operator’s action or inaction constitutes a breach of the agreement. On the other hand, the clause appears in the middle of a section that deals with operations and the standard of care for such operations. Accordingly, someone could plausibly argue that the clause applies only with respect to operational activities and that it protects the Operator against liability for an alleged breach of a standard of care (so long as the breach does not arise to the level of gross negligence), but not against liability for breach of an express and specific contractual requirement.

AAPL offshore Form 810 contains language almost identical to that which is used in Form 710. Further, like the exculpatory clause in Form 710, the exculpatory clause in Form 810 is written in all capital letters, and it appears in the middle of a paragraph that imposes a standard of care for the conduct of operations. RMMLF Form 3 also gives the Operator broad protection—perhaps broader than the AAPL Forms—by stating that the “Operator shall not be liable to any other Party for losses sustained in the

215. AAPL 710 art. 5. As between the parties to the operating agreement, this clause is designed to protect the Operator from losses or liabilities arising from the Operator’s own negligence, as long as the negligence does not rise to the level of gross negligence. Under the laws of some states, an indemnity clause that protects the indemnitee from liability for its own negligence must be conspicuous (the clause may also need to either expressly state that it applies even if the indemnitee was negligent or be clear and unambiguous in its application). All capital letters may help the clause satisfy the requirement of being conspicuous. State law would apply in state waters. Also, on the federal Outer Continental Shelf, the contract law of the nearest state typically is borrowed as surrogate federal law to govern disputes.

conduct of its operations hereunder, except such losses as may result from Operator's bad faith."²¹⁶

2. Forms Used Outside the U.S.

Model form operating agreements used outside the United States also contain exculpatory clauses that protect the Operator, some of which provide even broader protection to the operator than the forms most commonly used in the U.S.

The Australian and Canadian forms contain exculpatory clauses that are similar in scope to the exculpatory clauses in most of the AAPL Forms. AMPLA section 6.5 provides that "the Operator is not liable to the [Non-Operators] for any loss sustained or liability incurred in connection with the" joint operations, unless the Operator or a person for whom the Operator is vicariously liable "has committed fraud or Wilful Misconduct."²¹⁷ AMPLA section 6.6 requires each Non-Operator to indemnify the Operator for the Non-Operator's proportionate share of losses or liabilities not caused by such fraud or Wilful Misconduct, and section 6.7 requires the Operator to indemnify the other parties for losses or liabilities that are caused by such fraud or Wilful Misconduct. The CAPL Form is somewhat similar.²¹⁸

The UKCS Form, though, contains an exculpatory clause that may give the Operator even broader protection. The UKCS Form provides that the parties' obligation to indemnify the Operator in proportion to their respective ownership shares applies to all liabilities arising from operations, except those that arise from the Operator's "Wilful Misconduct."²¹⁹ The UKCS Form defines "Wilful Misconduct" in a manner that probably encompasses both gross negligence and intentional misconduct, but only by as meaning "an intentional or reckless disregard by *Senior Managerial Personnel* of Good Oilfield Practice or any of the terms of this Agreement."²²⁰ Curiously, the UKCS Form does not define "Senior Managerial Personnel," but (in what may be a drafting error) it defines "Senior Supervisory Personnel" in part as meaning "any person

216. Rocky Mountain Form 3 art. 4.5.

217. AMPLA cl. 6.5.

218. As between the parties, CAPL generally limits the Operator's liability as Operator to circumstances in which losses or liabilities arise from "Gross Negligence or Wilful Misconduct of the Operator, its Affiliates or their respective directors, officers, employees, agents or contractors." CAPL cl. 4.02. Barring such circumstances, the parties agree to bear liabilities arising from operations in proportion to their ownership share and to indemnify the Operator against liability exceeding its ownership share. CAPL cl. 4.01.

219. UKCS cl. 22.2.2.

220. UKCS cl. 1.1 (emphasis added).

employed by a Party as a director or other corporate officer or who occupies a senior managerial position in such Party with direct responsibility for the conduct of operations.”

The 2012 AIPN Form contains multiple options for the language of the exculpatory clause, and the parties will need to choose which option they prefer. The main option provides some of the broadest protection found in any model form. This exculpatory clause provides the Operator with protection against virtually all liabilities, even against liabilities arising from its gross negligence or willful misconduct;²²¹ but the Form also contains an optional clause that can negate the exculpatory clause in whole or part for liabilities that arise from the gross negligence or willful misconduct of “Senior Supervisory Personnel.”²²² If that option is chosen, the level of protection provided to the Operator will still be broader than that provided by most model forms, and will be similar to that provided by the UKCS Form.

V. RESIGNATIONS OF THE OPERATOR AND AUTOMATIC TERMINATIONS

Most joint operating agreement forms contain provisions recognizing that an Operator may resign, and some forms also specify circumstances that will result in a “deemed resignation” or an automatic termination of a party’s status as Operator. The first subsection below discusses the way that model form joint operating agreements govern express resignations by the Operator, and the next subsection discusses provisions that provide for “deemed resignations” or automatic termination of a party’s status as Operator when particular circumstances arise.

A. Express Resignations

All of the commonly-used JOA forms expressly allow the Operator to resign, though each requires that the Operator give appropriate notice and specifies some minimum time between the notice of resignation and the effective date of the resignation. The delay in the effective date of the resignation is designed to give the parties adequate time to select a new Operator and for that Operator to prepare to assume the role of Operator.

For example, under the 2015 version of AAPL Form 610, the “Operator may resign at any time by giving written notice thereof to Non-Operators.”²²³ Similar provisions appear in each of the prior versions of

221. 2012 AIPN art. 4.6.A and 4.6.B.

222. 2012 AIPN art. 4.6.D.

223. 2015 AAPL 610 art. V.B.1.

The giving of notices, including notices of resignation, is governed by Article XII under the 2015, 1989, 1982, and 1977 Forms. Section 20 of the 1956 Form

AAPL Form 610, as well as in the AAPL forms designed for use offshore.²²⁴ The 2015 Form states that a resignation will be effective “on the earlier of . . . [t]he time and date that a successor Operator has been selected . . . and assumes the duties of Operator . . . or 7:00 o’clock A.M. on the first day of the calendar month following the expiration of ninety (90) days after the giving of notice of resignation.”²²⁵ This language slightly differs from the language used in the prior AAPL forms, but the difference in language may not bring about a substantive change in the effective date and time of resignations. The 1989, 1982, and 1977 Forms each provided that a resignation generally would “not become effective until 7:00 o’clock A.M. on the first day of the calendar month following the expiration of ninety (90) days after the giving of notice of resignation . . . unless a successor Operator has been selected and assumes the duties of Operator at an earlier date.”²²⁶

The CAPL Form allows the Operator to resign with just forty-five days’ notice²²⁷—a *shorter* notice period than mandated by the AAPL Forms—but most joint operating agreements used outside the U.S. provide for a *longer* delay between notice of resignation and the effective date of resignation. The AIPN 2012 Model provides that, “Subject to Article 4.11, Operator may resign as Operator by so notifying the other Parties at least one hundred and twenty (120) Days before the effective date of such resignation.” Article 4.11.E of the AIPN Form further provides that a resignation is not effective until any necessary government approvals are obtained. This provision is included in recognition of the fact that many host governments prohibit a change in Operator without government consent. The 2011 version of AMPLA, an Australian form, provides that an Operator may resign, “having

governed the giving of notice. Article XII specifies what methods of delivery may be used and the point in time when delivery is considered complete (typically, “when received”). An Operator that wishes to resign should make sure that it uses an authorized method of delivering its notice of resignation in order to avoid a potential dispute regarding whether the resignation was effective.

224. The 1989, 1982, and 1977 Forms each contained an Article V.B.1. that included a sentence identical in language that found in the 2015 Form—“Operator may resign at any time by giving written notice thereof to Non-Operators.” Section 20 of the 1956 Form contained a provision that was identical in substance: “Operator may resign from its duties and obligations as Operator at any time upon written notice of not less than ninety (90) days given to all other parties.” Article 4.3 of AAPL 810 generally allows the Operator to resign by giving written notice. *See also* AAPL 710 art. 4.3.

225. 2015 AAPL 610 art. V.B.7.

