

## Chapter 12

# The New Horizontal Modified Operating Agreement and Additional Drafting Considerations

**James S. Robertson**  
**David J. Yellow Robe**  
**Robin S. Fredrickson**  
**Jeffrey S. Munoz**  
*Latham & Watkins LLP*  
Houston, Texas

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### § 12.01. Introduction and History of the American Association of Professional Landmen Form Operating Agreements.\*

The American Association of Professional Landmen (AAPL) issued its first AAPL Form 610 Model Form Operating Agreement in 1956 in an attempt to streamline the process of negotiating and drafting an effective joint operating agreement by means of a standardized form.<sup>1</sup> It was an immediate success and quickly became the standard for the American oil and gas industry (“Industry”).

As the Industry has evolved, so has the AAPL Model Form Operating Agreement. The AAPL released its first revision to the Model Form Operating Agreement in 1977 and the Model Form Operating Agreement was revised again in 1982 (“1982 JOA”).<sup>2</sup>

Oil prices slumped over the next several years and the Industry suffered hard times. In 1989, the AAPL released another revision to the Model Form Operating Agreement (“1989 JOA”) with a number of revisions addressing issues of solvency and adequate funding by reforming payments, default mechanisms, and security liens.<sup>3</sup>

Since the 1989 JOA was introduced, previously inaccessible oil and gas deposits have been opened to successful exploration and development through the combination of horizontal drilling and hydraulic fracturing. The rise of horizontal drilling has been swift and dramatic. In 1987, only about 50 horizontal wells existed.<sup>4</sup> Horizontal drilling has come to dominate the modern drilling landscape. Current estimates place the proportion

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\* The authors would like to thank Cassy E. Romano for her invaluable assistance in the drafting and editing of this chapter. Also, capitalized terms used herein and not otherwise defined in this chapter have the meanings given to them in the 1989 Joint Operating Agreement (JOA) and the Horizontal JOA, as applicable.

<sup>1</sup> David M. Patton, “Issues Raised by a Distressed Economy with Respect to Joint Operating Agreements and Other Common Oil and Gas Exploration and Development Agreements,” *Financial Distress in the Oil & Gas Industry*, ch. 4 (Feb. 2010) (providing that the AAPL’s name changed from the American Association of Petroleum Landmen to the American Association of Professional Landmen).

<sup>2</sup> Model Form Operating Agreement, AAPL Form 610 – 1982.

<sup>3</sup> Model Form Operating Agreement, AAPL Form 610 – 1989.

<sup>4</sup> Kathy Shirley, “Horizontal Wells Now Common,” *Explorer* (Sept. 2000), [http://archives.aapg.org/explorer/2000/09sep/horiz\\_drill.cfm](http://archives.aapg.org/explorer/2000/09sep/horiz_drill.cfm).

of total land-based drilling rigs in the United States engaged in horizontal drilling at 70 percent.<sup>5</sup> However, because none of the AAPL Model Forms addresses the concept of horizontal drilling, parties have had to incorporate provisions into their chosen Model Forms on an ad hoc basis to effectively address the relevant issues.

The AAPL recognized that the Industry would benefit from a standard form joint operating agreement with horizontal drilling and development modifications. As it had in the past, the AAPL formed a committee to review Industry needs and draft provisions responsive to those needs.<sup>6</sup>

Based upon the recommendations of this committee, the AAPL recently released a 1989 JOA that was modified for horizontal drilling and development (“Horizontal JOA”).<sup>7</sup> A number of the revisions modify or add definitions to address issues relevant to horizontal drilling. New provisions have also been added to address certain operational matters that are specific to horizontal wells. The AAPL’s modifications, however, are generally limited to horizontal drilling, and further modification is needed to address topics that are generally addressed by the Industry in joint operating agreements.

## **§ 12.02. Revisions to Definitions.**

To address the needs of horizontal drilling, several definitions of the 1989 JOA were modified and added to the Horizontal JOA. Each revision and addition is addressed below in alphabetical order, with any new language denoted by underlined text.

### **[1] — Authority for Expenditure.**

Operators distribute an Authority for Expenditure (AFE) in advance of operations to apprise the Non-Operators of the estimated cost thereof, as well as to provide sufficient information to allow the parties to determine

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<sup>5</sup> Baker Hughes, *North America Rotary Rig Count*, Baker Hughes (June 13, 2014), [phx.corporate-ir.net/phoenix.zhtml?c=79687 & p=rol-reports&other](http://phx.corporate-ir.net/phoenix.zhtml?c=79687&p=rol-reports&other).

<sup>6</sup> See Jeff Weems and Amy Tellegen, *The New Horizontal Agreement and the Prospect of an Entirely New Form*, Porter Hedges LLP, <http://www.porterhedges.com/portalresource/lookup/wosid/cp-base-430302/media.name=/2013-0923%20New%20Horizontal%20Agreement%20and%20Prospect%20of%20New%20Form.pdf> (last visited June 16, 2014).

<sup>7</sup> Model Form Operating Agreement – Horizontal Modifications, AAPL Form 610 – 1989.