July 3, 1996

The Honorable John T. Shively
Commissioner
Department of Natural Resources
400 Willoughby Avenue
Juneau, AK 99801-1724

David Johnston, Chair
Alaska Oil & Gas Conservation Commission
3001 Porcupine Drive
Anchorage, AK 99501-3120

Re: AOGCC/DNR Unitization Jurisdiction
A.G. file no: 663-96-0121
1996 Op. Att'y Gen. No. 3

Dear Commissioner Shively and Mr. Johnston:

You have asked for an opinion regarding the respective jurisdictions of the Alaska Oil and Gas Conservation Commission ("AOGCC") and the Department of Natural Resources ("DNR") over the unitization of production interests in state oil and gas leases. Specifically, you have asked whether the AOGCC has the power to unilaterally change the terms of the Prudhoe Bay Unit Agreement ("PBUA") by forcing the parties to combine their interests in the two Initial Participating Areas established under that Agreement, where those terms were entered into and approved by DNR under AS 38.05.180(p).

SUMMARY

A review of the facts, pertinent case law, and the statutes establishing the respective jurisdictions, authorities, and powers of the AOGCC and the DNR shows that the AOGCC cannot

use its compulsory unitization powers to force holders of interests in state oil and gas leases to alter the terms of a voluntary unitization agreement that has been entered into and approved by DNR under AS 38.05.180(p). In this context the AOGCC fulfills whatever statutory obligations it has, not by reworking the parties' contractual allocation of the costs and benefits of Prudhoe Bay production, but by issuing orders that implement specific oil field practices necessary to prevent waste, protect correlative rights, or ensure the greater ultimate recovery of oil and gas.

INTRODUCTION AND BACKGROUND

A. Unitization Generally

There is general agreement among courts that persons holding interests in land overlying a common supply of oil and gas have "correlative rights" with others similarly situated as well as a duty to the public not to waste the oil and gas:

> The term "correlative rights" is merely a convenient method of indicating that each owner of land in a common source of supply of oil and gas has legal privileges as against other owners of land therein to take oil and gas therefrom by lawful operations conducted on his own land limited, however, by duties to other owners not to injure the source of supply and by duties not to take an undue proportion of the oil and gas. In addition, of course, to this aggregate of legal relations, each landowner has duties to the public not to waste the oil and gas.

1 W.L. Summers, *The Law of Oil and Gas* § 63 at 180-81 (footnote omitted).

The standards of performance under those correlative rights and the public duty not to waste oil and gas have not been developed by courts. Instead, they are generally reflected in state conservation statutes that give administrative agencies the power to regulate the production of oil and gas to prevent waste:

> While litigation, apart from statute, has not often arisen in which the courts have had the opportunity to determine a standard of performance of the duty

> not to injure a source of supply of oil and gas, conservation statutes, defining and prohibiting waste and giving administrative agencies authority to make and enforce rules for its prevention, do determine such a standard of performance. An injury to the source of supply which violates the rights of the public also violates the rights of adjacent owners.

Id. at 184-186.

To prevent waste and to protect the public interest in maximizing the production of oil and gas, many conservation statutes include provisions like those in Alaska that provide for the development and production of an oil and gas deposit through "unitization" of the ownership interests in the common source of supply.[1] Unitization "refers to the combination of most, if not all, of the separate tracts in the field into one tract" so that the reservoir or field can be developed as "a single entity, without regard to surface boundary lines." 6 H.R. Williams and C.J. Meyers, *Oil and Gas Law* § 901 at 3-4 (1995) (footnote omitted). Unitization is necessary for certain oil field practices to be effective, and generally results in greater overall recovery:

> Both economics and property rights require the integration of a field in order for such operations as gas cycling, pressure maintenance, and secondary recovery to be conducted. Moreover, . . .greater recovery at less cost can be achieved when the field is treated as an entity and wells [are] so located that they maximize the use of reservoir energy. . . .

Williams and Meyers, § 901 at 3-4 (1995).

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[1] Conservation statutes generally provide two methods for combining ownership interests to prevent waste: unitization, and pooling. "Although the terms 'pooling' and 'unitization' are frequently used interchangeably, more properly 'pooling' means the bringing together of small tracts sufficient for the granting of a well permit under applicable spacing rules whereas 'unitization,' or, as it is sometimes described, 'unit operation,' means the joint operation of all or some part of a producing reservoir." 6 H.R. Williams and C.J. Meyers, *Oil and Gas Law* § 901 at 2-3 (1995). We are concerned here with unitization, which is provided for in Alaska under AS 31.05.110 and AS 38.05.180(p)-(q). We are not concerned with pooling, which is addressed in AS 31.05.100 and AS 38.05.180(s).

Although unitization thus provides comprehensive overall benefits to both the public and those with interests in the field, it frequently is difficult to accomplish voluntarily:

> It has long been argued that efficiency in the development and operation of oil and gas reservoirs and the prevention of waste of recoverable hydrocarbons require that such reservoirs be developed and operated as a unit without regard to surface boundaries. To achieve the maximum objectives of such a unitization program it is necessary that all persons having an interest in the program area become subject to the agreement. Without statutory compulsion, however, unanimity is frequently impossible to obtain. *The principal obstacle to full, voluntary agreement is the problem of dividing the proceeds of production.*

Id. § 910 at 85 (emphasis added; footnotes omitted). More particularly, "there is frequent acrimony as to the respective shares of production to be given owners of interests in favorable parts of the structure and owners of interests in less favorable areas, for example, persons with interests overlying the gas-cap of a gas-drive pool."[2] Because voluntary unitization is so difficult to accomplish, at least 33 states (including Alaska) and three Canadian provinces have enacted statutes providing for compulsory unitization under certain circumstances. *Id.*, § 912 at 96-98.

B. Unitization in Alaska

1. Pre-statehood

Alaska's statutes relating to conservation of oil and gas are now codified in AS 31.05. Many of them, however, were first enacted during territorial days in ch. 40, SLA 1955. The waste of oil and gas was prohibited in sec. 1, now AS 31.05.095. Section 2 defined waste in terms virtually

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[2] Williams and Meyers, § 910 at 86. As discussed in more detail *infra*, the problem of placing a value on the leasehold interests overlying the gas cap of the Prudhoe Bay reservoir was particularly acute given the lack of an available transportation system and market for Prudhoe Bay gas, and the uncertainty regarding when (or whether) a viable transportation system and market for that gas would be developed.

identical to those now appearing in AS 31.05.170(14). Section 3 created an Alaska Oil and Gas Conservation Commission, "to be composed of the Governor, the Territorial Highway Engineer and the Commissioner of the Alaska Department of Mines," who were to serve without compensation. The Commission was given many of the powers and duties now found in AS 31.05.030 (discussed below), including the power to prevent waste. Section 7.1 provided for both voluntary unitization and, in the absence of voluntary unitization, compulsory unitization:

> To prevent, or to assist in preventing waste, as prohibited by this Act, to insure a greater ultimate recovery of oil and gas, and to protect the correlative rights of persons owning interests in the tracts of land affected, such persons may validly integrate their interests to provide for the unitized management, development, and operation of such tracts of land as a unit. Where, however, such persons have not agreed to so integrate their interests, the Commission, upon proper petition, after notice and hearing, as hereinafter provided, shall be vested with jurisdiction, power and authority, and it shall be its duty to make and enforce such orders and do such things as may be necessary or proper to carry out and effectuate the purposes of this section.

Id. (This language now appears in AS 31.05.110(a) with only minor textual changes.)

The territorial commission's power to compel unitization was limited by section 7.4, however, in that no compulsory unitization order would be effective unless it was approved by "the lessees of record of not less than 62.5 percent of the unit area affected thereby and by the owners of record of not less than 62.5 percent . . . of the normal one-eighth landowners' royalty interest . . . ."[3] This mirrored the practice in other states: "In general, under these [conservation] statutes a regulatory agency is authorized to require unitization of a pool or some part thereof despite the objection of minority interests therein if a proposed plan has been approved by a requisite majority

[3] Following statehood, this provision was codified as AS 31.05.110(d). It was repealed by ch. 160, sec. 17, SLA 1978.

of the owners of interests in the premises to be unitized." Williams and Meyers, § 912 at 98.1-99 (1995).

2. Statehood to 1978

Following statehood, the First Alaska Legislature transferred the territorial commission's functions and authority to DNR. Ch. 64, sec. 16, SLA 1959. It also enacted the Alaska Lands Act, ch. 169, SLA 1959, now codified at AS 38.05, to provide for the management of the huge land grant given the new state.[4] One subsection of that Act, now codified as amended at AS 38.05.180, authorized the commissioner of natural resources to lease state lands for oil and gas purposes. *See* ch. 169, art. VIII, sec. 3(7), SLA 1959.