226. This provision is found in Article V.B.1. of the 1989, 1982, and 1977 Forms. Section 20 of the 1956 Form provided that the Operator could resign “upon written notice of not less than ninety (90) days.” *See also* AAPL-710 (2002) § 4.6; AAPL-810 (2007) § 4.6.

Article 4.2 of Rocky Mountain Form 3 provides that the Operator may resign with 3 months’ notice.

227. CAPL cl. 2.04.

given at least 180 days' notice."²²⁸ A form used on the United Kingdom Continental Shelf provides that an Operator has the "right to resign . . . at the end of any Month by giving not less than one hundred and eight (180) days notice to the Participants or such shorter period of notice as" a committee of the parties "may decide."²²⁹

If the Operator ceases performance of its duties early, it may be liable for breach of contract. In *Lancaster v. Petroleum Corp.*, the parties were using a joint operating agreement which provided: "Operator may resign from its duties and obligations as Operator at any time upon written notice of not less than ninety (90) days given to all other parties."²³⁰ On March 16, 1977, a natural gas well blew out. On March 21, the Operator notified the other parties that it was resigning. On March 25, just four days after giving notice, the Operator threatened to plug and abandon the well unless the other parties found a replacement Operator by 5:00 p.m. that day. One of the parties—Lancaster—found a company that agreed to become Operator on short notice, but only if Lancaster turned over a substantial portion of a back-in interest that it owned. Lancaster agreed, perhaps feeling that it had little choice. The well was brought under control and recompleted, after which it produced in paying quantities, though it never reached payout.

Lancaster brought suit against the former Operator for breach of the JOA provision that required the Operator to give ninety days' notice before its resignation would be effective. The district court found that the Operator did not breach the contract, but the Louisiana Third Circuit reversed, concluding that it was "abundantly clear" that the Operator had breached the contract's ninety-day notice requirement.²³¹ The court then awarded damages based on the market value of the mineral interest that Lancaster relinquished in order to entice a company to agree to become Operator on such short notice.²³²

Neither the 2015 Form nor the earlier AAPL Forms specify who decides whether the successor Operator will assume the duties of Operator prior to the date on which the outgoing Operator's resignation would otherwise be effective. Because the delay in effective date protects the Non-Operators, it seems clear that the outgoing Operator should not have the right to demand that the successor Operator assume the duties of

228. AMPLA cl. 6.2(b).

229. UKCS cl. 5.2.1.

230. *Lancaster v. Petroleum Corp.*, 491 So. 2d 768, 776 (La. App. 3rd Cir. 1986). The quoted language is identical to that in the first sentence of Section 20 of the 1956 Form. Based on this and other quoted language, it appears that the parties' agreement was largely based on the 1956 Form, but that it contained additional provisions.

231. *Id.* at 777.

232. *Id.* at 777-8.

Operator “earlier.” Further, the parties other than the successor Operator and outgoing Operator probably do not have a right to demand that the successor assume responsibilities earlier. But if the successor Operator has been selected and believes it is ready to assume its new duties earlier, does the successor have a right to demand that the outgoing Operator relinquish control earlier? Or, must the outgoing Operator, the other parties, or both, concur? If the other parties must concur, is a majority sufficient?

B. Deemed Resignations and Automatic Terminations of Operator

Under the 2015 version of AAPL Form 610, the Operator will be “deemed” to have resigned upon the occurrence of any one of three different circumstances. This is governed by Article V.B.2, which states:

2. Events Deemed Resignation of Operator: If, after the effective date of this agreement, Operator (i) terminates its legal existence, (ii) sells, transfers or has a loss of title to more than_% of its interest in the Contrast Area as shown on Exhibit “A,” or (iii) is no longer capable of serving as Operator, then Operator shall be deemed to have resigned without any action by Non-Operators, except for selection of a successor Operator. A change of a corporate name or type of business entity of Operator shall not be deemed resignation of Operator.

The 1989 and 1982 Forms also provided for “deemed” resignations upon the occurrence of any one of three circumstances, but the 2015 version of the deemed-resignation is different from the two prior versions. Like the 2015 Form, the 1989 and 1982 Forms provided that the Operator would be deemed to have resigned if it terminates its legal existence or it becomes incapable of serving as Operator. But otherwise, the 1989 and 1982 Forms only provided for a deemed resignation in the event that the Operator no longer owned an interest “hereunder in the Contract Area.” In contrast, as shown by the quoted language above, the 2015 Form contemplates that the parties may provide that the Operator is deemed to have resigned if it reduces its ownership interest by a specified amount.

This change provides parties with more flexibility, which should be welcome. If parties wish to avoid having an Operator that owns no working interest whatsoever, they may wish to avoid having an Operator that owns only a small interest. But parties who use the 2015 Form should be careful to make sure they fill-in the blank contained in Article V.B.2. If the parties fail to fill-in the blank, it is not clear how a court would interpret that portion of Article V.B.2. For example, a court might treat the blank as

a zero, or it might conclude that the “transfer-of-interest” portion of the deemed-resignation clause will have no effect.

Further, parties should be careful to make sure, when they fill-in the blank, that they all have the same understanding of the clause. At least two potential bases for confusion exist. First, as written, the clause appears to require the parties to specify the portion of the Operator’s interest that must be transferred in order for there to be a deemed resignation, not the minimum portion that must be retained in order to avoid a deemed resignation.

Second, there could be confusion about what is meant by the percentage specified when they fill-in the blank. The percentage specified in Article V.B.2 refers to the percentage of the Operator’s interest, not the percentage of the total that must be transferred in order to trigger a deemed resignation. Thus, if the Operator starts with 40% of the total working interest, and the parties wish for there to be a deemed resignation if the Operator’s interest falls below 10% of the total working interest, the parties should fill-in the blank with “75” (because it would require the Operator transferring more than 30% of the total interest, which would equal 75% of its own interest, in order to trigger a deemed resignation).

If parties use the 2015 Form, they may wish to alter the form to address those potential bases of confusion. In addition, in the event that there is a change in the Operator, the parties should consider whether they wish to revise the Article V.B.2 percentage. Suppose, for instance, that the parties choose a successor Operator that owns 20% of the total working interest to replace an Operator that owned a 40% interest, but the parties still wish for a deemed resignation to occur in the event that the Operator’s total working interest falls below 10% of the total working interest. In that case, the parties would need to amend Article V.B.2 to provide that there would be a deemed resignation of the Operator if it transferred more than 50% of its own interest. Otherwise, if the parties retain the language providing that a deemed resignation will occur in event that the Operator transfers 75% of its interest, the new Operator that starts with 20% of the total working interest could drop to a 5% total interest before a deemed resignation occurs.

A fourth potential change relates to the fact that Article V.B.2 refers to a sale, transfer, or loss of title. The parties may wish to supplement Article V.B.2 to provide for the possibility of a deemed resignation if the Operator’s interest is reduced because of a failure of title under Article

IV.B.1,²³³ as well as a loss of title under Article IV.B.2,²³⁴ but not a loss under Article IV.B.3. (A loss under Article IV.B.3 does not result in a readjustment of ownership percentages under the JOA, which are reflected on Exhibit “A.”)²³⁵

Other model forms also provide for various circumstances that will result in an automatic termination. Such circumstances include the Operator selling its entire ownership interest (or, under some agreements, selling enough that its ownership share falls below a specified percentage or below the percentage interest held by another party), and material breaches of the agreement that are not corrected after notice and a reasonable time to cure.²³⁶

C. Effect of Bankruptcy on Operator Status

The 2015 and 1989 versions of AAPL Form 610 provide that, if an Operator becomes insolvent, bankrupt, or is placed in receivership, the Operator will be “deemed to have resigned without any action by Non-Operators, except the selection of a successor.”²³⁷ Those Forms recognize,

233. A failure of title can occur under art. IV.B.1 when the parties are not co-owners of a single lease, but instead they have each contributed separate leases or other mineral interests to a group of interests that will be governed by the JOA. In such circumstances, each party’s individual ownership percentage in the JOA will, presumably, reflect some agreed upon estimate of the value that the interest contributed by that party bears to the total value of all the interests governed by the JOA. A failure of title occurs if it is determined that title to an oil and gas lease or other mineral interest contributed by a party was invalid as of the effective date of the JOA. In the event of a failure of title, the ownership percentage (in the JOA) of the party who contributed that lease is adjusted downward unless the party timely acquires a new lease or otherwise cures the title failure. For a discussion of loss of title versus failure of title, see Gary B. Conine and Bruce M. Kramer, *Property Provisions of the Joint Operating Agreement*, ROCKY MTN. MIN. L. FDN. SPECIAL INST. ON OIL AND GAS AGREEMENTS: JOINT OPERATIONS (2008).

