

STATE OF MICHIGAN
DEPARTMENT OF ENVIRONMENTAL QUALITY

ORDER OF THE SUPERVISOR OF WELLS

IN THE MATTER OF:

THE PETITION OF JORDAN DEVELOPMENT)
COMPANY, LLC, FOR AN ORDER FROM THE)
SUPERVISOR OF WELLS FORMING A 160-ACRE)
DUNDEE FORMATION DRILLING UNIT AS AN) ORDER NO. 03-2014
EXCEPTION TO R 324.301 AND COMPULSORY)
POOLING ALL INTERESTS INTO THE DRILLING UNIT)
IN PINCONNING TOWNSHIP, BAY COUNTY,)
MICHIGAN.)

SECOND AMENDED OPINION AND ORDER

This case involves the Petition of Jordan Development Company, LLC (Petitioner), for approval to drill and complete the Weber 1-29 HD1 well for oil and gas exploration within a drilling unit in the stratigraphic interval known as the Dundee Formation. The Petitioner is requesting a 160-acre drilling unit for the Weber 1-29 HD1 well as an exception to the 40-acre drilling unit size established by general rule spacing, R 324.301. The proposed unit consists of the E 1/2 of SE 1/4 of Section 29 and the W 1/2 of SW 1/4 of Section 28, T17N, R4E, Pinconning Township, Bay County, Michigan. The Petitioner has not obtained a commitment to the Proposed Unit from the lessee of oil and gas leases not owned by the Petitioner. Therefore, the Petitioner seeks an Order of the Supervisor of Wells (Supervisor) designating the Petitioner as operator of the 160-acre drilling unit and requiring compulsory pooling of all uncommitted leases within that geographic area for which the owners have not agreed to voluntary pooling.

Jurisdiction

The development of oil and gas in this state is regulated under Part 615, Supervisor of Wells, of the Natural Resources and Environmental Protection Act, 1994 PA 451, as amended, MCL 324.61501 *et seq.* The purpose of Part 615 is to

ensure the orderly development and production of the oil and gas resources of this state. MCL 324.61502. To that end, the Supervisor may establish drilling units and compulsorily pool mineral interests and lessees' interests within said units.

MCL 324.61513(2) and (4). However, the formation of drilling units by compulsory pooling of interests can only be effectuated after an evidentiary hearing. 1996 MR 9, R 324.302 and R 324.304. The evidentiary hearing is governed by the applicable provisions of the Administrative Procedures Act, 1969 PA 306, as amended, MCL 24.201 *et seq.* See 1996 MR 9, R 324.1203. The evidentiary hearing in this matter was scheduled on March 21, 2014.

FINDINGS OF FACT

The Petitioner specifically requests that the Supervisor issue an Order that:

1. Grants an exception to the drilling unit size established by general rule spacing under R 324.301, by establishing a 160-acre drilling unit for the proposed Weber 1-29 HD1 well consisting of the E 1/2 of SE 1/4 of Section 29 and the W 1/2 of SW 1/4 of Section 28, T17N, R4E, Pinconning Township, Bay County, Michigan.
2. Requires compulsory pooling of all tracts, mineral interests, and lessees' interests within the proposed drilling unit that have not agreed to voluntary pooling with the Petitioner.
3. Names the Petitioner as operator of the Weber 1-29 HD1 well.
4. Authorizes the Petitioner to recover certain costs and other additional compensation from the parties subject to the compulsory pooling order.

The Administrative Law Judge determined that the Notice of Hearing was properly served and published. An Answer to the Petition, dated March 12, 2014, was filed by Arbor Energy, LLC (Respondent). No other Answers to the Petition were received; therefore, the Petitioner Jordan Development Company, LLC and Respondent Arbor Energy, LLC are the only parties to this Cause.

The Petitioner filed a Reply, Motion to Strike, and Motion in Limine in Response to the Allegations Contained in the Answer of Arbor Energy, LLC on March 18, 2014.

The Supervisor designated the hearing to be an evidentiary hearing pursuant to R 324.1205(1)(b); however, oral testimony was not given. On March 21, 2014, the parties stipulated to entry of a standard compulsory pooling order in lieu of presenting testimony and agreed to submit a joint proposed order to the Supervisor before May 21, 2014, the deadline agreed upon for Respondent to decide to participate in the unit. The parties stipulated that, in the event the parties could not agree on language in a joint proposed order, each party would submit its own proposed order for the Supervisor to "choose".