In addition to authorizing leasing of the lands, a proprietary function, that subsection also included specific provisions relating to the unitization of state lands leased for oil and gas purposes, a conservation function. For conservation purposes, lessees with interests in a common source of supply of oil or gas were authorized to enter into a cooperative or unit plan of development or operation "whenever determined and certified by the Commissioner to be necessary or advisable in the public interest." The commissioner was given the discretion "with the consent of the holders of leases involved, to establish, alter, change, or revoke drilling, producing, rental, minimum royalty, and royalty requirements" of the leases and, again with the consent of the lessees, to adopt regulations with respect to the leases and an approved cooperative or unit plan determined "necessary

[4] Under section 6 of the Alaska Statehood Act, the new State of Alaska became entitled to select 103,350,000 acres of federal land (subsections (a) and (b)), was granted the school, university, and mental health land grants previously made to the Territory of Alaska (subsection 6(k)), and succeeded to the United States' title to tide and submerged lands underlying navigable waters within its boundaries (subsection 6(m)). Alaska Statehood Act, Pub. L. 85-508, § 6, 72 Stat. 339 (1958).

or proper to secure the proper protection of the public interest." Ch. 169, art. VIII, sec. 3(7), SLA 1959. The commissioner was given the power to include in state leases a provision "requiring the lessee to operate under such a reasonable or cooperative or unit plan" and to "prescribe such a plan under which such a lessee shall operate, which shall adequately protect all parties in interest, including Alaska." *Id*. An approved plan could include, in the commissioner's discretion, a provision vesting the commissioner or another person or a state agency with the authority "to alter or modify from time to time the rate of prospecting and the quantity and rate of production under such plan." *Id*. Finally, these provisions were stated to be "in addition to, and shall in no way repeal, diminish, change or abrogate the provisions of" the 1955 conservation legislation that, under ch. 64, SLA 1959, also was the DNR's responsibility to administer.[5]

3. Post-1978

In 1978, the legislature enacted three measures of significance here. First, ch. 155, SLA 1978, repealed and reenacted the statute authorizing the commissioner of natural resources to lease state lands for oil and gas purposes, AS 38.05.180. The reenacted statute retained the prior provisions relating to unitization, including the provisions authorizing state lessees to unitize with others and authorizing the commissioner to prescribe a "reasonable cooperative or unit plan. . . [which] must adequately protect all parties in interest, including the state." AS 38.05.180(p). It also retained the prior language that the provisions of AS 38.05.180 concerning cooperative or unit plans are in addition to and do not affect AS 31.05.

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[5] Most of the provisions of section 3(7) of chapter 169, art. VIII, SLA 1959, now appear, with only minor changes, in AS 38.05.180(p). The last two provisions referenced in the text are now found in AS 38.05.180(q). Section 3(7) also included authorization for state lands to be pooled with other lands, a provision that is now codified at AS 38.05.180(s).

The second significant 1978 Act was ch. 158, SLA 1978, which transferred the authority and responsibility for administration of the state's oil and gas conservation statutes from DNR to a newly created "independent quasi-judicial agency of the state," the AOGCC. AS 31.05.005(a). DNR was given "the same standing (no more nor less) before the Commission as granted by law to any other proprietary interest." AS 31.05.026(e). The AOGCC's authority was made applicable to "all land in the state lawfully subject to its police powers," expressly including "all land included in a voluntary cooperative or unit plan of development or operation entered into in accordance with AS 38.05.180(p)." AS 31.05.027. And, under sec. 5 of ch. 158, "[a]ll references in AS 31.05 to department or Department of Natural Resources except in AS 31.05.026 shall be read as [the AOGCC] in order to implement this Act." As a result, the AOGCC was given "jurisdiction and authority over all persons and property, public and private, necessary to carry out the purposes and intent of this chapter." AS 31.05.030(a). It was directed to "investigate to determine whether or not waste exists or is imminent, or whether or not other facts exist which justify or require action by it." AS 31.05.030(b). And it was directed to "adopt rules, regulations and orders and take other appropriate action to carry out the purposes of this chapter." AS 31.05.030(c).

The third significant 1978 Act was ch. 160, SLA 1978. So far as relevant here, that Act added "the filing and approval of a plan of development and operation for a field or pool in order to prevent waste, insure a greater ultimate recovery of oil and gas, and protect the correlative rights of persons owning interests in the tracts of land affected" to the list of things the AOGCC was authorized to require. Ch. 160, sec. 1, SLA 1978 (adding AS 31.05.030(d)(9)). It added "the quantity and rate of the production of oil and gas from a well or property" to the list of things the AOGCC was authorized to regulate "for conservation purposes" and provided that "this authority

shall also apply to a well or property in a voluntary cooperative or unit plan of development or operation entered into in accordance with AS 38.05.180(p)." Ch. 160, sec. 2, SLA 1978 (adding AS 31.05.030(e)(6)). The act also repealed AS 31.05.110(d), which had provided that no compulsory unitization order would be effective unless ratified by the lessees of at least 62.5 percent of the unit area and at least 62.5 percent of the owners of the landowners' royalty interest in the unit. Ch. 160, sec. 17, SLA 1978. Of particular significance here, this act also added a new subsection to the unitization section, AS 31.05.110, which provided:

> This section applies to all involuntary units formed in the state. Subsections (a) and (g) - (p) of this section apply to all voluntary units formed in the state and to a voluntary cooperative or unit plan of development or operation entered into in accordance with AS 38.05.180[p].

Ch. 160, sec. 2, SLA 1978, codified at AS 31.05.110(q).[6]

C. The PBUA

On March 29, 1977, Atlantic Richfield Company, BP Alaska, Inc., and Exxon Corporation filed an application with the commissioner of DNR pursuant to AS 38.05.180 and 11 AAC 83.355 "for approval and certification of a voluntary unit agreement for the Prudhoe Bay Unit."[7] The Oil and Gas Conservation Committee in the Division of Oil and Gas Conservation ("DOGC"), which had assumed the powers and duties of the territorial Conservation Commission, concluded that a plan of operations subsequently submitted by the applicants was "consistent with

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[6] Originally this subsection referred to AS 38.05.180(m), which, prior to its 1978 repeal and reenactment, was the provision now codified at AS 38.05.180(p). AS 31.05.110(q) now correctly refers to AS 38.05.180(p).

[7] Decision and Findings of the Director, Division of Minerals and Energy Management ["DMEM"] with Respect to Application for Approval of Unit Agreement, Prudhoe Bay (May 25, 1977) ("DMEM Decision") at 1.

sound conservation practices based on currently available data."[8] The DOGC director approved the application for the PBUA and the accompanying plan of operations and forwarded his decision to the commissioner on May 19, 1977.[9] The commissioner approved the director's decision on June 2, 1977.[10] The commissioner also signed the Unit Agreement, approving it as "a unit plan of development or operation on behalf of the State of Alaska," as authorized by Chapter 38.05 of the Alaska Statutes. PBUA at 1, 36. Under Article 3 of the Unit Agreement, all of the oil and gas rights in the leases executed by the State "are hereby unitized so that Unit Operations may be conducted as if the Unit Area had been included in a single lease executed by the State of Alaska . . . ." PBUA, Art. 3.1 at 7.

The primary oil and gas reservoir subject to the Unit Agreement is referred to as the Prudhoe Bay (*Permo-Triassic*) Reservoir. The Unit Agreement identifies two portions of the reservoir, the Oil Rim and the Gas Cap.[11] The existence of these two distinct portions of the

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[8] May 19, 1977 memorandum from Hoyle H. Hamilton, Director, DOGC, to O.K. Gilbreath, Jr., Director, DMEM.

[9] DMEM Decision at 6.

[10] Approval of Prudhoe Bay Unit Agreement by the Commissioner of the Department of Natural Resources (June 2, 1977) at 2.

[11] The "Prudhoe Bay (Permo-Triassic) Oil Rim" is "that portion of the Prudhoe Bay (Permo-Triassic) Reservoir which originally contained Oil and Solution Gas and which was not originally occupied by Gas Cap Gas." PBUA, art. 5, § 5.1(d), p. 17. The Prudhoe Bay (Permo-Triassic) Gas Cap is "that portion of the Prudhoe Bay (Permo-Triassic) Reservoir which originally contained Gas Cap Gas and which is distinguished from the Prudhoe Bay (Permo-Triassic) Oil Rim as being that portion of the Permo-Triassic Reservoir which originally existed above the gas-oil contact or contacts as determined by the Working Interest Owners." PBUA, art. 5, § 5.1(b), p. 16. Article 1 of the Unit Agreement provides the following other relevant definitions:

1.3 *Gas Cap Gas* is natural gas (with all of its constituent elements,

reservoir means that oil and gas do not exist in the same proportion everywhere in the Prudhoe Bay field, and that each lease of each working interest owner overlies a different amount of oil and gas. Due in substantial measure to difficulties associated with placing a value on the Gas Cap Gas in the absence of an available transportation system and market for that gas, the working interest owners could not agree on a single equity ownership interest in Prudhoe Bay hydrocarbons. The working interest owners therefore divided the Prudhoe Bay Unit into two, largely overlapping, Initial

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> including condensate and gas plant liquids, derived or extracted from it after it leaves the Reservoir) which originally occurred in a Reservoir in gaseous form and not in solution with Oil.
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> 1.4 *Gas Cap* is that portion of a Reservoir occupied by Gas Cap Gas originally in place and not by Oil or Solution Gas.
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> * * *
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> 1.7 *Oil* is any hydrocarbon produced in liquid form at the wellhead and originally existing in liquid form in the Reservoir.
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> * * *
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> 1.9 *Oil Rim* is that portion of a Reservoir occupied by Oil and Solution Gas originally in place and not by Gas Cap Gas.
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> * * *

1.20 *Solution Gas* for the purposes of distinguishing it from Gas Cap Gas, is any gaseous hydrocarbon which originally occurred in a Reservoir in solution with Oil. Solution Gas for purposes of distinguishing it from Oil, is any hydrocarbon which originally occurred in a Reservoir in solution with Oil and which was converted to a gaseous form by changes in pressure or temperature effected by ordinary production methods. In either case, the term Solution Gas includes all constituent elements including gas plant liquids derived or extracted therefrom after it leaves the Reservoir.