234. A loss of title occurs under art. IV.B.2 if an oil and gas lease that was contributed by a party terminates after the effective date of the JOA because some payment necessary to maintain the lease was not paid. If the party that was responsible for making the payment cannot obtain a new lease to compensate for the loss of title, that party’s ownership percentage in the JOA is reduced.

235. If a lease that is subject to the JOA terminates after the effective date of the JOA because of a failure to develop the lease or to comply with implied covenants, there is no adjustment of ownership in the JOA.

236. 1989 AAPL 610 art. V.B.1; 1982 AAPL 610 art. V.B.1; 1977 AAPL 610 art. V.B.1; AAPL 710 art. 4.3; AAPL 810 art. 810; AMPLA cl. 6.2; CAPL cl. 2.02; Rocky Mountain Form 3 art. 4.3.

237. This is contained in art. V.B.3 of the 2015 and 1989 Forms. The 1982 and 1977 Forms each provide in art. V.B.1 that the Non-Operators can remove the Operator if it “becomes insolvent, bankrupt or is placed in receivership.”

however, that bankruptcy law or a bankruptcy court might prevent enforcement of this provision. The Forms provide:

If a petition for relief under the federal bankruptcy laws is filed by or against the Operator, and the removal of Operator is prevented by the federal bankruptcy court, all Non-Operators and Operator shall comprise an interim operating committee to serve until Operator has elected to reject or assume the agreement to the Bankruptcy Code.²³⁸

If there are only two parties to the agreement, a third person is appointed to the operating committee, presumably for the purpose of helping avoid deadlocks on committee votes.²³⁹

Other model forms also contain clauses stating either that the party serving as Operator will cease being Operator in the event that it enters bankruptcy or becomes insolvent or that the other parties have the right to remove the bankrupt (or insolvent) party from the position of Operator.²⁴⁰

VI. REMOVAL OF OPERATOR

Most operating agreements allow the Non-Operators to remove the Operator under certain circumstances. The circumstances under which removal is allowed can vary from one model operating agreement to another. Some operating agreements only allow removal for “good cause” or other specified reasons. Under other operating agreements, no special reason may be needed for the Non-Operators to remove the Operator. Like the circumstances (if any) needed to justify removal, the procedures for removal also will vary based on the particular operating agreement.

The 2015 version of the AAPL Form 610 contains different rules for removing an Operator that owns an interest governed by the agreement than for removing an Operator that does not own such an interest.²⁴¹ The 2015 Form’s rules for removing an Operator that owns an interest are similar to the rules for removing an Operator under earlier versions of the AAPL Form 610 (the earlier forms generally presume that an Operator will own an interest). Below, this Article discusses the general rules for removing an Operator under the 610 Forms (this includes the rules under the pre-2015 Forms and the 2015 rules for removing an Operator that owns

238. 2015 AAPL 610 art. V.B.3; 1989 AAPL 610 art. V.B.3.

239. 2015 AAPL 610 art. V.B.3; 1989 AAPL 610 art. V.B.3.

240. 1982 AAPL 610 art. V.B.1; 1977 AAPL 610 art. V.B.1; AAPL 710 art. 4.4(a); AAPL 810 art. 4.4.2(c); AIPN art. 4.10.A.1; AMPLA cl. 6.2.D; CAPL cl. 2.02A(a); UKCS cl. 5.3.2(a).

241. See 2015 AAPL 610 art. V.B.4 (Operator that owns an interest) and art. V.B.5 (non-owning Operator).

an interest), and the 2015 Form's rules for removing a "non-owning Operator."

A. General Rules for Removal of Operator Under AAPL Forms

The rules for removal include the substantive requirements needed to justify removal and the procedures that must be followed to remove an Operator.

1. The Substantive Grounds Necessary for Removal

The usual circumstance likely will be that the Operator owns an interest. Under the 2015 and 1989 versions of Form 610, an Operator that owns an interest "may be removed only" if "good cause" for removal exists and the Operator fails to "cure the default" that constitutes good cause within a specified time after delivery of a notice "detailing the alleged default."²⁴² The 2015 Form states that "'good cause' shall include, but not be limited to, Operator's (i) gross negligence or willful misconduct; (ii) the material breach of or inability to meet the standards of operation contained in Article V.A.; or (iii) material failure or inability to perform its obligations or duties under this agreement."²⁴³ The 1989 Form describes "good cause" in substantively identical language.

The "standard of operation" that is referenced in both the 2015 and the 1989 Forms' definition of "good cause" is described in identical language in Article V.A of each Form. The language states that the Operator must "conduct its activities under this agreement as a reasonably prudent operator, in a good and workmanlike manner, with due diligence and dispatch, in accordance with good oilfield practice, and in compliance with applicable law and regulations."

The 1982 and 1977 Forms did not refer to "good cause" as a prerequisite for removal, but those Forms only authorized removal in certain circumstances. Under the 1982 and 1977 Forms, the Non-Operators can remove the Operator "if it fails or refuses to carry out its duties hereunder, or becomes insolvent, bankrupt or is placed in receivership."²⁴⁴ The 1982 and 1977 Forms do not require that the operator

242. 2015 AAPL 610 art. V.B.4. Article XII of the form governs what is required for a "delivery."

243. 2015 AAPL 610 art. V.B.4.

244. This provision is contained in art. V.B.1 of each of the Forms. There is some discussion of "good cause" and cases dealing with this issue in commentary. See, e.g., Christopher S. Kulander, *Old Faves and New Raves: How Case Law Has Affected Form Joint Operating Agreements—Problems and Solutions (Part Two)*, 1 OIL AND GAS, NAT. RES., AND ENERGY J. 165 (2015).

be given an opportunity to cure the grounds for removal. The 1956 version of the AAPL Model Form did not expressly provide for removal.

AAPL Form 710 authorizes removal of the Operator in circumstances similar to the recent 610 forms. The parties may remove the Operator if the Operator “commits a substantial breach of a material provision of the operating agreement” and fails to cure it within a specified time, or if the Operator becomes insolvent.²⁴⁵ Form 710 also authorizes the parties to remove the Operator if the Operator makes a partial transfer of its working interest (other than to an affiliate) that is large enough so that the Operator no longer has the largest working interest of all parties to the agreement.²⁴⁶ The Operator is automatically removed if it ceases to own a working interest.²⁴⁷ AAPL Form 810 authorizes removal if the Operator commits “a substantial breach of a material provision” of the joint operating agreement and, after notice of the breach, either fails to correct the breach within thirty days, if the breach is one that can reasonably be cured within that time, or fails to commence a cure within thirty days if the breach is one that cannot be cured within thirty days.²⁴⁸

2. Procedure for Removal

Under the 2015 and 1989 versions of Form 610, an operator cannot be removed unless it fails to cure the grounds for removal within a specified time after receiving notice of the “default.” The pre-removal notice to the Operator must be in writing.²⁴⁹ The amount of time to which the Operator is entitled for curing the default depends on the circumstances. The general rule is that the Operator is entitled to thirty days, but the Operator is only entitled to forty-eight hours to cure “if the default concerns an operation then being conducted.”²⁵⁰ As previously noted, the 1982 and 1977 Forms do not require that the Non-Operators give the Operator an opportunity to cure.

Subject to the existence of grounds for removal and the Operator’s right to attempt to cure such “default,” the 2015 and 1989 Forms provide that Non-Operators can remove the Operator “by the affirmative vote of Non-Operators owning a majority interest based on ownership as shown on Exhibit ‘A’ remaining after excluding the voting interest of Operator.”²⁵¹ Similarly, if grounds for removal exist, the 1982 and 1977 Forms allow the

245. AAPL 710 art. 4.4(d).

246. AAPL 710 art. 4.4(c).

247. AAPL Form 710 art. 4.3.

248. AAPL Form 810 art. 4.4.2(b).

249. 2015 AAPL Form 610 art. V.B.4; 1989 AAPL Form 610 art. V.B.1.

