

27.23-18 - Oil and Gas Lease Maintenance Procedures (Issued: 07/11/2005)

Supersedes

- DNR Department Procedure 2318.18 - Oil and Gas Lease Maintenance Procedures, Issued 09/14/2001.

NOTE: The content of this document has not been revised since Issued 09/14/2001.

The only change involves the conversion and numbering to the current DNR Policies & Procedures Manual Structure.

Approval Signature

K. L. Cool, Director, Department of Natural Resources

Supersedes

- DNR Department Procedure 2306.6 – OIL AND GAS LEASING POLICY AND LEASE AMENDMENTS (dated May 11, 1979)
- Rescinded Natural Resources Commission Policy 2306 (dated April 13, 1995)
- DNR Director's Letter 53 (dated August 19.1982)

Policy:

It shall be the policy of the Natural Resources Commission (NRC) to manage State-owned minerals in a manner that protects and enhances the public trust. Surface and mineral ownership may be consolidated when it is in the best interests of the State. Minerals shall be developed in an orderly manner to optimize revenue consistent with other public interest and natural resource values.

Purpose:

The State of Michigan owns over 3.8 million acres of combined surface and mineral rights, and an additional 2.1 million acres of mineral rights only. Also, the State owns 25 million acres of Great Lakes bottomlands. Under the provisions of P.A. 451 of 1994, Part 5, Section 502, the NRC and Director of the Department of Natural Resources (DNR) are responsible for managing these lands and mineral resources to ensure protection and enhancement of the public trust.

The Department shall develop procedures for the administration of State Oil and Gas Leases that provide for occasions when renegotiation of certain terms of a lease are desired by either the Department or the lessee. Such negotiations are at the option of the Department, and may include:

- A. Assignments of lease or lease interests that may occur during the life of the lease. As a general policy, all assignments of working interests of leases must be

submitted to the Department for approval. No assignment will be valid without the written consent of the Department, and approval is at the option of the Department.

- B. Extension of the primary term of a lease. The term of any lease shall not be extended except where it is determined that such extension is in the best interest of the State, and is consistent with the terms of the lease. No extension shall be granted (1) for a period of more than one year, not to exceed two one-year extensions; and (2) which provides for less than the standard royalty and rental rates in State leases offered at public auction at the time the extension is approved. Any extension granted shall be consistent with the extension provision of the lease, and shall require payment by the lessee of an extension fee.

Whenever the lessee requests the Department, as lessor, to consent to pooling of lands to form a drilling unit beyond that already provided for in the lease, or to consent to unitization, the lessee shall submit or present to the Department sufficient data for the State to determine if the proposed voluntary pooling or unitization is in the State's best interest.

The Department shall establish a continuing program for the monitoring of State oil and gas leases to determine if drainage of hydrocarbons may be occurring. Where drainage is suspected on State-owned minerals under lease, the Department shall establish a remedy to protect the State's interest.

The Department shall continue to study and update methods of monitoring production on State leases to ensure that the State is receiving just compensation consistent with the terms of State leases.

Staff will continue to evaluate and review the oil and gas leasing program. Market studies and sales analyses will be conducted by the Department in order that trends and patterns can be established as guidelines for policy and management decisions by the Commission and staff. These assessments will be for the purpose of continued improvement in the leasing method and the overall leasing program for State-owned minerals to (1) ensure that the State lease is competitive, (2) acquire and maintain expertise in the management of hydrocarbon development, and (3) provide that changing conditions are reflected in the overall oil and gas leasing program.

The Department shall prepare an annual report each year, a report of the complete State leasing program activities for the preceding year which shall include, but not be limited to, (1) the number of leases and drilling permits granted, (2) the number of producing wells completed, (3) relevant data obtained by the Department on oil and gas activities in Michigan, (4) a summary of the revenues generated and their ultimate disposition, (5) a summary and forecast of activities for the current fiscal year, and (6) a summary and assessment of any identified problems and any recommendations for changes in the leasing program. The complete report will be made available to all interested parties.

Related Procedures:

- Oil and Gas Leasing Procedure No. [27.23-14](#).
- Oil and Gas Lease Classification Procedure, No. [27.23-15](#).
- Oil and Gas Lease Compliance Procedure, No. [2306.E8](#).