PBUA, art. 1, pp. 2-4.

Participating Areas: the Oil Rim Participating Area ("ORPA") and the Gas Cap Participating Area ("GCPA").[12] Each working interest owner is assigned a "tract participation percentage" for each lease (or tract) it holds in each participating area.[13] Production from the Unit is allocated to each participating area "in accordance with methods, formulas and procedures as provided in the Unit Operating Agreement."[14] The stated goal of these "methods, formulas and procedures" is to allocate

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[12] Article 5.2 of the Unit Agreement establishes the two Initial Participating Areas and sets forth, in accordance with Exhibit C to the Agreement, the tract participation percentages for each working interest owner:

> 5.2 *Participation for Prudhoe Bay (Permo-Triassic) Reservoir Participating Areas.* The Oil Rim Participating Area shown on Exhibit D-1 and the Gas Cap Participating Area shown on Exhibit D-2 are hereby established as the initial Participating Areas. The Tract Participations initially agreed to by the Working Interest Owners for the Oil Rim and Gas Cap Participating Areas are shown in Exhibit C. Tract Participations have been assigned to the Tracts within the Oil Rim Participating Area primarily on the basis of Oil and Solution Gas originally in place and to the Gas Cap Participating Area primarily on the basis of Gas Cap Gas originally in place, as determined by agreement of the Working Interest Owners. Because development of the Tracts and the available information concerning Unitized Substances is not complete enough to allow final determination of Tract Participations as of the Effective Date, the Working Interest Owners agree that the initial Tract Participations shall be subject to adjustments or corrections as provided in the Unit Operating Agreement.

PBUA, art. 5, p. 17.

[13] Because the Oil Rim Participating Area and the Gas Cap Participating Area overlap considerably, most of the leases received tract participation percentages in both areas. *Compare* Unit Agreement, Exh. C, Part I at C-1 through C-4, *with* Unit Agreement, Exh. C, Part II at C-5 through C-7.

[14] Unit Agreement, Art. 6.1. The Unit Operating Agreement is a separate agreement among the working interest owners to which the State is not a party. The Operating Agreement deals in detail with, among other things, voting rights (Arts. 5, 35), tract operations (Art. 8), taxes (Art. 12),

Gas Cap Gas to the Gas Cap Participating Area, and to allocate Oil and Solution Gas to the Oil Rim Participating Area.[15] Production that has been allocated to a particular participating area is then further allocated to each working interest owner based upon the sum total of that owner's tract participation percentages in that area.[16] *See* AOGCC Conservation Order No. 360, August 9, 1995

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insurance (Art. 13), production allocation (Arts. 27-29), and Unit expense allocation and adjustments (Arts. 30-34). However, "[i]nsofar as the respective rights and obligations of Working Interest Owners on the one hand and the State of Alaska on the other hand are concerned, this [Unit] agreement shall control in case of any conflict between it and the Unit Operating Agreement." PBUA, art. 18, p.34.

[15] Unit Agreement, Article 6.1. The definitions of Gas Cap Gas, Oil, and Solution Gas are set forth in note 11, above. Article 6.1 provides as follows:

> *Allocation of Unitized Substances Produced from Participating Areas.* All Unitized Substances produced and saved from the Unit Area shall be allocated to the Participating Area established for such Reservoir and to the Working Interest Owners therein; except that where there are separate Oil Rim and Gas Cap Participating Areas within a Reservoir, production therefrom of Gas Cap Gas shall be allocated to the Gas Cap Participating Area of such Reservoir, and to the Working Interest Owners therein, and production therefrom of Oil and Solution Gas shall be allocated to the Oil Rim Participating Area of such Reservoir and to the Working Interest Owners therein. Such allocations shall be in accordance with methods, formulas and procedures as provided in the Unit Operating Agreement.
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> Unitized Substances allocated to each Working Interest Owner in a Participating Area shall be allocated to the several Tracts in such Participating Area in which such Working Interest Owner owns a Working Interest in the proportion that the product of such Working Interest Owner's Working Interest in each such Tract multiplied by the current Tract Participation for such Tract bears to the sum of all such products for that Working Interest Owner. The amount of Unitized Substances allocated to each Tract, regardless of whether the amount is more or less than the actual production of Unitized Substances from the well or wells, if any, on such Tract, shall be deemed for all purposes to have been produced from such Tract.

[16] *Id.*

(revised November 3, 1995) ("C.O. 360") at 13, ¶¶ 102, 103. For example, BPXA receives 50.68 percent of production allocated to the Oil Rim Participating Area but only 13.84 percent of production allocated to the Gas Cap Participating Area. *Id.* ARCO and Exxon Co. USA ("Exxon"), on the other hand, each receive 21.78 percent of production allocated to the Oil Rim Participating Area and 42.56 percent of production allocated to the Gas Cap Participating Area.[17]

D. Recent AOGCC Action: The "MI/NGL" Dispute

A dispute has arisen between the two working interest owners responsible for operating the Prudhoe Bay Unit -- ARCO and BPXA -- regarding the proper levels of natural gas liquids ("NGLs") and miscible injectant ("MI"), respectively, to be derived from the Unit's separator off-gas.[18] NGLs can be blended with oil and shipped through the Trans-Alaska Pipeline System ("TAPS") for sale. MI is used as an integral part of the Unit's enhanced oil recovery (EOR) program. The Central Gas Facility ("CGF"), however, can process only a fixed amount of separator off-gas

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[17] Other owners and their respective interests are:

	ORPA	GCPA
Mobil Oil Co.	1.89%	0.28%
Phillips Petroleum Co.	1.88%	0.26%
Chevron USA Production Co.	0.67%	0.48%
Amerada Hess Corp.	0.54%	0.00%
Texaco Exploration and Prod. Co.	0.55%	0.00%
Louisiana Land and Exploration Co.	0.04%	0.00%
Marathon Oil Co.	0.05%	0.00%
Shell Land and Energy Co.	0.14%	0.00%

C.O. 360 at 13, ¶ 103.

[18] Separator off-gas is "hydrocarbon and nonhydrocarbon natural gas, including NGL Components and all other constituent elements of such natural gas except Separator Liquid, that is produced or otherwise voided from the Reservoir. . . . " Prudhoe Bay Unit Operating Agreement, § 26.002 at p. 114 (April 1, 1977).

each day. As a result, producing more NGLs for sale and shipment through TAPS reduces the amount of MI available for EOR projects. Because all oil derived from enhanced oil recovery is allocated to the Oil Rim Participating Area, and 90 percent of the NGLs are allocated to the Gas Cap Participating Area, C.O. 360 at ¶ 104, BPXA benefits from greater production of MI for enhanced oil recovery, while ARCO (and Exxon) benefit from greater production of NGLs for blending and sale. *See id.*, ¶ 153.

Effective February 1995, Alyeska Pipeline Service Co. ("Alyeska"), the operator of TAPS, removed all limits on the volume of NGLs that could be blended with oil for shipment through TAPS other than one based on vapor pressure control. C.O. 360, ¶ 10. ARCO, as operator of the CGF, increased the production of NGLs to meet the new vapor pressure control limit. *Id.*, ¶ 12. BPXA, as operator of Skid 50 (where NGLs are blended with oil for delivery to TAPS), refused to allow these additional NGLs to be blended with the crude oil stream, effectively precluding the production of additional NGLs. *Id.*, ¶ 13. ARCO attempted to blend additional NGLs at an earlier point in the process but BPXA further reduced Skid 50 blending to offset ARCO's efforts. *Id.*

ARCO brought its dispute with BPXA to the AOGCC, and asked it to rule that the best conservation practice concerning NGLs and MI is to blend and ship the maximum volume of NGLs allowed by TAPS. C.O. 360 at ¶ 14. BPXA, in turn, argued that the best conservation practice would be to produce the greatest possible quantity of MI (700 mmscfpd) at the expense of greater blending of NGLs. *Id.*, ¶¶ 15 and 18. Each contended that only its approach would prevent waste. *Id.*, ¶¶ 94, 96, and 97.