250. *Id.*

251. *Id.*

Non-Operators to remove the Operator by the vote of parties “owning a majority interest . . . remaining after excluding the voting interest of Operator.”²⁵² But the 1982 and 1977 Forms add an additional requirement—those Forms require that there be two or more Non-Operators voting for removal.²⁵³ The 2015 and 1989 Forms do not include such a requirement.

Thus, if the Operator has a 40% ownership interest, so that the Non-Operators collectively own 60% “after excluding the voting interest of Operator,” the parties seeking removal of the Operator under Form 610 would need an “affirmative vote” for removal from a majority of the 60%. In other words, they would need a vote for removal from Non-Operators holding interests that exceed 30%, assuming that all of the Non-Operators vote. Further, under the 1982 and 1977 Forms, that vote would need to come from at least two Non-Operators. If one of the Non-Operators held a 35% interest, that party’s vote would not be sufficient to remove the Operator.

It is worth noting that the Forms require an “affirmative vote” of a majority in interest (after excluding the Operator’s interest), not a majority in interest of those who choose to vote. Thus, if a Non-Operator fails to vote or votes to abstain, that non-vote or abstention may effectively work as a vote against removal. That being said, the AAPL Forms do not attempt to govern the removal process in minute detail. For example, the Forms do not specify whether an in-person meeting is required or whether votes by mail or email are sufficient. The Forms also do not specify whether votes (assuming that there is a meeting) will be by voice vote or in writing or who will chair the meeting.

B. Removal of Non-Owning Operator Under 2015 Version of AAPL Form 610

The 2015 version of the AAPL Form 610 contains special rules for removing an Operator that does not own an interest governed by the agreement.²⁵⁴ Such an Operator may be removed in one of two ways. First, such an Operator “may be removed at any time, with or without good cause, by an affirmative vote of parties owning a majority ownership interest” under the agreement.²⁵⁵ This procedure does not require notice or an opportunity to cure.

Second, if good cause for removal of a non-owning Operator exists, the Operator may be removed by a vote of Non-Operators owning a

252. 1982 AAPL Form 610 art. V.B.1; 1977 AAPL Form 610 art. V.B.1.

253. 1982 AAPL Form 610 art. V.B.1; 1977 AAPL Form 610 art. V.B.1.

254. 2015 AAPL Form 610 art. V.B.5.

255. *Id.*

majority of the interest that remains after excluding the interest of any Affiliate of the Operator.²⁵⁶ Removal of a non-owning Operator under this second method must follow the removal procedure specified for removing an Operator that owns an interest.²⁵⁷ Thus, the Operator would have to be given written notice and time to cure the alleged default.

The special rules for removal of a non-owning Operator are new in the 2015 Form. Before, there was no need for such provisions because the prior versions of the AAPL Form 610 required that the Operator own an interest that was governed by the agreement.

C. Forms Used Outside the U.S.

Like the AAPL Forms, model form operating agreements used outside the United States typically provide that the Operator may be removed in the event of a serious breach of its duties. The 2012 AIPN Form provides that the Non-Operators may remove the Operator if the Operator commits a material breach of the joint operating agreement and, after being given notice of the breach, either fails to commence a cure within thirty days or fails to diligently pursue a cure to completion.²⁵⁸ The Form contains blank spaces that give the parties the chance to choose the percentage vote (in ownership interest) of the Non-Operators that is required to remove the Operator and whether a certain number of Non-Operators (by heads) also must vote in favor of removal in order for the Operator to be removed.²⁵⁹ If the Operator disputes whether it committed a material breach or failed to cure it, the Operator remains appointed until the matter is resolved as provided in the agreement's dispute resolution section (typically by arbitration).²⁶⁰

The AMPLA Form provides that “[t]he appointment of the Operator continues [until] the Operator commits a Breach Default Event and fails to remedy the default within 60 days of service of a written notice of default served by a [Non-Operator].”²⁶¹ The Form defines “Breach Default Event” as including various insolvency events or a “material breach of any of its material obligations” other than a failure to timely pay money due under the agreement.²⁶² Clause 5.3.1 of the UKCS form contains a similar provision.

256. *Id.*

257. *Id.*

258. 2012 AIPN art. 4.10.B.

259. *Id.*

260. *Id.*

261. AMPLA cl. 6.2(d).

262. AMPLA cl. 1.1.

The CAPL Form also has a unique means of removal—the “challenge of operator.” Clause 2.03.A provides that, if any non-operator party is prepared to conduct joint operations “on more favourable terms and conditions,” it can propose that it do so. The existing Operator then has sixty days in which to agree to operate on the terms proposed by the challenger (in which case the incumbent Operator remains as Operator) or to resign (in which case the challenger is obligated to assume the operatorship on the terms it stated in the challenge). Given that Operators generally are expected to serve on a “no gain, no loss” basis, it is not clear that this sort of clause would be useful in many cases, though it is possible that a challenger would offer to charge less overhead than allowed under the contract or less for the use of its own personnel and equipment than an incumbent Operator.

VII. SELECTION OF SUCCESSOR OPERATOR

Most model form operating agreements contain provisions governing the selection of a “successor Operator.” Often, these include substantive requirements that parties must own interests governed by the joint operating agreements in order to qualify for consideration as the successor operators. In addition, model forms generally contain provisions to govern the selection procedure.

A. General Requirement that Successor Operator Own an Interest

The 1989, 1982, and 1977 versions of AAPL Form 610 require that the successor Operator be chosen from amongst the parties to the joint operating agreement, which seems to limit the allowable candidates to those who own an interest governed by the joint operating agreement.²⁶³ (The 1956 version did not impose such a requirement.)²⁶⁴ The AAPL 710 form also states that the parties must choose any successor Operator “from amongst the Parties.”²⁶⁵

The 2015 version of AAPL Form 610 imposes a general requirement that the Operator own an interest, but the Form also expressly recognizes that the parties may choose a “non-owning Operator.”²⁶⁶ The 2015 Form goes on to state, however, that a “condition precedent” to a non-owner serving as Operator is that the “non-owning Operator and the Non-

263. This requirement is found in art. V.B.2 of the 1989, 1982, and 1977 versions of AAPL Form 610.

264. 1956 AAPL 610 art. 20, entitled “Resignation of Operator.”

265. AAPL 710 art. 4.5.

266. 2015 AAPL 610 art. V.A.; A non-owning operator is sometimes called a “contract operator.”

Operators must enter into a separate agreement, or insert Article XVI provisions [into the joint operating agreement], to govern the relationship between them.”²⁶⁷ Presumably, the parties to the joint operating agreement must unanimously agree to such a separate agreement or to such Article XVI provisions as a prerequisite to service of a non-owning Operator.

Although the 1989, 1982, and 1977 Forms require that any successor Operator be chosen from amongst the parties that own an interest, courts sometimes find that the parties waived this requirement or that they are estopped from raising an objection to the Operator’s lack of ownership interest when the parties chose a non-owning party as Operator and one of the parties did not object until the new Operator served for some time.²⁶⁸

Several other model forms do not expressly state that a successor Operator must own an interest governed by the agreement, but sometimes the forms seem to assume that a successor Operator will own such an interest. For example, clause 2.06 of the CAPL Form provides that certain circumstances, such as insolvency, will preclude a “Party” from being appointed as Successor Operator. Companies that are “Parties” to the joint operating agreement will be owners. Obviously, the intent of Clause 2.06’s reference to “Party” is not to preclude insolvent *owners* from being selected as a successor Operator while allowing insolvent non-owners to be the successor Operator. Rather, the form simply assumes that the entity chosen to be the successor Operator will be a “Party” and hence an owner.