ASSIGNMENT PROCEDURES

WHO

DOES WHAT

APPLICANT

1. Prepares Assignment of interests in State oil and gas leases on State Assignment Forms:
 - A. For Assignments involving one State lease, the applicant completes PR-4301.
 - B. For Assignments involving multiple State leases, the applicant completes PR-4302.
 - C. Checks appropriate box on Assignment form identifying Assignment as either a Full or a Partial Assignment. Full assignments involve the transfer of Lessee status to another legal entity. Partial assignments do not involve the transfer of Lessee responsibility.
2. Submits the completed application to DNR Cashier's office along with the required application fee:
 - A. \$25.00 per lease per assignment for full Assignments.
 - B. \$10.00 per lease per assignment for partial Assignments.

DNR CASHIER'S OFFICE

3. Date stamps cover letter.
4. Forwards cover letter, copy of check, and copy of remittance report to appropriate MLMS Staff.

DNR FMFM-MLMS STAFF

6. Notes date of Assignment. All assignments must be processed within 30 days of receipt. Assignment must be approved, returned unapproved, or the applicant must be notified in writing of an extension of the 30-day time period or the Assignment is automatically approved.
7. Reviews Assignment to ensure that it has been submitted on the required State Form No. PR4301 or PR4302 (Assignment of Oil and Gas Leases). Those not submitted on either of the required forms are returned unapproved.
8. Confirms that the Assignment form has been fully executed by both the Assignor and the Assignee, and includes the signatures of the required notaries. If Assignment is not fully executed, it is returned unapproved.
9. Confirms that the required Assignment Review Fee has been paid. Assignments submitted without the required fees are returned unapproved. Assignment fees are as follows:
 - A. \$10.00 per lease per Assignment for partial Assignments.
 - B. \$25.00 per lease per Assignment for full Assignments.
10. Reviews submitted Assignment form and Department Hold Action List to determine if Assignee is on the Department Hold Action List. If Assignee is on

the Department Hold Action List, Assignment is returned unapproved with letter of explanation. (No rights can be conveyed to any person or other legal entity on the Hold Action List.)

11. Reviews Assignment form to see if standard form is altered in any way or purports to assign rights in easements, personal property or private leases. If Assignment contains any of the above, it is returned unapproved with letter of explanation.
12. Reviews Assignment and confirms that one of the boxes on first page identifies it as being a full or partial Assignment. If neither of the boxes is checked, the Assignment is returned unapproved.
13. Based on the box checked as outlined in "1.C." above, identifies Assignment as either partial or full. Depending on whether the assignment is partial or full, Staff proceeds with the following steps.
14. Processes assignments:

A. Partial Assignments:

1. Reviews number of Assignment forms submitted. Only one copy of the Assignment form needs to be submitted for partial Assignments. This one copy can be a photocopy or an original. If Assignee submits two copies and requests that an approved copy is returned to them, Staff should do so.
2. Stamps the Assignment in the Department execution signature area of Assignment form with Assignment Stamp A. Using a red ink pen, Staff prints in the date that the Assignment is approved (date processed by Staff).
3. Stamps bottom of Assignment form with Assignment Stamps B and C.
4. Gives approved Assignments to MLMS Secretary to complete process.

DNR MLMS SECRETARY

5. Enters all information into the Assignment log, including accounting information pertaining to Assignment fees paid.
6. Makes appropriate number of photocopies of Assignment for all lease files associated with the Assignment.
7. Files Assignment copies in lease files.

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B. Full Assignments:

1. Reviews number of Assignment forms submitted. Two original, fully executed Assignment forms must be submitted for each Assignment submitted for approval. If only one original is submitted, Assignment is returned unapproved.

2. Ensures Assignee has a Performance Bond on file, and determines if the Bond is adequate to add the additional acreage associated with the Assignments. If not, Assignment is returned unapproved with a cover letter and Assignment fees are refunded. Cover letter must include information on how to obtain proper and adequate bonding, and information on resubmitting Assignment and fees after bonding has been obtained. Bonding schedule is as follows:

<u>AMOUNT OF BOND</u>	<u>MAXIMUM ACRES</u>
\$10,000.00	0-5000
\$25,000.00	5001-10,000
\$50,000.00	10,001-UNLIMITED

3. Confirms by lease number that the Assignor is the current Lessee of each of the Leases listed on the Assignment form. If Assignor is not the Lessee of the leases listed on the Assignment, changes the identification of the Assignment from a full Assignment to a partial Assignment.
 - a. Checks the partial Assignment box on the Assignment and makes a manual notation (in ink) that the Assignment is a partial Assignment.
 - b. Initials and dates these changes on the Assignment.
 - c. Processes the Assignment as a partial Assignment, as outlined above.
 - d. Returns one copy to individual who submitted Assignment, along with a cover letter explaining that Assignment was approved as a partial Assignment.
4. Verifies rent paid to date and expiration date of each lease. If rent is delinquent or lease is expired, full assignment request is returned unapproved.
5. If Assignor is the Lessee of some of the leases listed in the Assignment but is not the Lessee of all leases listed on the Assignment, the Assignment is returned unapproved. In a transmittal letter, Assignee is instructed to resubmit the Assignment as two Assignments: one full, listing all of the leases in which they are the Lessee; and one partial, listing all of the leases where they are not the Lessee.
6. If Assignor is the Lessee of all leases listed on the Assignment, Staff proceeds to the next step.
7. Pulls all lease files associated with the assignment, and files out-cards in place of the files.

8. Compares on a lease-by-lease basis, the legal descriptions in which rights are being conveyed through the Assignment.
 - a. In instances where a legal description listed on the Assignment is different than that listed in the lease, Assignment is mailed back to Assignor unapproved.
 - b. In instances where each of the legal descriptions listed in the Assignment, per lease, represent 100% of the descriptions held by each lease, proceed to Step 9.
 - c. In instances where the legal description of one or more of the leases listed on the Assignment is the same as the description on the corresponding lease but describes only a portion of the leased premises, the following steps must be taken. For each lease where the Assignee is assigning all of their rights to only a portion of the leased property, that lease will be split into two leases. The Section Manager must pre-approve the split of any leases. If the Section Manager does not approve the split of a lease, Assignment is mailed back to Assignor unapproved, along with a cover letter of explanation.
 - i. Original lease retains the original lease number, and Assignor remains the Lessee of the remaining acreage held by the original lease.
 - ii. The acreage conveyed by the Assignment becomes a new lease, and the Assignee becomes the Lessee of the new lease. The lease number of this newly created lease will be the original lease number, plus the Suffix A. If the original lease has already been split and there is already a new lease with the Suffix A associated with the lease number, use the next letter in the alphabet, etc.
 - iii. Makes note(s) for secretary to separate the original lease(s) into two leases. For each new lease created, a separate note attached to the original lease file is necessary so that the Secretary splits the lease correctly. Note should identify acreage (by legal description) of lands to be included in the new lease.
9. Initials area next to signature block where Section Manager will approve the Assignment by signature. The initials tell the Section Manager that staff has reviewed

all aspects of the Assignment, and that Manager should approve the Assignment.

10. Forwards Assignment, associated lease files, and written instructions to Secretary for processing.
11. Enters pertinent information on the Assignment Log.

DNR MLMS SECRETARY

12. Prepares Assignment for Department execution, and obtains required signatures.

DNR MLMS MANAGER

13. Executes DNR approval of the Assignment by signing Assignment agreement.

DNR MLMS SECRETARY

14. Drafts transmittal letter.
15. Updates LOTS and Lease files to identify the Assignee as the new Lessee. If this is a new suffix, Secretary creates new lease file and makes entry for LOTS, showing a new lease has been created by the Assignment.
16. Mails executed copy of Assignment with cover letter to Assignee (or applicant).
17. Files DNR copy of Assignment in lease file, with copy in each lease file involved.
18. Files lease files under new Lessee(s) name(s).
19. Removes out-card(s) from file drawer of previous Lessee(s) associated with the Assignment.
20. Updates Lease numeric book as needed to show name changes for Lessee.

OIL AND GAS LEASE EXTENSION PROCEDURES

WHO

DOES WHAT

LESSEE / REQUESTOR

1. Submits request to extend the expiration date of an existing lease and includes the required extension review fee of \$250.00 per lease per extension request no later than 30 days prior to the expiration date of the primary term.

DNR CASHIER'S OFFICE

2. Date stamps and copies cover letter and application fee check.
3. Forwards cover letter, copy of check, and copy of remittance report to MLMS secretary.

MLMS SECRETARY

5. Enters data from request into the Lease Extension Log.
6. Retrieves applicable lease file(s) from cabinet(s), inserts out card(s), and forwards all to MLMS Staff.
7. Forwards cover letter, copy of check, and copy of remittance report to appropriate MLMS staff.