The AOGCC accepted ARCO's position, concluding that "[a]t least in the short term, the quantity and rate of production of oil and gas most likely to prevent waste and ensure greater ultimate recovery is to produce the maximum blendable volume of NGLs from hydrocarbons delivered to the CGF." C.O. 360, Conclusion 16. However, the AOGCC considered it "unlikely" that the parties would be before it on the question whether to maximize blendable NGLs or make more MI if the ownership interests in the Oil Rim Participating Area and the Gas Cap Participating Area were integrated. *Id.*, ¶ 140. For the future, the AOGCC offered its preliminary conclusion that further integration of the Oil Rim Participating Area and the Gas Cap Participating Area would be necessary:

> Sufficient evidence has been heard regarding the effects of property and contractual arrangements on Prudhoe Bay development and operation to convince the [AOGCC] that the next phase of these proceedings should be more focused than the general investigation previously anticipated. It appears that more complete unitization and integration of interests in the Prudhoe Oil Pool will be necessary to prevent waste, ensure a greater ultimate recovery of oil and gas, and protect correlative rights. Consequently, in the absence of voluntary efforts, further hearings in this matter will be directed toward developing a plan of compulsory unitization.

Id., Conclusion 18. The AOGCC ordered a hearing "to develop a plan for compulsory unitization of the Prudhoe Oil Pool," citing AS 31.05 generally and AS 31.05.027, 31.05.030, 31.05.095, and 31.05.110, specifically, as authority.[19]

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[19] C.O. 360, Order 2. For its part, DNR determined that it also had jurisdiction to hold a hearing and issue orders relating to the MI/NGL dispute. Decision Regarding Jurisdiction, *In the Matter of the Appropriate Reservoir Management for Optimization of Natural Gas Liquids Blending, Utilization of Miscible Injectant, and Maximization of the Economic and Physical Recovery within the Prudhoe Bay Unit*, before the Commissioner of Natural Resources and Commissioner of the Department of Revenue (August 20,1995) ("DNR Decision re: Jurisdiction") at 1-2 and 81-82.

THE AOGCC CANNOT COMPEL UNITIZATION OF OIL AND GAS INTERESTS WHERE THOSE INTERESTS ARE ALREADY SUBJECT TO A UNIT PLAN APPROVED BY DNR UNDER AS 38.05.180(p)

A. The AOGCC's Compulsory Unitization Authority Is Limited to Instances Where the Parties Have Not Entered into a Voluntary Unit Approved by DNR under 38.05.180(p)

Because administrative agencies "are creatures of statute, deriving from the legislature the authority for the exercise of any power they claim," *Rutter v. State*, 668 P.2d 1343, 1349 (Alaska 1983) (citation omitted), an agency cannot issue an order which goes beyond its statutory authority. *Far North Sanitation v. APUC*, 825 P.2d 867, 870 (Alaska 1992). *See Leedom v. Kyne*, 358 U.S. 184, 188-89 (1958). The issue here is whether the legislature has authorized the AOGCC to order the further unitization of oil and gas interests that are already subject to a unit plan approved by DNR under AS 38.05.180(p).

1. Alaska Statute 31.05.110(q) limits the AOGCC's compulsory unitization powers to oil and gas interests not already part of a unit plan approved by the DNR

The principal statutory provision establishing that the AOGCC's compulsory unitization authority does *not* extend to cases where oil and gas lessees have already agreed to integrate their interests under a plan approved by DNR is AS 31.05.110(q). That subsection makes *all* of AS 31.05.110 applicable to *in*voluntary units, but only *some* of its provisions applicable to voluntary units and those entered into and approved by DNR under AS 38.05.180(p):

> This section [*i.e.*, AS 31.05.110] applies to all involuntary units formed in the state. Subsections (a) and (g) - (p) of this section apply to all voluntary units formed in the state and to a voluntary cooperative or unit plan of development or operation entered into in accordance with AS 38.05.180(p).

AS 31.05.110(q). Subsections (b) - (f) -- those that expressly do not apply to voluntary units and those entered into under AS 38.05.180(p) -- are the subsections governing the AOGCC's compulsory unitization powers.

Subsection (b), the first subsection identified by the legislature as not applying to DNR-approved unit plans, empowers the AOGCC to issue an order "providing for the unitization and unitized operation of the pool" if, after notice and hearing, the commission "finds that (1) the unitized management. . .of a pool is reasonably necessary to carry on. . .[any] form of joint effort calculated to substantially increase the ultimate recovery of oil and gas from the pool; (2) one or more of the unitized methods of operation. . . is feasible, and will prevent waste. . .; (3) the estimated additional cost, if any, of conducting such operations will not exceed the value of the additional oil and gas so recovered; and (4) the unitization and adoption of one or more of the unitized methods of operation is for the common good. . . ." AS 31.05.110(b). The next subsection identified by the legislature as not applying to DNR-approved unit plans, AS 31.05.110(c), sets forth the specific provisions the order must contain.[20] Of particular relevance here is AS 31.05.110(c)(2), the provision that empowers the AOGCC to establish "the division of interest or formula for the

[20] AS 31.05.110(c), among other things, requires that the order include provisions for "the efficient unitized management" of the unit with actual operations carried on by the unit itself or by one or more of the lessees designated by vote of the lessees (and "not by the [AOGCC]") as unit operator, AS 31.05.110(c)(1); a "division of interest or formula" for fairly and equitably apportioning and allocating production from the unit to the those entitled to share in or benefit from that production, AS 31.05.110(c)(2); the financing and sharing of costs of unit development and operation, AS 31.05.110(c)(3); the procedure and basis on which wells and equipment on the unitized land will be taken over and used for unit operations, AS 31.05.110(c)(4); "an operating committee to have general overall management and control of the unit" and subordinate "subcommittees, boards or officers" as required for efficient management, AS 31.05.110(c)(5); "the time when the plan of unitization becomes effective,"AS 31.05.110(c)(6); and the time and manner "by which the unit shall or may be dissolved and its affairs wound up,"AS 31.05.110(c)(7).

apportionment and allocation of the unit production. . . ." Because the legislature has specifically indicated that this provision does not apply to unit plans approved by DNR, the AOGCC clearly does not have the power to compel the signatories to the PBUA to adhere to an apportionment and allocation formula devised by the commission.[21]

The Alaska Supreme Court recognizes a presumption "that the legislature intended every word, sentence, or provision of a statute to have some purpose, force, and effect, and that no words or provisions are superfluous." *Rydwell v. Anchorage School District*, 864 P.2d 526, 530-31 (Alaska 1993) (citation omitted). The only interpretation of AS 31.05.110(q) that gives full effect to all of its terms is that the provisions establishing the AOGCC's compulsory unitization powers (AS 31.05.110(b)-(f)) do not apply to voluntary units and unit plans approved by DNR under AS 38.05.180(p). Any other reading would render that subsection utterly superfluous. Moreover, by specifically identifying only subsections (a) and (g) through (p) as applying to unit plans approved by the DNR, the legislature has clearly manifested an intent that the subsections not so identified do *not* apply. *See Burrel v. Burrel*, 696 P.2d 157, 165 (Alaska 1984) ("[i]t is an accepted rule of statutory construction that to include specific terms presumptively excludes those which are not enumerated"). *See also* 2A N.J. Singer, *Sutherland Statutes and Statutory Construction* § 47.24 at

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[21] The other subsections that do not apply to unit plans approved by DNR, AS 31.05.110(d) through (f), also relate to the AOGCC's compulsory unitization powers. Subsection (d), AS 31.05.110(d), prior to its repeal by ch. 160, sec. 17, SLA 1978, provided that no compulsory unitization order would be effective unless ratified by the lessees of at least 62.5 percent of the unit area and at least 62.5 percent of the owners of the landowners' royalty interest in the unit. Subsection (e) provides that the AOGCC's hearings and other proceedings will be governed generally by the procedures set forth in AS 31.05.040 (regulations and orders), AS 31.05.050 (notice), and AS 31.05.060 (action by commission). AS 31.05.110(e). Finally, subsection (f) prohibits production from the unit by persons other than those authorized by the unit and in any manner not provided for in the plan of unitization. AS 31.05.110(f).

228 (5th Ed. 1992) (same). The AOGCC therefore may not apply its compulsory unitization powers to oil and gas interests that are already subject to a unit plan, such as the PBUA, that has been approved by DNR under AS 38.05.180(p).[22]

2. Alaska Statute 31.05.110(a) confirms the legislature's intent to limit the AOGCC's compulsory unitization powers to oil and gas interests that have not been voluntarily unitized

AS 31.05.110(a) confirms the legislature's intent to limit the AOGCC's compulsory unitization powers to oil and gas interests that have not been voluntarily unitized. That statute provides as follows:

> To prevent, or to assist in preventing waste, to insure a greater ultimate recovery of oil and gas, and to protect the correlative rights of persons owning interests in the tracts of land affected, *these persons may validly integrate their interests to provide for the unitized management, development, and operation of such tracts of land as a unit. Where, however, they have not agreed to integrate their interests, the [AOGCC]*, upon proper petition, after notice and hearing, has jurisdiction, power and authority, and it is its duty to make and enforce orders and do the things necessary or proper to carry out the purposes of this section.