B. Procedure for Choosing Successor Operator Under AAPL Forms

If an Operator resigns or is removed, the parties must elect a successor Operator.²⁶⁹ The parties entitled to vote include all parties that own an interest at the time the election occurs, including any new parties to whom the outgoing Operator has transferred its interest. This rule is made explicit in the 2015 Form, which states, “[t]he successor Operator shall be selected by . . . parties. . . including . . . the former Operator and/or any transferee(s) of the former Operator’s interest, to the extent that they are owners within

267. *Id.*

268. Oklahoma Oil & Gas Expl. Drilling Program 1983-A v. W.M.A. Corp., 877 P.2d 605, 608 (Okla. Civ. App. 1994); Oil Corp. v. Hillin, 890 S.W.2d 931, 934 (Tex. App. El Paso 1994).

269. The five versions of the AAPL 610 Model Form each provide that, after an Operator has resigned or been removed, a successor Operator “shall” be selected by “the parties.” 2015 AAPL 610 art. V.B.6; 1989 AAPL 610 art. V.B.2; 1982 AAPL 610 art. V.B.2; 1977 AAPL 610 art. V.B.2; 1956 AAPL 610 art. 20. AAPL Forms 710 and 810 also state that, after resignation or removal of an Operator, the parties “shall” choose a successor Operator. AAPL 710 art. 4.5; AAPL 810 art. 4.5.

the contract area.”²⁷⁰ The prior AAPL Forms were less explicit on this point, but should be interpreted in the same way. The earlier agreements refer to the “parties” voting,²⁷¹ with “parties” broad enough to cover any entity owning an interest governed by the JOA, even if the entity only recently acquired an interest.

Indeed, an Oklahoma appellate court reached this result in a case decided under the 1956 Form. In *Duncan Oil Properties, Inc. v. Vastar Resources, Inc.*, a new Operator had to be chosen because the former Operator had assigned its entire interest to Vastar Resources.²⁷² One of the non-operators argued that Vastar was not entitled to vote. That non-operator relied on Article 18 of the 1956 Form, which provided, “Should a sale be made by Operator of its rights and interests, the other parties shall have the right . . . to select a new Operator.” The non-operator argued that “other parties” only included the entities that already were parties to the JOA prior to the former Operator’s sale of its interest. The appellate court disagreed, suggesting that the word “other” was meant to exclude the former Operator that no longer held an interest, though it might still be bound by certain provisions in the JOA.²⁷³ As for the assignee of the former Operator’s interest, the court explained it “is now a party to the JOA” whose vote should be “counted in the selection of the new operator.”²⁷⁴ The court also noted that Article 20 referred to the “new Operator” being selected by “all” parties.²⁷⁵

The election rules contained in the 1977 through 2015 versions of the AAPL Form 610 have at least four common features: (1) each party that owns an interest at the time of the election is entitled to vote;²⁷⁶ (2) the vote of each party is weighted by its ownership percentage; (3) if an Operator that was removed or is deemed to have resigned fails to vote or votes to succeed itself, the Operator’s vote is disregarded; and (4) a candidate for successor Operator must receive the vote of a majority in interest in order to be elected, or, if the Operator’s voting interest is disregarded for the reason specified above, the candidate must receive a majority in interest after excluding the voting interest of the Operator.²⁷⁷

270. 2015 AAPL 610 art. V.B.6.

271. The 1989 version of Form 610, for example, provides that the “[t]he successor Operator shall be selected by the parties owning a[n] . . . interest.” 1989 AAPL 610 art. V.B.2.

272. 16 P.3d 465 (Okla. 2000).

273. *Id.* at 468.

274. *Id.*

275. *Id.* at 467, 468.

276. This includes new parties to whom an outgoing Operator has transferred its interest.

277. 2015 AAPL 610 art. V.B.6; 1989 AAPL 610 art. V.B.2.; 1982 AAPL 610 art. V.B.2; 1977 AAPL 610 art. V.B.2; 1956 AAPL 610 art. 20.

These similarities aside, the election procedures in the 1977 though 2015 versions of the Form contain some differences.

The 1989 and 1982 versions of the AAPL Form 610 provide that “[t]he successor Operator shall be selected by the affirmative vote of two (2) or more parties owning a majority interest.”²⁷⁸ Thus, the vote of a single party would not be sufficient, no matter how large that party’s voting interest. The 1977 Form requires the votes of two or more parties if the outgoing Operator’s vote is disregarded, but does not appear to require the votes of two or more when the outgoing Operator’s vote is not disregarded.²⁷⁹ The 2015 Form eliminates the requirement that two or more parties vote for a candidate in order for that candidate to be elected successor Operator. The 2015 Form states, “The successor Operator shall be selected by the affirmative vote of one (1) or more parties owning a majority interest.”²⁸⁰

It is possible for the parties to reach a deadlock in the election of a successor Operator. A deadlock can occur in one of at least four types of circumstance. The first circumstance is the situation in which a candidate needs both a majority in interest and the votes of two or more parties. If a party that holds a majority in interest (or a majority in interest of the votes that count if the outgoing Operator’s vote is being excluded) votes for a particular candidate and no other party supports that candidate, then no candidate will be able to obtain both a majority in interest and the support of two or more parties. Notably, the 2015 Form eliminates this potential for deadlock by eliminating the requirement that a candidate receive votes from two or more parties.

Second, because the Forms appear to require the votes of a majority in interest, rather than a majority in interest of the parties that choose to vote, a deadlock could occur if some parties fail to vote or abstain. The Forms provide for disregarding the vote of an outgoing Operator that has been removed or is deemed to have resigned if that party fails to vote, but the Forms do not otherwise provide for disregarding the voting interest of any party that fails to vote.

A third potential deadlock scenario is possible, though it probably would be rare. If three or more candidates receive votes, then it is possible that no candidate would receive a majority even if there are no abstentions or failures to vote. The Forms do not provide for a run-off, so presumably multiple rounds of balloting could result in a continuing deadlock in which more than two candidates receive votes and no candidate receives a majority.

278. 1989 AAPL 610 art. V.B.2.

279. 1977 AAPL 610 art. V.B.2.

280. 2015 AAPL 610 art. V.B.6.

Fourth, even if there are no abstentions and only two candidates for successor Operator, a deadlock could occur in the event that each of two candidates receives 50% of the vote. The 1989, 1982, and 1977 Forms do not provide any procedures for breaking a tie. Presumably, the tie could only be broken if a party changes its vote. In contrast, the 2015 Form provides a tie-breaker. The 2015 Form states that, if the “vote results in a tie, the candidate supported by the former Operator or a majority of its transferee(s) shall become the successor Operator.”

The 2015 Form does not completely eliminate the chance that a tie would result in a deadlock. A tie could still result in deadlock if the outgoing Operator refuses to support either of the candidates (perhaps in a situation in which the outgoing Operator is voting to succeed itself or refusing altogether to vote). Or, if the outgoing Operating transfers a portion of its interest to one or more transferees, while retaining a portion of its interest, and the “transferee(s)” who received a portion of the outgoing Operator’s interest reach a deadlock regarding how to break the tie vote that results when all parties have voted, the deadlock could remain. Nonetheless, the 2015 Form’s tie-breaker mechanism should greatly reduce the risk that a tie-vote will result in deadlock.

If there is a 50% to 50% tie-vote, the operation of the tie-breaker seems reasonably straightforward. But a few questions can arise in other situations. Suppose, however, that there were three candidates for successor Operator. Two candidates each received a 40% vote, and the Operator “supported” the third candidate, who received a 20% vote. Can the Operator break the tie by choosing the candidate who received the 20% vote? Alternatively, suppose that one candidate receives 40% of the vote, another candidate receives 35%, and a 25% interest either abstains or votes for a third candidate. There is no tie, but there is a deadlock. Could the outgoing Operator break the tie? If the Operator has multiple assignees, do they vote by heads or percentage interest? Of course, these scenarios will probably not occur often, but they could be problematic on rare occasions.

The tie-breaker procedure seems to have merit because it lessens the chance of deadlock that could be very costly to the parties. On the other hand, a consequence of the tie-breaker is that whenever a single party owns a majority interest, that party is given more power, thus reducing the leverage of the minority owners.

The provision found in the 2015 Form that requires disregarding the vote of an outgoing Operator voting for itself or refusing to vote also has merit. This is illustrated by *Fasken Land and Minerals, Ltd., v. Occidental Permian Ltd.*, in which Occidental Permian Ltd. (“OPL”) served as unit operator under a unit operating agreement.²⁸¹ OPL owned nearly 75% of

281. 225 S.W.3d 577 (Tex. App. 2005).

the working interests. D.H. Acquisition Ltd. and two other entities that the court called the “Fasken entities” collectively held between 23% and 24% of the working interests. Two other companies held less than 1% each.