MLMS STAFF

8. Reviews terms of the original lease document to determine if an extension can be considered.
 - A. If lease allows for an extension:
 1. Review the bonus paid when original lease was issued.
 2. Reviews State and Federal lease auction sale data from the past five years and notes bonus bids received on parcels located within three miles of extension parcels requested.
 3. Review current private lease bonus data for area, if available.
 4. Review production data from adjacent and nearby producing wells and unitized areas.
 5. Determines and negotiates appropriate bonus to be charged to lessee / requestor for extension requested.
 6. Prepares an Oil & Gas Lease Extension Work Sheet for each lease being extended.
 - B. If lease does not allow for any additional extensions:
 1. Drafts letter denying request to extend, noting exact lease language disallowing the request.

2. Notifies lessee that parcel can be nominated for the next sale or may qualify for direct leasing.
 3. Retains the review fee, as it is non-refundable and cannot be applied towards subsequent nomination or direct lease application fee, even for the same parcel.
9. Returns all documents to secretary for processing.

MLMS SECRETARY

10. Prepares Oil and Gas Lease Rental and Bonus Remittance form per Extension Work Sheet(s).
11. Finalizes cover letter or denial letter, as instructed by MLMS staff.
12. Prepares Oil & Gas Lease Extension Agreement(s) as instructed by MLMS staff.
13. Forwards cover letter, Extension Agreement(s), and Oil and Gas Lease Rental and Bonus Remittance form to MLMS staff for final review.

MLMS STAFF

14. Reviews cover letter, Extension Agreement(s), and Oil and Gas Lease Rental and Bonus Remittance form.
15. Returns all documents to secretary for processing.

MLMS SECRETARY

16. Makes corrections / changes to cover letter, Extension Agreement(s), and/or Oil and Gas Lease Rental and Bonus Remittance form as directed, and submits to MLMS Staff for cover letter signature.
17. Mails out executed cover letter, Extension Agreement(s), and Oil and Gas Lease Rental and Bonus Remittance form, if applicable, to Lessee / requestor.
18. Places a copy of the yet to be executed Extension Agreement in each file and places a copy of the cover letter and Oil and Gas Lease Rental and Bonus Remittance form in the first lease listed in request for multiple extension requests.
19. Enters negotiated bonus and rental amounts requested into Lease Extension Log.
20. Forwards lease files back to MLMS Staff, to be held in a "pending applicant" status.

LESSEE / REQUESTOR

21. Completes the following areas of the Lease Extension Agreement:
 - A. Enters Liber and Page recording information of original lease (middle of page 1).

NOTE: If Liber and Page information is left blank, it is assumed that Lessee / requestor did not record the original Lease.
 - B. Lessee signature date (top of page 2).
 - C. Signs and notarizes "Acknowledgment by Lessee" section (page 2).
22. Returns the Oil and Gas Lease Rental and Bonus Remittance form along with a check payable to the "State of Michigan" for the total rental and bonus due to the Cashier's Office.

23. Returns original executed Extension Agreement(s) and a copy of the entire remittance sent to the Cashier's Office directly to MLMS Staff.

DNR CASHIER'S OFFICE

24. Processes the remittance utilizing the Index, PCA, and Agency Object Codes listed on the Oil and Gas Lease Rental and Bonus Remittance form, validates bottom right-hand area of form, forwards the original to OFS-FRA for posting revenue to LOTS, and forwards a copy to MLMS Staff.

MLMS STAFF

25. Verifies that the proper bonus and rental was paid, and enters validation numbers and date received on Oil & Gas lease Extension Work Sheet.
26. Reviews Extension Agreement(s) for any changes made and ensures signature page has been properly signed and notarized.
27. Initials Extension Agreement in the area above MLMS Manager signature block.
28. Returns file to MLMS secretary.

MLMS SECRETARY

29. Prepares signature blocks for MLMS Manager's signature and notarization, then forwards to MLMS Manager.

MLMS MANAGER

30. Executes Extension Agreement(s) and forwards them back to MLMS Secretary.

MLMS SECRETARY

31. Notarizes signature of MLMS Manager.
32. Copies fully executed Extension Agreement(s) and attaches to front of existing lease in lease file.
33. Enters LOTS maintenance to reflect approved extension details.
34. Prepares cover letter, and mails original executed Extension Agreement(s) to lessee / requestor.
35. Refiles lease(s) under company name in numerical order.

POOLING AND UNIT AGREEMENT REVIEW PROCEDURE

WHO

DOES WHAT

XXXX

1. TO BE DEVELOPED

DRAINAGE REVIEWS PROCEDURE

WHO

DOES WHAT

XXXX

1. TO BE DEVELOPED