(Emphasis added.)

The two sentences of AS 31.05.110(a) set out two alternative methods for unitizing oil and gas properties. First, it authorizes the parties to agree to integrate their lands. Where the parties have not done so, however, the AOGCC is expressly given the power to do what is necessary to accomplish that result -- *i.e.*, to compel unitization.

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[22] As noted previously, the PBUA was approved not only by the Commissioner of DNR, but by the AOGCC's predecessor, the Oil and Gas Conservation Committee in the Division of Oil and Gas Conservation. This memorandum, however, does not address whether principles of estoppel or other legal doctrines may be invoked to preclude the AOGCC from altering the terms of the PBUA.

The goal of statutory construction, of course, is "to give effect to the legislature's intent, with due regard for the meaning statutory language conveys to others." *Tesoro Alaska Petroleum Co. v. Kenai Peninsula Borough*, 746 P.2d 896, 905 (Alaska 1987) (citation omitted). The first sentence of AS 31.05.110(a) provides for voluntary unitization with no mention of the AOGCC. The AOGCC is expressly given "jurisdiction, power and authority" only in the second sentence, subject to the condition precedent that the parties "have not agreed to integrate their interests." The meaning this language conveys to others is that the AOGCC's power to compel unitization is limited to instances in which the parties have not integrated their interests. This meaning is consistent also with the purposes generally of compulsory unitization statutes, which are "a legislative response to the need for compulsory process to deal with persons having minority interests in premises overlying a producing formation who refuse to unitize their premises with others despite the public interest in maximum recovery of hydrocarbons." Williams and Meyers, § 912 at 96 (emphasis added). If all persons with interests overlying a producing formation agree to unitize their interests, there is no need for a compulsory process.

If the legislature had intended the AOGCC to have the same jurisdiction, power, and authority where the parties had already agreed to integrate their interests, moreover, the language conditioning the express grant of that power to instances "[w]here. . . they have not agreed to integrate their interests" would have been unnecessary and superfluous. *See Rydwell*, 864 P.2d at 530-31 (courts presume legislature intended every word, sentence, or provision of statute to have purpose, force, and effect). Limiting the AOGCC's power to compel unitization to instances in

which the parties "have not already agreed to integrate their interests" gives purpose, force, and effect to that phrase.[23]

3. The statutory provisions describing the AOGCC's general jurisdiction and powers are not inconsistent with the conclusion that it cannot compel further integration of oil and gas interests that are already subject to a unit agreement approved by DNR

There are a number of statutory provisions that define in broad terms the scope of the AOGCC's jurisdiction and authority. Most significant among them is AS 31.05.030, which provides in part:

> Sec. 31.05.030. Powers and duties of commission.
> (a) The commission has jurisdiction and authority over all persons and property, public and private, necessary to carry out the purposes and intent of this chapter.

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[23] The AOGCC also appears to have interpreted its general powers under AS 31.05.030 and its specific compulsory unitization authority under AS 31.05.110 as reaching only those cases where an agreement has not already been entered into:

> A copy of an agreement validly integrating the interests of all persons owning interests in affected property in the pool or portion of the pool for which development is contemplated by the operator must be filed with the [AOGCC] no later than 30 days before the commencement of regular production from the pool. *In the absence of an agreement*, the [AOGCC] will, in its discretion, after notice and public hearing in accordance with 20 AAC 25.540, issue an order creating a unit, or an area of participation within a unit, which integrates the interests of all persons owning an interest in the pool or a portion of the pool.

20 AAC 25.517(c) (emphasis added). The AOGCC's longstanding interpretation that its compulsory unitization authority applies only "[i]n the absence of an agreement" is of course consistent with the limitations imposed by AS 31.05.110(a) and AS 31.05.110(q), and thus should be given effect. *Cf. Public Defender Agency v. Superior Court, Third Judicial District*, 534 P.2d 947, 952 (Alaska 1975) ("[c]ontinuous, contemporaneous and practical interpretation by executive officers...is a valuable aid in determining meaning").

> (b) The commission shall investigate to determine whether or not waste exists or is imminent, or whether or not other facts exist which justify or require action by it.
>
> (c) The commission shall adopt regulations and orders and take other appropriate action to carry out the purposes of this chapter.
>
> (d) The commission may require . . . (9) the filing and approval of a plan of development and operation for a field or pool in order to prevent waste, insure a greater ultimate recovery of oil and gas, and protect the correlative rights of persons owning interests in the tracts of land affected.
>
> (e) The commission may regulate, for conservation purposes . . . (6) the quantity and rate of the production of oil and gas from a well or a property; this authority shall also apply to a well or property in a voluntary cooperative or unit plan of development or operation entered into in accordance with AS 38.05.180(p).

Other statutory provisions confirm the broad scope of the AOGCC's authority. For example, AS 31.05.027 provides that the AOGCC's authority "applies to all land in the state lawfully subject to its police powers" and, in particular, "applies to all land included in a voluntary cooperative or unit plan of development or operation entered into in accordance with AS 38.05.180(p)." Alaska Statute 31.05.026(e) provides that the DNR "shall have the same standing (no more or less) before the [AOGCC] as granted by law to any other proprietary interest." Alaska Statute 31.05.060(a) provides that the AOGCC "may act upon its own motion." Finally, AS 31.05.095 prohibits the waste of oil and gas.

The question is whether these broad grants of power to the AOGCC override the specific limitations of AS 31.05.110(q) that the AOGCC's compulsory unitization powers do not apply to oil and gas interests that are already subject to a voluntary unit agreement or a unit plan entered into and approved by DNR under AS 38.05.180(p).

a. The statutes establishing the AOGCC's general jurisdiction and powers must be read together with the legislature's grant of authority to DNR and the specific limitations set forth in AS 31.05.110(q)

Statutory construction begins with an analysis of the language of the statute construed in light of its purpose. *Borg-Warner Corp. v. Avco Corp.*, 850 P.2d 628, 633 n. 12 (Alaska 1993) (citation omitted). Ordinarily, an unambiguous statute is enforced as written without judicial construction or modification. *Lake v. Construction Machinery, Inc.*, 787 P.2d 1027, 1030 (Alaska 1990). "[H]owever, this rule is not controlling when a seemingly unambiguous statute must be considered in conjunction with another act. In that case, [the court] will examine the legislative history and adopt a reasonable construction which realizes legislative intent, avoids conflict or inconsistency, and gives effect to every provision of both acts." *Id.* (citation omitted).

The statutes establishing the AOGCC's general jurisdiction and powers must be read in conjunction with AS 38.05 and the provisions that specifically empower the DNR to approve voluntary or cooperative unit plans of development on state land, as well as with the specific limitations set forth in AS 31.05.110(q). The most reasonable interpretation under this approach is that the legislature intended to limit the AOGCC's compulsory unitization powers to circumstances where the leaseholders had not already agreed to unitize their interests under a plan approved by DNR. This construction "gives effect to every provision of each act," *Lake*, 787 P.2d at 1030, by recognizing the legitimate statutory obligations of DNR and the specific limitations of AS 31.05.110(q), while acknowledging the AOGCC's power to carry out its statutory responsibilities on all land -- including state-owned land already included in a unit plan approved by DNR -- through its ability to issue orders that require or forbid specific oil field engineering practices. This

construction "realizes legislative intent," *Lake*, 787 P.2d at 1030, because, among other things, it is consistent with the legislature's view that compulsory unitization is a remedy of last resort. *See infra.* This construction also "avoids conflict or inconsistency" by reconciling DNR's statutory responsibility to approve unit plans on state land with the AOGCC's ability to prevent waste, ensure the greater ultimate recovery of oil and gas, and protect correlative rights through orders relating to specific oil field engineering practices. A legislative grant of jurisdiction to the AOGCC over all land in the state simply is not inconsistent with the legislature's concurrent decision to limit the scope of the particular remedies or powers available to the AOGCC under certain circumstances.

b. The legislature's specific instructions regarding the limitations of the AOGCC's compulsory unitization powers control over the more general expressions of the scope of the AOGCC's authority

Even if the statutes governing the AOGCC's general powers and jurisdiction were somehow interpreted as being inconsistent with the specific limitations of AS 31.05.110(q), the limitations set forth in this latter provision must be given effect. It is an accepted rule of statutory construction that "if a specific section conflicts with a general section, the specific section controls." *Burton v. State Farm Fire and Casualty Co.*, 796 P.2d 1361, 1363 (Alaska 1990) (citation omitted). Because the legislature articulated a specific intent under AS 31.05.110(q) to exempt unit plans approved by DNR from the statutory provisions relating to the AOGCC's compulsory unitization powers, the Alaska courts will give effect to that intent, regardless of the existence of other, more general statutory provisions that could be interpreted differently.