The parties held a vote to remove OPL as Operator. Under the terms of the unit operating agreement, the working interest owners could “remove Unit Operator by the affirmative vote of at least eighty-five percent (85%) of the voting interest remaining after excluding the voting interest of Unit Operator.”²⁸² All of the parties other than OPL voted to remove OPL.²⁸³ Thus, the vote was sufficient to remove OPL.

The parties then moved to the selection of a successor. The unit operating agreement provides that “a successor Unit Operator shall be selected by the affirmative vote of three (3) or more Working Interest Owners having at least eighty-five per cent (85%) of the combined voting interest of all Working Interest Owners, provided no Unit Operator who is removed may vote to succeed itself.”²⁸⁴ A representative of Fasken nominated D.H. Acquisition to be the successor operator.²⁸⁵ The parties other than OPL each voted in favor of D.H. Acquisition, but OPL voted its 74.67% interest “against” D.H. Acquisition.²⁸⁶ Thus, the affirmative vote was less than 25%. OPL conceded that it had been removed as Operator, but it argued that D.H. Acquisition had not been selected as a successor Operator because it failed to obtain an “affirmative vote of . . . eighty-five per cent (85%) of the combined voting interest of all Working Interest Owners.” OPL also asserted that it had a right or duty to continue serving as Operator until a successor Operator was selected.

The Fasken entities brought suit in a Texas state court asserting multiple claims, including a claim that OPL breached the unit operating agreement by continuing to operate and by failing to recognize the selection of D.H. Acquisition as successor Operator. They argued that OPL’s vote against D.H. Acquisition was the equivalent of OPL voting for itself—something prohibited under the parties’ agreement.²⁸⁷ Accordingly, OPL’s negative vote should be disregarded. This would leave D.H. Acquisition with an affirmative vote from more than 85% of the voting interests counted.

The appellate court disagreed, concluding that the unit operating agreement was designed “to ensure” that the selection of a successor Operator would be based on an “affirmative vote” from a “super-majority” of the working interest owners. Thus, OPL was entitled to vote against

282. *Fasken*, 225 S.W.3d at 592.

283. *Id.* at 587.

284. *Id.* at 592.

285. *Id.* at 587.

286. *Fasken*, 225 S.W.3d at 587.

287. *Id.* at 592-3.

D.H. Acquisition because such a vote was not the equivalent of OPL voting for itself. Further, the agreement required that the super-majority based on the vote of “at least 85 percent . . . of *all* working interest owners.” Thus, OPL’s vote could not be disregarded.

C. Other Forms

The 2012 AIPN Form provides that, after removal or resignation of an Operator, the operating committee must “meet as soon as possible to appoint a successor Operator.”²⁸⁸ If a party has been removed as Operator for reasons other than a decrease in ownership interest or a change in control of the entity, both of which can be grounds for removal under the AIPN Form,²⁸⁹ both that party and its affiliates are disqualified from consideration to be the successor Operator.²⁹⁰ The percentage vote needed for election as successor Operator is to be set by the parties in Article 5.9.²⁹¹ No party can be appointed as Operator against its will, and reflecting the fact that many nations require governmental approval before there is a change in Operator, the AIPN Form provides that the resignation or removal of a party as Operator and its replacement by a successor Operator, is not effective until any required governmental approval is obtained.²⁹²

The AMPLA Form provides that when an Operator resigns or is removed, the parties “must promptly appoint a new Operator.”²⁹³ The form provides that the parties may not reappoint an Operator that has been removed “for default or following an Insolvency Event.”²⁹⁴ The AMPLA Form also contains a provision that could help in the event that the parties reach an impasse in attempting to select a successor operator. In particular, the form provides that, “[i]f a new Operator cannot be appointed and act immediately, the [party] holding the largest Participating Interest must act as interim Operator until the new Operator is appointed and commences its duties.”²⁹⁵

The selection of a new Operator under the CAPL Form is governed by Clause 2.06. As a general rule, the election of a party as the new Operator requires the vote of at least two parties that are not affiliates and which collectively own more than 50% of the working interests governed by the

288. 2012 AIPN art. 4.11.A.

289. 2012 AIPN arts. 4.10.C and 4.10.D.

290. 2012 AIPN art. 4.11.B.

291. 2012 AIPN art. 4.11.A. *See also* AIPN art. 5.9.

292. 2012 AIPN art. 4.11.A.; 2012 AIPN art. 4.11(E).

293. AMPLA cl. 6.4(a).

294. AMPLA cl. 6.4(b).

295. AMPLA cl. 6.4(c).

agreement.²⁹⁶ However, a party that owns a 60% or larger interest can simply elect itself.²⁹⁷ A party cannot be elected as Operator unless it has given its written consent.²⁹⁸ A party is disqualified from being the new Operator if that party was replaced as Operator within the past 30 months or in the event that any of the circumstances exist that would justify removal of that party as Operator under the CAPL Form.²⁹⁹ If the parties are not able to timely select a new Operator before the outgoing Operator's duty to serve ends, the party (other than the party that is being replaced as Operator) that has the largest interest generally will serve as Operator in the interim.³⁰⁰

Clause 5.5 of the UKCS provides for a successor Operator to be chosen by the operating committee, subject to approval by governmental authorities and the consent of the party that is selected.³⁰¹ If no party is willing to serve as Operator, the agreement treats that as a decision to abandon the joint operations and relinquish the right to operate that was received by the granting instrument.³⁰²

VIII. TRANSFER OF OPERATORSHIP TO AFFILIATE OF OPERATOR

The 1989, 1982, and 1977 versions of AAPL Form 610 provide that a change of corporate name or structure, or the "transfer of Operator's interest to any single subsidiary, parent or successor corporation shall not be the basis for removal of Operator."³⁰³ This provision would seem to allow the Operator to transfer not only its ownership interest, but the Operatorship to another party, provided that such party is a "subsidiary, parent or successor corporation." It also would seem necessary that the Operator transfer its entire interest to that party. The AAPL 710 Form contains a very similar optional provision, but the 2015 version of AAPL Form 610 eliminates this provision.³⁰⁴ Under the 2015 version, there does not appear to be any right to transfer the Operatorship to an affiliate.

With minor exceptions, the CAPL Form allows the Operator to transfer the operatorship to an affiliate to which the Operator is also assigning its ownership interest.³⁰⁵ The 2012 AIPN Form generally allows

296. CAPL cl. 2.06(C).

297. *Id.*

298. CAPL cl. 2.06(D).

299. CAPL cl. 2.06(B).

300. CAPL cl. 2.06(D). If two parties tie for the largest interest, the one that has held its interest for the longest time becomes temporary Operator. *Id.*

301. UKCS cl. 5.5.

302. UKCS cl. 5.6.

303. This is contained in art. V.B.1 of each of those three Forms.

304. AAPL 710 art. 4.4(e).

305. CAPL cl. 2.09.

an Operator to assign the operatorship to an affiliate, as long as the Operator is assigning its entire interest to the affiliate.³⁰⁶ Such a transfer would seem to require operating committee approval under the AMPLA Form.³⁰⁷

The 1956 version of AAPL Form 610 provided that if the Operator sold its “rights and interest,” the Non-Operators would have the right, within sixty days of the sale, to select a new Operator “by a majority vote in interest,” but that absent such a selection the transferee would serve as Operator.³⁰⁸ The 1956 version did not distinguish between transfer to an affiliate and assignment to an unrelated party. Thus, the Non-Operator’s right to designate a new Operator appears to apply after the Operator transfers its interest to an affiliate. Likewise, Rocky Mountain Form 3 appears to give the parties the right to select a successor Operator after any transaction in which the Operator “sell[s]” its entire interest, including when the transfer is to an affiliate.³⁰⁹

IX. ASSIGNMENT OF OPERATORSHIP TO NON-AFFILIATE

Sometimes the question arises whether an Operator may assign its right to operate to a Non-Affiliate.