The Petitioner filed its proposed Order on April 30, 2014, and subsequently filed a Motion for Issuance of Compulsory Pooling Order on May 9, 2014, citing Respondent's failure to follow through on a proposed order pursuant to the terms of the parties' stipulation on the record. The Respondent filed a consolidated Answer to the Motion in this Cause and Cause 04-2014 on June 5, 2014, citing the following: discrepancies in the interpretation of the stipulated agreement, allegations that the Petitioner did not follow through with its offer to allow review of data, and allegations that the Petitioner did not provide proper notice to interested parties. The Petitioner filed a Reply to Answer of Arbor Energy, LLC, in both Causes 03-2014 and 04-2014 on June 11, 2014, disputing the allegations of the Respondent and on July 14, 2014, the Respondent filed a consolidated Denial of Jordan Development Company, LLC's Petition for Compulsory Pooling disputing the Petitioner's proposed order and the Petitioner's Reply to Answer.

I have reviewed the transcript and all filings in this matter and find that the Petitioner has substantially fulfilled the agreements it stipulated to on March 21, 2014. The Respondent's attorneys were present on March 21, 2014, and made no objections when the Administrative Law Judge determined that the Notice of Hearing was properly served and published. I find that the Petitioner has adequately demonstrated substantial compliance with the notice requirements of Part 615.

I. Drilling Unit

The parties stipulate that the proposed 160-acre drilling unit is approved for the Weber 1-29 HD1 well.

II. Drilling Unit Operator

The parties stipulate that the Petitioner is to be designated as Operator of the Weber 1-29 HD1 well.

III. Compulsory Pooling

The Petitioner has obtained oil and gas leases covering 125 acres in the proposed 160-acre unit. Leases for the remaining 35 net acres that are not committed or pooled into the proposed 160-acre unit are owned by the Respondent, Arbor Energy, L.L.C.

The following financial institution owns an interest in a leased tract and has failed or refused to execute a subordination agreement, subordinating their interest to the operative lease:

Financial Institution

Independent Bank,
230 West Main Street, Ionia, MI 48846

Mortgagor

David A. Fryzel, et ux

The parties in this matter stipulated that compulsory pooling is necessary to form a full 160-acre drilling unit. The parties stipulated the risk of the Weber 1-29 well being a dry hole supports additional compensation from the pooled owners of 200 percent of the actual drilling costs incurred, 150 percent of actual completion costs and 100 percent of actual equipping costs incurred.

The parties stipulated to entry of a standard pooling order, the provisions of such being governed by R 324.1206. R 324.1206(5) establishes that the unleased mineral owner shall be subject to a one-eighth royalty interest. The Respondent now argues that this does not apply to it as the interest the Petitioner is asking be pooled is, in fact, leased to the Respondent.

If we look to other areas of Part 615, it references the pooling of separately owned tracts and interests (R324.1206(4)) and pooling of properties or parts of properties (MCL 324.61513(4)). I find the Respondent has not agreed to voluntary pooling and therefore is subject to compulsory pooling and a one-eighth royalty interest.

CONCLUSIONS OF LAW

Based on the Findings of Fact, I conclude, as a matter of law:

1. The Petitioner was unable to voluntarily pool all mineral interests and lessees' interests within the proposed drilling unit. The Supervisor may compulsorily pool properties when pooling cannot be agreed upon. Compulsory pooling is necessary to prevent waste and protect the correlative rights of the Pooled Owners in the proposed drilling unit. MCL 324.61513(4).
2. This order is necessary to provide for conditions under which each mineral owner who has not voluntarily agreed to pool all of their interest in the pooled unit may share in the working interest share of production. 1996 MR 9, R 324.1206(4).
3. The Petitioner is an owner within the drilling unit and, therefore, is eligible to drill and operate Weber 1-29 HD1 well. 1996 MR 9, R 324.1206(4).
4. The Petitioner is authorized to take from each nonparticipating interest's share of production the cost of drilling, completing, equipping, and operating the well, plus an additional percentage of the costs as identified in the Determination and Order section of this Order for the risks associated with drilling a dry hole, and the mechanical and engineering risks associated with the completion and equipping of the well. 1996 MR 9, R 324.1206(4).
5. The parties to a proceeding may, by stipulation in writing or entered on the record, agree upon facts, law, or procedure involved in the matter. Stipulations of fact shall be considered as evidence in the proceeding. 1996 MR 9, R 324.1205(4).
6. Spacing for wells drilled in Bay County to the Dundee Formation is 40 acres as set by R 324.301. Exceptions to R 324.301 may be granted by the Supervisor after a hearing.
7. The Supervisor has jurisdiction over the subject matter and the persons interested therein.

8. Due notice of the time, place, and purpose of the hearing was given as required by law and all interested persons were afforded an opportunity to be heard. 1996 MR 9, R 324.1204.