4. Legislative history supports the conclusion that the AOGCC's compulsory unitization powers do not extend to oil and gas interests that have already been included in a unit plan approved by the DNR

Construing AS 31.05.110 as evincing a legislative intent that the AOGCC's compulsory unitization authority is limited to instances where the parties have not agreed to integrate their interests also is consistent with the statement of legislative policy that accompanied the 1978 repeal of AS 31.05.110(d).[24] A Free Conference Committee letter of intent adopted unanimously by the full House of Representatives reveals a clear legislative preference for voluntary unitization and an intent that compulsory unitization be limited to cases of "extreme necessity" where the parties had not agreed to unitize voluntarily:

> Section 17 of FCCS SCS HB 815 repeals Section 31.05.110(d), thus providing the Commissioner with the power to force all working and royalty interests in a pool or field, the boundaries of which are delineated by the Department, to cooperatively unitize their interests in a manner which protects correlative rights and provides for the management of field development and operation as a single unit, thus affording the best known methods for the prevention of waste as defined by AS 31.05.
>
> It is not the intent of the legislature that the Commissioner draft and impose a unitization agreement and the terms of the agreement upon the parties of

[24] Alaska Statute 31.05.110(d) provided that a compulsory unitization order would not be effective unless approved by the lessees of at least 62.5 percent of the unit area and the owners of at least 62.5 percent of the landowners' royalty interest. It was repealed in sec. 17 of ch. 160, SLA 1978; the AOGCC was granted its unitization authority in ch. 158, SLA 1978. Both of the bills that became ch. 160 and ch. 158--HB 815 and HB 830, respectively--were sponsored by Rep. Chatterton and were considered contemporaneously, or nearly so, during the committee hearing process in both the House of Representatives and the Senate. The bill that became ch. 160, moreover, was passed by both the House of Representatives and the Senate two days before the bill that became ch. 158 was passed. Under these facts, the history relevant to the repeal of AS 31.05.110(d) is "a proper source of evidence of legislative intent" underlying the AOGCC's unitization authority. *See State v. Bundrant*, 546 P.2d 530, 545 (Alaska), *app. dismissed sub nom. Uri v. Alaska*, 429 U.S. 806 (1976).

> interest, except in cases of extreme necessity. Rather it is the intent of the legislature that the Commissioner normally exercise his authority to encourage the parties in interest to timely negotiate and finalize a voluntary unit agreement, or, when petitioned to do so, and he considers unitization necessary for the purpose of meeting the intent of this chapter, by drafting an agreement for acceptance by the parties. The agreement should, to the extent possible, contain[] terms which meet the needs of all parties in a manner that encourages acceptance.

1978 House Journal (June 16, 1978) at 1720.[25] Broadly construing the AOGCC's compulsory unitization powers to permit it to compel amendment of a unit agreement approved by DNR under AS 38.05.180(p) would be contrary to the legislature's stated intent to encourage voluntary unitization and limit compulsory unitization to cases of "extreme necessity."[26] It would also be contrary to what one treatise calls the "guiding principle" when a question is raised as to the extent

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[25] HB 815 ultimately became ch. 160, SLA 1978. At the time the legislature passed the bill, the AOGCC had not yet been created and implementation of AS 31.05 was still the responsibility of the DNR. The references to the "Commissioner" and the "Department" were thus appropriate at the time the letter of intent was adopted. The letter nevertheless evinces a clear legislative preference for voluntary unitization under the statutes that now define the powers of the AOGCC.

[26] The only legislative history of AS 31.05.110(q) discovered to date is contained in what appears to be the minutes of the House Finance Committee for April 27, 1978 (p. 555). These minutes summarize the testimony of Rep. Chatterton, the sponsor of the bill that added subsection (q), as follows:

> Section 12, [Rep. Chatterton] advised, adds a new subsection (q) that tries to assure that the conservation statute applies equally to lands that are included in a unit and are under Title 38, which is now a very gray area.

This summary does not rebut the conclusion that subsection (q) makes *all* of AS 31.05.110 applicable to involuntary units and only subsections (a) and (g) through (p) applicable to unit plans approved under AS 38.05.180(p). Under subsection (q), the "conservation statute" clearly applies to lands included in a unit under Title 38; the only provisions of the statute that do not apply are those relating to compulsory unitization, as they are unnecessary where a unit has already been approved by the DNR. This legislative history does not overcome the apparent meaning of the statute. *Cf. Chokwak v. Worley*, 912 P.2d 1248, 1253 (Alaska 1996) (legislative history was insufficiently strong to require that literal language of statute be narrowed by interpretation).

to which an oil and gas conservation order can modify a pre-existing contract: "That is, there is a preference for freedom of contract. A. . .conservation order should extend only so far as necessary to prevent waste and protect correlative rights." 1 B.M. Kramer and P.H. Martin, *The Law of Pooling and Unitization* § 13.08 at 13-55 (3d Ed. 1994). This preference for freedom of contract is not surprising given, as noted previously, how difficult it is to unitize voluntarily. Such agreements "ordinarily are the products of long and careful negotiations among the owners of interests in the premises sought to be. . . unitized, [with the] negotiations extending in some cases over a number of years." Williams and Meyers, § 924 at 509. "Each negotiation has its own unique problems and substantial skills are required of those persons seeking to obtain agreement on a. . .unitization plan." *Id*. The record compiled in the AOGCC proceedings following issuance of C.O. 360 supports these general assertions, and shows, if anything, that negotiating the PBUA and the provisions in the Unit Operating Agreement implementing the PBUA's two participating area structure was even more difficult than the usual case.

5. Substantial considerations of public policy support the conclusion that the AOGCC's compulsory unitization powers do not extend to oil and gas interests that have already been included in a unit plan approved by the DNR

The AOGCC's primary responsibility is to prevent waste.[27] As identified in both AS 31.05.030(d)(9) and AS 31.05.110(a), its broader responsibilities are to prevent waste, to ensure

[27] Alaska Statute 31.05.030(b) states that the AOGCC "shall investigate to determine whether or not waste exists or is imminent, or whether or not other facts exist which justify or require action by it." The Wyoming Supreme Court, interpreting a statute that in all substantive respects is identical to AS 31.05.030(b), has stated that "the primary function" of Wyoming's analogue to the AOGCC is "the prevention of waste." *Majority of the Working Interest Owners in the Buck Draw Field Area v. Wyoming, Oil and Gas Conservation Commission*, 721 P.2d 1070, 1080 (Wyoming 1986).

a greater ultimate recovery of oil and gas, and to protect correlative rights. Its focus is on proper oil field engineering practices.[28] It has never been an active participant in the negotiation of unit agreements on state land.[29] It has no statutory authority to consider and no expertise in the kind of complex economic issues that will have to be resolved to protect the rights of all interested parties once the means of maximizing the recovery of oil and gas have been determined.[30] And it appears

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[28] *See, e.g.*, 1984 Inf. Op. Atty Gen. (April 24; 166-198-84) at 8-9 (footnote omitted):

> [T]he [A]OGCC, the duties and powers of which are set out in Title 31 of the Alaska Statutes, is responsible statewide for ensuring maximum recovery of oil and gas by means of conservation orders which dictate the engineering mechanics of oil and gas production (flow rate, surface casing requirements, etc.).

See also Testimony of AOGCC Chairman David Johnston before the Senate Resources Committee, September 12, 1995, at 17 ("in terms of our definition of waste, it doesn't talk to economics, but it talks about good oil field engineering practices"); *id. at* 28 (agreeing with Sen. Pearce that the AOGCC is concerned with "good engineering practices"); testimony of AOGCC Chairman Chat Chatterton before the Senate Special Committee on Oil & Gas, March 31, 1987 (minutes following "Number 348") (AOGCC does "limiting of production purely from an engineering standpoint").

[29] Although 20 AAC 25.517(a) requires generally that an operator file with the AOGCC for approval a plan of development and operation before the development and operation of an oil or gas pool, a different rule applies to operators on state leases: "If properties to be developed are leased from the state, and committed to a unit approved by the commissioner of the Department of Natural Resources under AS 38.05.180, the plan of development and operation, and all updated plans of development and operation, required by AS 38.05.180, must be submitted to the [AOGCC] *for informational purposes*." (Emphasis added.) 20 AAC 25.517 became effective April 2, 1986 (Register 97). Ken Boyd, Director of the Division of Oil and Gas in DNR, testified before the Senate Resources Committee, September 12, 1995, at 44, that the AOGCC does not have to "sign off" on either unitization or operating agreements on state land and that only DNR does so.

[30] *See* 1977 Inf. Op. Atty Gen. (February 14) at 7 ("the use of economic criteria, rather than engineering criteria, would represent a drastic change in regulatory practice in Alaska (and anywhere else for that matter) and thus, should only be undertaken in response to clear legislative direction"). *See also* testimony of AOGCC Chairman Chat Chatterton before the Senate Special Committee on Oil & Gas, March 3, 1987 (minutes at 4, following Number 348), on SB 49, a bill that, had it passed, would have added economic waste to the things that the AOGCC was to prevent (AOGCC does not

that its consistent and long-standing administrative practice has been to defer to DNR all issues other than oil field engineering practices.