A. AAPL Form 610

The position of Operator is created by contract and comes with certain contractual rights and duties. As a matter of general contract law, a party to a contract can freely assign its contractual rights—the consent of the other party or parties to the contract is not needed.³¹⁰ There are exceptions to the free assignability of contracts if the parties have agreed that the rights cannot be assigned or the contract is one that is deemed purely personal.³¹¹

306. 2012 AIPN art. 4.12.

307. AMPLA cl. 7.7(a).

308. 1956 AAPL 610 art. 18 (this is included in the same article as the preferential rights provision).

309. Rocky Mountain 3 art. 4.3.

310. RESTATEMENT (SECOND) OF CONTRACT § 317; *Beattie v. State ex rel. Grand River Dam Auth.*, 41 P.3d 377, 381 (Okla. 2002); *Crim Truck & Tractor Co. v. Navistar Intern. Transp. Corp.*, 823 S.W.2d 591, 595 (Tex. 1992); *Somont Oil, Inc. v. Nutter*, 743 P.2d 1016, 1020 (Mont. 1987); LA. CIV. CODE art. 2642.

311. RESTATEMENT (SECOND) OF CONTRACT § 317; *Beattie v. State ex rel. Grand River Dam Auth.*, 41 P.3d 377, 381 (Okla. 2002); *Crim Truck & Tractor Co. v. Navistar Intern. Transp. Corp.*, 823 S.W.2d 591, 595 (Tex. 1992); *Somont Oil, Inc. v. Nutter*, 743 P.2d 1016, 1020 (Mont. 1987); LA. CIV. CODE arts. 2642, 2653.

The 2015 Form expressly provides that the “Operatorship is [not] assignable.”³¹² Under basic principles of contract law, this prohibition should be enforceable. Accordingly, if an Operator purports to assign its Operating rights, the purported assignment should not have the effect of actually transferring operating rights. Instead, depending on circumstances, the purported assignment should be deemed as either a resignation by the Operator or as having no effect whatsoever.

The express prohibition on assignment of the Operatorship is a change. The 1989 Form (like the 1982 and 1977 Forms) did not expressly address whether the Operatorship could be assigned. On the other hand, certain provisions in those Forms could be read as implicitly making the Operatorship non-assignable.

In particular, each of the Forms provides that, if the Operator resigns, all of the parties participate in a vote to select the successor Operator. One could argue that, if an Operator purports to assign its Operating rights, the purported assignment is an attempt by the Operator to resign and select its own successor in violation of the Forms’ provisions that all parties participate in the selection of a successor Operator. Further, in at least one situation—that in which the Operator assigns its entire working interest and also purports to assign the operatorship—the argument that a purported assignment of the Operatorship violates the terms of the older AAPL 610 Forms is even stronger. This is because the 1989 and 1982 Forms each provide that, if the Operator “no longer owns an interest hereunder in the Contract Area,” the Operator will be deemed to have resigned.³¹³

The argument that the Operator may not transfer the operatorship to a Non-Affiliate arguably is strengthened by the provision in the 1989 version of AAPL 610 that “[a] change of a corporate name or structure of Operator or transfer of Operator’s interest to any single subsidiary, parent or successor corporation shall not be the basis for removal of Operator.”³¹⁴

Of course, the Operator who makes a purported assignment and the company that receives the assignment could make counterarguments. If the Operator purported to assign the Operatorship but retained an interest governed by the JOA (so that the “deemed resignation” provision does not apply), the Operator and its assignee could argue that an assignment is not

312. 2015 AAPL 610 art. V.A.

313. *See* 1989 AAPL 610 art. V.B.1; 1982 AAPL 610 art. V.B.1. Article V.B.1 of the 1977 Form contains similar language, but it does not contain the word “hereunder.” The 1977 Form provides for a deemed resignation if the Operator “no longer owns an interest in the Contract Area.”

314. 1989 AAPL 610 art. V.B.1. This argument would be stronger if the quoted provision stated that a transfer to an affiliate would not result in automatic termination, rather than saying it would not be a basis for removal.

a resignation. Accordingly, there was no resignation and therefore no basis for applying the procedure for selecting a successor Operator upon the resignation of an Operator.

Further, even if the Operator assigned its entire interest along with the Operatorship, the Operator and its assignee could argue that there was no resignation. Suppose, for example, that a hypothetical Operator, “XYZ Corp.,” simultaneously assigned its working interest and Operatorship to NewCo Corp. In such a case, XYZ and NewCo could argue that the Operator never had zero interest because neither XYZ nor NewCo held the position of Operator at a time when it had zero interest. XYZ held a working interest up until the time that it assigned the Operatorship and NewCo received a working interest at the same time that it received an assignment of the Operatorship.

There is very little case law on the assignability of the Operatorship under the AAPL Forms. Some cases have held that, if an Operator assigned the Operatorship and the other parties did not timely object, those parties either waived the election requirement or were estopped from complaining about the lack of an election.³¹⁵ Of course the application of waiver or estoppel theories under appropriate facts is not very remarkable. But in at least one case, a court held that the Operatorship is assignable. In *Santa Fe Energy Operating Partners, L.P. v. Universal Resources Corp.*, two parties that each owned a fifty percent interest in certain oil and gas properties entered a joint operating agreement, with Santa Fe Energy being the Operator.³¹⁶ The parties appear to have used the 1982 Form.³¹⁷ Several years later, Santa Fe assigned its working interest and its rights under the operating agreement to Bridge Oil Company. The Non-Operator (Universal Resources) filed suit in a Texas state court, arguing that Santa Fe could not assign its rights as Operator.

The trial court agreed and entered judgment for Universal. The appellate court reversed, but not based on the sort of potential argument outlined above. A contractual right can be non-assignable for one of two main reasons—the contract is purely personal or the parties have agreed that it will be non-assignable. The appellate court addressed both possibilities. The court concluded that the Operatorship was not purely

315. *Abraxas Petroleum Corp. v. Hornburg*, 20 S.W.3d 741, 747 (Tex. App. El Paso 2000).

316. 1996 WL 457251 (Tex. App. 1996).

317. The court did not state what form was being used, but the court quoted “Article V(B)(1)” from the parties’ contract. The 1989, 1982, and 1977 Forms each have slightly different wording in art. V.B.1, and the language quoted by the court appears to match the 1982 Form.

personal, cited three cases that it said supported this conclusion, and then, without further analysis, declared that it agreed.³¹⁸

Although the court's opinion was short on analysis, the court's conclusion that the Operatorship is not purely personal is probably correct. A contract is purely personal when "the duties imposed upon one party [are] of such a personal nature that their performance by someone else would in effect deprive the other party of that for which he bargained."³¹⁹ A classic example of a purely personal contract is one in which a party has contracted for a performance by a particular "artist or author whose skills and talents are unique."³²⁰

The appellate court likewise concluded that the operating agreement itself did not bar assignment of the Operatorship. Universal argued that Article V.B.1 made the Operatorship non-assignable, but the court summarily dismissed the argument without seriously analyzing it. The court supported this result by breezily asserting that a provision in Article XVI of the JOA that the agreement was binding on successors and assigns would be rendered meaningless if Article V.B.1 was interpreted as making the Operatorship non-assignable.

But the appellate court's assertion is plainly wrong. Even if the Operatorship was non-assignable, the agreement's Article XVI still would have meaning because the working interests governed by the operating agreement apparently were assignable. The working interests are generally assignable and Universal does not appear to have argued that Santa Fe could not assign its working interest—only that Santa Fe could not assign the Operatorship. Thus, although plausible arguments exist in favor of the result reached by the court, the court's reasoning was clearly flawed. Nonetheless, the result stands as authority that the Operatorship is assignable under the 1982 AAPL Form. And given that the relevant provisions of the 1989 and 1977 Form are similar to those in the 1982 Form, *Santa Fe* could also be cited as authority to support an argument that the Operatorship is assignable under those Forms too.

In contrast to the conclusion reached by *Santa Fe*, some prominent oil and gas lawyers have concluded that the 1982 and 1989 AAPL Forms make the Operatorship non-assignable, at least in the cases in which an Operator transfers its entire working interest to someone else.

For example, in 2008, Professors Ernest Smith and John Lowe wrote that Article V.A of the 1989 Form "clearly contemplates that the choice of a new Operator is at the option of the JOA participants, rather than the

318. *Santa Fe*, 1996 WL 457251 (Tex. App. 1996).