DETERMINATION AND ORDER

Based upon the stipulations of the parties, the Supervisor determines that compulsory pooling to form a 160-acre Dundee Formation drilling unit is necessary to protect correlative rights and prevent waste by the drilling of unnecessary wells.

NOW, THEREFORE, IT IS ORDERED:

1. A 160-acre Dundee Formation drilling unit is established, as an exception to R 324.301, for the Weber 1-29 HD1 well comprising the following area:
E 1/2 of SE 1/4 of Section 29 and the W 1/2 of SW 1/4 of Section 28, T17N, R4E, Pinconning Township, Bay County, Michigan.
2. All properties, parts of properties, and interests in this area are pooled into the drilling unit. This pooling is for the purpose of forming a drilling unit only.
3. Each Pooled Owner shall share in production and costs in the proportion that its net mineral acreage in the drilling unit bears to the total acreage in the drilling unit.
4. The Petitioner is named the Operator of the Weber 1-29 HD1 well. The Operator shall commence the drilling of the Weber 1-29 HD1 well within ninety (90) days of the effective date of this Order, or the compulsory pooling authorized in this Order shall be null and void as to all parties and interests. The Supervisor may grant a reasonable extension of time to commence drilling upon receipt of a request from the Petitioner, with substantiation, for an extension. This pooling Order applies to the drilling of the Weber 1-29 HD1 well only.
5. A Pooled Owner shall be treated as a working interest owner to the extent of 100 percent of its interest owned in the drilling unit. The Pooled Owner is considered to hold a 1/8 royalty interest, which shall be free of any charge

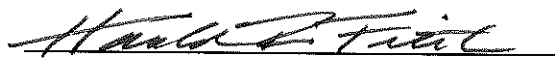
for costs of drilling, completing, or equipping the well, or for compensation for the risks of the well or operating the proposed well including post-production costs.

6. A Pooled Owner shall select one of the following alternatives and advise the Supervisor and the Petitioner, in writing, accordingly:
 - a. To participate, then within ten (10) days of making the election, pay to the Operator the Pooled Owner's share of the estimated costs for drilling, completing, and equipping the well, or give bond to the Operator for the payment of the Pooled Owner's share of such cost promptly upon completion; and authorize the Operator to take from the Pooled Owner's remaining $\frac{7}{8}$ share of production, the Pooled Owner's share of the actual costs of operating the well; or
 - b. To be carried, then if the well is put on production, authorize the Operator to take from the Pooled Owner's remaining $\frac{7}{8}$ share of production:
 - (i) The Pooled Owner's share of the actual cost of drilling, completing, and equipping the well.
 - (ii) An additional 200 percent of the actual drilling costs, 150 percent of the actual completion costs, and 100 percent of the actual equipping costs attributable to the Pooled Owner's share of production, as compensation to the Operator for the risk of a dry hole.
 - (iii) The Pooled Owner's share of the actual cost of operating the well.
7. By stipulation, the Respondent had until 5:00 p.m. on May 21, 2014, to select one of the alternatives in paragraph 6, above, and advise the Supervisor and the Petitioner, in writing. As the Respondent had not notified the Supervisor, in writing, of its decision by May 21, 2014, the Respondent is deemed to have elected the alternative described in Paragraph 6(b).
8. The amounts of \$757,500.00 for estimated drilling costs (dry hole costs); \$1,309,500.00 for estimated completion costs; and \$723,000.00 for estimated equipping costs are fixed as well costs. Actual costs shall be used in determining a Pooled Owner's final share of well costs and in

determining additional compensation for the risk of a dry hole. Within sixty (60) days after commencing drilling of the well, and every thirty (30) days thereafter until all costs of drilling, completing, and equipping the well are accounted for, the Operator shall provide to a Pooled Owner a detailed statement of actual costs incurred as of the date of the statement and all costs and production proceeds allocated to that Pooled Owner.

9. The Operator shall certify to the Supervisor that the following information was supplied to each Pooled Owner no later than the effective date of the Order:
 - a. The Order.
 - b. The Authorization for Expenditure (AFE).
10. A Pooled Owner shall remain a Pooled Owner only until such time as a lease or operating agreement is entered into with the Operator. At that time, terms of the lease or operating agreement shall prevail over terms of this Order.
11. The Supervisor retains jurisdiction in this matter.
12. The effective date of this Order is Sept. 4, 2014.

DATED: August 28, 2014


HAROLD R. FITCH
ASSISTANT SUPERVISOR OF WELLS
Office of Oil, Gas, and Minerals
P.O. Box 30256
Lansing, Michigan 48909-7756