DNR, on the other hand, although its authority generally applies only to land owned by the state, is responsible for implementing much broader public interests:

> DNR is responsible in large part for implementing the constitutional mandate that the legislature "provide for the utilization, development, and conservation of all natural resources belonging to the State. . . for the maximum benefit of its people." Alaska Const. art. VIII, § 2. *See* AS 44.37.020(a). In the area of oil and gas leasing, the agency's function is not to run an enterprise but to make decisions that "best serve the interests of the state." AS 38.05.035(e).

State, Department of Natural Resources v. Arctic Slope Regional Corporation, 834 P.2d 134, 143 (Alaska 1991).

When making decisions "for the maximum benefit of [the state's] people" and that "best serve the interests of the state" in administering state land for oil and gas purposes, DNR shares some of the same goals given the AOGCC under AS 31.05. Not surprisingly, to that end the legislature left with DNR powers similar to those it transferred to the AOGCC.[31] However, because

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have "in-house discipline" to address economic waste because it has no economists; "some agency would need some real sharp economists to administer it"); testimony of AOGCC Commissioner David Johnston before the House Oil and Gas Committee, February 10, 1992 (minutes following 92-7, Number 172), on HB 433, a bill that, had it passed, would have added "economic waste" to the things that the AOGCC was to prevent (AOGCC "didn't possess qualifications to determine economic waste); and AOGCC Chairman David Johnston's testimony before the Senate Resources Committee, September 12, 1995, at 16-17 ("nothing in our statute really points to considering economics"); *id*. at 26 ("We chose, at the time in '92, as a policy decision by the legislature and by the administration at that time, not to add economics to the powers and duties of the [AOGCC], and clearly, um, now under powers and duties, the [AOGCC] may regulate for conservation purposes, and is silent to economics").

[31] For example, as has been discussed, AS 38.05.180(p) authorizes state lessees to unite with others "in collectively adopting or operating under a cooperative or a unit plan of development or

DNR's responsibility is significantly broader than the AOGCC's with respect to state land, DNR also has authority to address both economic and physical recovery issues as part of its consideration of the overall best interests of state and the interests of other parties.[32] It has experience as an active participant in the negotiation and subsequent amendment of unit agreements on state land under AS 38.05.180(p), which includes the negotiation and subsequent amendment of the Unit Agreement at issue here. To the extent any state agency does, DNR has the expertise to address the kind of complex economic issues that have to be resolved to protect all interested parties where state oil and gas leases are involved. Under these circumstances, exempting unit plans approved by DNR under

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operation of the pool, field, or like area, or a part of it, when determined and certified by the commissioner to be necessary or advisable in the public interest." It also permits the commissioner to include a provision in state oil and gas leases "requiring the lessee to operate under a reasonable cooperative or unit plan" and to "prescribe a plan under which the lessee must operate" which "must adequately protect all parties in interest, including the state."

[32] Alaska Statute 38.05.180(a) includes a legislative finding that "(1) the people of Alaska have an interest in the development of the state's oil and gas resources to (A) maximize the economic and physical recovery of the resources." 11 AAC 83.303(a) provides that the commissioner of natural resources will approve a proposed unit agreement if it (1) promotes the conservation of all natural resources, including all or part of an oil or gas pool or field, (2) promote the prevention of both economic and physical waste, and (3) protect all interested parties including the state. In making those determinations, 11 AAC 83.303(b) provides, among other things that the commissioner will consider "(5) the economic costs and benefits to the state." Under 11 AAC 83.303(c), the commissioner will consider the criteria in (a) and (b) when evaluating any requested approval or authorization for a unit agreement, an extension or amendment of a unit agreement, a plan of exploration, development, or operations, a participating area, or a proposed or revised production or cost allocation formula. And DNR has formally determined that it has the legal authority to conduct investigations and issue orders related to the MI/NGL dispute giving rise to your request for this opinion. DNR Decision Regarding Jurisdiction, *supra* n. 19. The Alaska Supreme Court has recognized that the state's economic welfare is promoted "by maximizing the amount it receives for the lease of its lands" and "the legitimacy of using the state's police power to protect the government's financial stability." *Arctic Slope Regional Corp.*, 834 P.2d at 143.

AS 38.05.180(p) from the AOGCC's compulsory unitization powers is consistent with sound public policy.

B. The AOGCC Has No Implied Authority to Overturn Unit Plans Approved by DNR under AS 38.05.180(p)

As shown above, AS 31.05.110(q) limits the AOGCC's compulsory unitization authority to cases where the parties have not adopted a unit plan approved by the DNR under AS 38.05.180(p). The AOGCC, however, appears to suggest that the limitations imposed by AS 31.05.110(q) should not apply where the unit plan approved by DNR does not, in the AOGCC's view, sufficiently or "complete[ly]" unitize the oil and gas interests that have been made subject to the plan. *See* C.O. 360, Conclusion 18 ("It appears that more complete unitization and integration of interests in the Prudhoe Oil Pool will be necessary to prevent waste, ensure a greater ultimate recovery of oil and gas, and protect correlative rights. Consequently, in the absence of voluntary efforts, further hearings in this matter will be directed toward developing a plan of compulsory unitization"). Implicit in this suggestion is that the AOGCC has the power to review a "voluntary cooperative or unit plan of development or operation entered into in accordance with AS 38.05.180(p)," and to substitute its judgment for that of the DNR regarding whether the unit agreement is valid. The relevant statutes, however, contain no express grant of power to the AOGCC to review DNR's approval of a unit plan under AS 38.05.180(p) and, for the reasons discussed below, the courts are unlikely to find that the AOGCC has an implied power to do so.

An administrative agency "has no inherent powers, but only such as have expressly granted to it by the legislature or have, by implication, been conferred upon it *as necessarily incident to the exercise of those powers expressly granted.*" *State v. Dept. of Transp. of Wash.*, 33 Wash.2d

448, 206 P.2d 474-75 (1949) (emphasis added), *quoted with approval in Greater Anchorage Area Borough v. City of Anchorage*, 504 P.2d 1027, 1033 n.19 (Alaska 1972), *overruled on other grounds, City & Borough of Juneau v. Thibodeau*, 595 P.2d 626, 629 (Alaska 1979). *See State Farm Mutual Automobile Insurance Co. v. Barnes*, 585 P.2d 929, 931 (Colo. App. 1978) ("[p]owers not expressly granted to a regulatory agency will be implied only if such powers are necessary in order to achieve the objectives of the statute, and if the implied power is exercised in a reasonable manner"). In determining whether a power is necessarily implied, however, courts generally employ a rule of strict construction. *See Public Service Commission v. Formal Complaint of WWZ Co.*, 641 P.2d 183, 186 (Wyoming 1982) ("the statutes creating and empowering the [agency] must be strictly construed and any reasonable doubt of the existence of any power must be resolved against the exercise thereof"); *Williams v. Public Service Commission*, 754 P.2d 41, 50 (Utah 1988) ("[t]o ensure that the administrative powers of the PSC are not overextended, 'any reasonable doubt of the existence of any power must be resolved against the exercise thereof'"); *Swede v. City of Clifton*, 125 A.2d 865, 869 (N.J. 1956) ("where there is reasonable doubt of the existence of a particular power, the power is denied").

Consistent with these principles, the Alaska Supreme Court narrowly construes the scope of an agency's implied powers. *See McDaniel v. Cory*, 631 P.2d 82, 88 (Alaska 1981) (fine levied by Human Rights Commission held invalid where "no statutory authority exists which gives the Commission the power to award damages to complainants in public accommodation discrimination cases"); *Warner v. State*, 819 P.2d 28, 31 n. 1 (Alaska 1991) ("[f]ollowing *McDaniel*, we will narrowly interpret a statute as to the question of whether it grants the agency the discretion to promulgate rules").

There is no basis for concluding that the AOGCC has the implied power under its organic statutes to substitute its judgment for that of the DNR under AS 38.05.180(p) regarding the validity of a unit agreement among working interest owners holding state oil and gas leases. The limitations imposed by AS 31.05.110(q), which exempt unit plans approved by the DNR from the AOGCC's compulsory unitization powers, would be meaningless, or virtually so, if the AOGCC could ignore a DNR determination approving a particular unit plan. Such authority is not "necessarily incident to the exercise of those powers expressly granted" to the AOGCC, *Greater Anchorage Area Borough*, 504 P.2d at 1033 n.19, because that agency has broad powers apart from its compulsory unitization powers to prevent waste, ensure the greater ultimate recovery of oil and gas, and protect correlative rights, on and off state land. There is no need to imply the further power to review and reject DNR approvals of unit plans to enable the AOGCC to carry out its statutory responsibilities, and therefore the courts will not imply that power.