319. *Farmland Irrigation Co. v. Dopplmaier*, 308 P.2d 732, 740 (Cal. 1957).

320. *Earth Prod. Co. v. Oklahoma City*, 441 P.2d 399, 404 (Okla. 1968) (rejecting contention that contract relating to removal of sand was purely personal).

outgoing operator” who no longer owns an interest, and that “an assignment of operating rights is contrary to the contractual procedure for selecting a successor operator.”³²¹ They also seem to suggest that an assignment of operating rights, although not “expressly preclude[d]” by the language of the 1989 Form, is inconsistent with the expectations implied by the language of the Form.

A prominent practitioner, in discussing the standards for deemed resignation of the Operator in the 1989 Form, states:

The second standard, “no longer owns an interest in the Contract Area,” is used frequently. It is this standard which prohibits a party who is the Operator from passing operatorship to a purchaser or assignee. The operatorship is personal to the party and cannot be assigned. When the Operator assigns its interest it “no longer owns an interest in the Contract Area” and it thus has no right to retain or assign operatorship. A successor Operator must be selected pursuant to Article V.B.2.³²²

Another prominent practitioner addressed the *Santa Fe* decision directly. He suggested that the authorities cited by *Santa Fe* support the proposition that the rights and duties of an Operator are not purely personal, and therefore the Operator’s “rights to operate are generally assignable” absent a contrary provision in the joint operating agreement.³²³ He concluded, however, the holding of *Santa Fe* was wrong because the AAPL Forms’ change in Operator provisions supersede both the general assignability of contract rights and Article XVI’s assignment clause “in the context of a sale of all of the Operator’s interest.”³²⁴

An additional provision in the 1989, 1982, and 1977 Forms that suggests that the Operatorship is generally not assignable is the provision that provides that the Operator’s transfer of its interest to “any single subsidiary, parent or successor corporation shall not be the basis for removal of Operator.”³²⁵ If the Operatorship generally was assignable, this provision would not be necessary.

321. See *supra* note 207.

322. Andrew B. Derman, THE NEW AND IMPROVED 1989 JOINT OPERATING AGREEMENT: A WORKING MANUAL 31-2 (this is No. 15 in the American Bar Association’s “Natural Resources, Energy, and Environmental Law Section Monograph Series”).

323. Timothy W. Dowd, *A.A.P.L. Form 610 Model Form Operating Agreement: Selected Provisions Impacting Onshore Producing Property Interests*, ROCKY MTN. MIN. L. INST. 47 (2001).

324. *Id.*

325. This is contained in art. V.B.1 of each of those three Forms.

Finally, as noted in the section above on transfer of the Operator's interest to an affiliate, the 1956 Form allowed the assignment of the Operatorship when the Operator sold its interest, but subject to the other parties' right to choose a new Operator within sixty days of the sale.³²⁶

B. AAPL Offshore Forms

Neither AAPL Model Form 710 nor Form 810 expressly prohibit assignment of the operatorship, but each provides that the parties to the operating agreement must choose a new Operator in the event that the Operator resigns (or is removed).³²⁷ A purported assignment of the position of Operator would effectively be a resignation, combined with a simultaneous transfer of the operatorship to a Successor Operator chosen by the outgoing Operator. Thus, a purported assignment would be inconsistent with the offshore forms' stipulation that, after a resignation by the Operator, the successor Operator is chosen by the parties. One could argue that an assignment of the operatorship does not involve a resignation by the outgoing Operator, and that an assignment of the Operatorship is permissible, but any such argument seems inconsistent with the expectations within the industry.

C. International Forms

The 2012 AIPN Form prohibits the Operator from assigning its rights and duties as Operator to a Non-Affiliate.³²⁸ The CAPL Form generally does likewise.³²⁹ The UKCS Form does not expressly address assignment of the operatorship, but much like the AAPL offshore forms, it seems to anticipate that the parties as a whole, not the outgoing Operator alone, choose any successor Operator.³³⁰

The AMPLA Form states that "[t]he Operator may delegate to a Third Party, including an Affiliate, any of its rights, remedies, powers, discretions and obligations, provided that . . . the Operator may only delegate the whole of its rights, remedies, powers, discretions and obligations with the approval of the Operating Committee."³³¹ This would prohibit a general assignment of the operatorship, absent consent of the

326. 1956 AAPL Form 610 art. 18.

327. AAPL Form 710 art. 4.5; AAPL 810 art. 4.5.

328. 2012 AIPN Form 4.12.

329. CAPL cls. 2.02(A)(g) & 2.09.

330. UKCS cl. 5.5.

331. AMPLA cl. 7.7.

Operating Committee.³³² The AMPLA Model Form requires an Operator who has delegated rights or obligations to inform the Operating Committee at its next meeting of the delegation and the “identity of the delegate.”³³³ The Form states that a delegation does not relieve the Operator of any of its obligations.³³⁴

CONCLUSION

Often, multiple companies either co-own the oil and gas exploration and production rights in a particular area or they separately own such rights in nearby areas that the companies have decided to explore and develop in a coordinated fashion. In these circumstances, the companies sometimes enter joint operating agreements to govern the exploration and development process and to define their respective rights and duties with respect to one another. Such agreements are common throughout the world, and they constitute one of the most important types of contracts that relate to oil and gas exploration and production.

Several model forms exist and are commonly used as the basis for joint operating agreements, though some parties draft their own agreements. Although parties often “customize” their operating agreements by altering some terms in the model forms, the use of model forms saves transactional costs because parties become familiar with their terms. Moreover, the forms are drafted to handle various issues in ways that are generally accepted as commercially reasonable within the oil and gas industry, neither unduly favoring the party that serves as Operator or the parties who are Non-Operators. These factors combine to save drafting and negotiating time, and improve the likelihood that negotiations will result in agreement.

Probably the most common forms used for onshore operations in the United States are various versions of the AAPL Model Form 610 (the form has been updated several times over the years). The most recent version is the “2015 Form.” Other AAPL Forms are designed for use offshore. Outside the United States, the 2012 AIPN Form is commonly used. Also, other model forms are common in specific jurisdictions.

Under virtually all joint operating agreements, a single party that is called the “Operator” is given both the right and duty to conduct all operations. Important issues relating to the Operatorship include: the

332. If interpreted literally, this provision arguably would allow an Operator to assign the Operatorship to a Non-Affiliate, provided that the Operator retained some portion of its original obligations. For example, if the Operator retained the right and obligation to operate one well, the Operator might be able to assign all of its remaining rights and obligations.

333. *Id.*

334. *Id.*

Operator's duties, the standard of care to which an Operator is held, and the nature of the relationship between the Operator and Non-Operators. Virtually all model forms attempt to have the Operator serve on a "no gain, no loss" basis. The "no gain, no loss" principle provides that the Operator should neither make a profit nor incur a loss because of its service as Operator. Instead, the party that serves as Operator will make a profit or incur a loss based solely on its status as one of the owners of the oil and gas rights being developed.

Although there are some substantive differences between the provisions in different model form joint operating agreements, the similarities in terms are striking. One of the reasons for similarities between model forms is that the drafters of one model form considered the language of prior forms during the process of drafting a new form. Further, whether a joint operation is taking place in the southern United States, the Rockies, or in some other country, many of the same commercial considerations and balancing of interests between Operators and Non-Operators will apply. Further, the similarities are probably driven by the fact that the oil and gas industry is, in part, an international industry, rather than a multitude of separate oil and gas industries in each jurisdiction or productive basin, and thus some of the industry's customs, norms, and expectations remain constant from one jurisdiction to another.

Model forms typically try to ensure that the Operator, in the conduct of its duties as Operator, will be characterized as an independent contractor, rather than as an agent of the parties. Further, the model forms attempt to avoid the existence of a partnership or similar relationship between the parties. Rather than a partnership or similar relationship, the parties attempt to remain mere co-owners (or, in common law terms, "tenants in common") who use the joint operating agreement to govern the exploration and development of their co-owned asset. In this way, the parties seek to have their relative rights and duties to one another governed by the joint operating agreement and the standards established by it, rather than standards imported from the laws governing partnership, principal-agency relationships, or fiduciary relationships.