This conclusion is supported by the reasoning of the Alaska Supreme Court in *McDaniel*. The *McDaniel* court found no implied power to assess a damages remedy despite the Human Rights Commission's argument that "if a respondent. . . is not forced to pay damages, the purpose of the statute cannot as a practical matter be effectuated" and that "[t]his would result in many situations where no meaningful relief would be available." 631 P.2d at 88. The Court's response was that "[i]f there is merit to this argument, the legislature, rather than this court, must remedy the defect."[33] It nevertheless went on to consider and reject the merits of the Commission's

[33] *McDaniel*, 631 P.2d at 88. It should be noted that there was some legislative effort directed at resolving the jurisdictional dispute between the DNR and the AOGCC during the Second Session of the Nineteenth Legislature. On December 29, 1995, Representatives Green and Davis introduced House Bill No. 381, entitled "An Act relating to oil and gas conservation and recovery." Section 1

argument because "[t]he Commission has been given broad powers to enjoin and compel affirmative action to eliminate discriminatory practices and may construct an appropriate remedy without resort to damages." *Id.*

Like the Human Rights Commission in *McDaniel*, the AOGCC also "has been given broad powers to enjoin and compel affirmative action to eliminate" practices that are contrary to its statutory responsibilities, such as the waste of oil and gas, and thus "may construct an appropriate remedy without resort to" a remedy that has not been specifically provided for by the legislature. For example, under AS 31.05.030, the AOGCC may "regulate, for conservation purposes. . . the quantity and rate of the production of oil and gas from a well or property," and this authority expressly extends to a well or property in a unit plan approved by the DNR under AS 38.05.180(p). *See* AS 31.05.030(e)(6). In addition, the AOGCC has the power to require the making and filing of

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of this bill would have authorized the AOGCC to "modify a determination or action of the commissioner of natural resources authorized by. . .AS 38.05.180(p), (q), or (u); . . . ." Section 2 would have provided that an order of the AOGCC would prevail over "a determination or action of the commissioner of natural resources authorized by. . .AS 38.05.180(p), (q), or (u). . . . ." And section 3, the final section, would have amended AS 38.05.180(q) to provide that "the provisions of (p) of this section and this subsection may be modified by the Alaska Oil and Gas Conservation Commission by an order entered under AS 31.05.100 - 31.05.110." In a bill analysis dated January 8, 1996, the AOGCC (through David W. Johnston, Chairman), supported the bill on the ground that it "will remove any ambiguity about the prevailing authority of the Commission under its police powers to prevent waste, protect correlative rights and ensure a greater ultimate recovery [of oil and gas]." In a bill analysis dated January 25, 1996, the Department of Natural Resources (through Ken Boyd, Director of the Division of Oil and Gas) opposed the bill on a number of grounds, one of which was that it would "direct an agency not charged with maximizing the economic benefits from the State's lands, to control oil and gas development and operations on State lands," something that, in DNR's view, "could significantly impact the State's economic and financial welfare." In a letter dated February 12, 1996, addressed to David Koivuniemi, Deputy Commissioner of the Department of Administration, all three commissioners of the AOGCC recommended that, "[t]o help resolve these jurisdictional issues," the Department of Law undertake a "deliberate review of the statutes...in advance of any legislative effort to amend the law." The bill ultimately failed to pass.

reports, well logs and other information on wells drilled for oil or gas, AS 31.05.030(d)(2); the drilling, casing or plugging of wells to "prevent blowouts, cavings, seepages and fires," AS 31.05.030(d)(3); the furnishing of a reasonable bond sufficient to ensure the repair of a well causing waste, AS 31.05.030(d)(4); the measurement and fixing of gas-oil and water-oil ratios for particular wells, AS 31.05.030(d)(5); and the measuring and monitoring of oil and gas pool pressures, AS 31.05.030(d)(8). The AOGCC also has the power to investigate whether waste exists or is imminent, AS 31.05.030(b); impose penalties for violations of AS 31.05 or an AOGCC regulation or order adopted under it, AS 31.05.150; and seek injunctive relief any time "it appears that a person is violating or threatening to violate any provision of this chapter, or any regulation or order of the [AOGCC]." AS 31.05.160(a).

These authorities give the AOGCC a variety of options to accomplish the purposes of the state's conservation statutes that stop short of compulsory reunitization of a unit agreement entered into and approved by DNR pursuant to its statutory responsibilities. Indeed, the MI/NGL proceedings before the AOGCC, which culminated in C.O. 360 and an order requiring, at least in the short term, the production of the maximum amount of blendable NGLs by the working interest owners, prove the efficacy of these alternate procedures. Although the AOGCC may believe that altering the underlying contractual arrangements of the working interest owners as approved by DNR will be more efficient than dealing with allegations of waste on a case by case basis, the relevant statutes provide no authority to the AOGCC to review DNR approvals of unit plans under AS 38.05.180(p).[34]

[34] This conclusion is not inconsistent with the rule that an agency has the power to conduct proceedings to determine whether it has jurisdiction. *Cf. FPC v. Louisiana Power & Light Co.*, 406

C. Even If the Authority and Jurisdiction of the AOGCC and DNR Overlapped in Such a Way That the AOGCC Could Compel Unitization of Oil and Gas Leases on Terms Different Than Those Already Approved by DNR, Principles of Comity and Deference Would Require the AOGCC to Refrain from Exercising That Jurisdiction

The analysis above concludes that AS 31.05.110(q) unambiguously exempts oil and gas interests from the AOGCC's compulsory unitization powers where those interests are already subject to a unit plan approved by DNR under AS 38.05.180(p). Nevertheless, even if the limitations imposed by AS 31.05.110(q) could somehow be ignored, and the statutes defining the authority of the AOGCC were interpreted to permit compulsory reunitization of state oil and gas leases already subject to a DNR-approved unit plan, the fact the AOGCC can accomplish its statutory objective of preventing waste without infringing upon DNR's jurisdiction renders it likely that the Alaska courts would preclude the AOGCC from using its compulsory unitization powers here.

As noted above, shortly after statehood the legislature made DNR responsible for both conservation of oil and gas, under laws now codified at AS 31.05, and the management of state lands under AS 38.05. Prior to the 1978 legislation establishing the AOGCC, the potential for conflict between the administration of these two sets of laws was minimal because DNR

U.S. 621, 647 (1972) (applying doctrine that agency has primary authority to determine its own jurisdiction). Thus, although AS 31.05.110(q) exempts voluntary unit agreements and unit agreements approved by the DNR from the ambit of the AOGCC's compulsory unitization powers, the AOGCC has the authority to inquire, as an initial matter, whether there is, in fact, a voluntary unit agreement or a unit agreement approved by the DNR. Although it is unnecessary for the purposes of this memorandum to address the full scope of the AOGCC's power to review the validity of a voluntary unit agreement (other than one approved by the DNR), at a minimum it would have the authority to ensure that such an agreement is not a sham designed to avoid the Commission's jurisdiction. But where, as here, there is no question that the unit agreement at issue has been approved by DNR pursuant to its responsibilities under AS 38.05.180(p), the AOGCC's inquiry, at least insofar as its compulsory unitization powers are concerned, has reached the end of its statutory rope.

administered them both. As a result of the establishment of the AOGCC in 1978, however, both the AOGCC and DNR have at least some statutory authority over the production of oil and gas from state land, and the potential for conflict exists. This potential for conflict, though, imposes additional obligations upon both agencies: where two agencies share the same or comparable statutory responsibilities, each "must fully enforce the requirements of its own statute, but must do so, insofar as possible, in a way that minimizes the impact of its actions on the policies of the other statute." *New York Shipping Association v. Federal Maritime Comm'n*, 854 F.2d 1338, 1367 (D.C. Cir. 1988). "[T]he policies of diverse statutory regimes are best preserved if each agency scrupulously avoids deciding questions of law or policy that more properly lie within the jurisdiction of another agency, when a more limited inquiry into the requirements of its own statute is sufficient to dispose of the question before it." *Id.* at 1368. Furthermore, an administrative agency "'should be particularly careful in its choice of remedy. . . because of the possible effects of its decision on the functioning of [another statutory policy].'" *Id.* at 1370 (quoting *Burlington Truck Lines v. United States*, 371 U.S. 156, 172 (1962)).

The conclusion that an agency must choose to the extent possible a remedy that does not conflict with the jurisdiction of another is based upon necessary principles of comity and deference among related agencies. As one court has articulated it:

> [P]rinciples of comity and deference to sibling agencies are part of the fundamental responsibility of administrative tribunals charged with overseeing complex and manifold activities that are also the appropriate statutory concern of other governmental bodies. This is a corollary application of the broader principle that where a court has concurrent, discretionary jurisdiction with another court or an administrative agency, the decision to exercise jurisdiction *vel non* should be fully responsive to the competence, expertise and status of the other tribunal.

Hinfey v. Matawan Regional Board of Education, 391 A.2d 899, 907-08 (N.J. 1978) (citations omitted; emphasis added).[35] These principles "are designed to assure that a controversy, or its most critical facets, will be resolved by the forum or body which, on a comparative scale, is in the best position by virtue of its statutory status, administrative competence and regulatory experience to adjudicate the matter." *Id.*

Under the approach advocated in *Hinfey* and *New York Shipping Association*, the AOGCC, assuming it had the power to apply its compulsory unitization powers to oil and gas interests already subject to a unit plan approved by DNR, must analyze the alternatives it has for carrying out its statutory responsibilities in terms "of the possible effects those alternative courses of action may have on the functioning and policies" of DNR's statutory regime. If there is the

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[35] The New Jersey Court described the rationale underlying the rule of comity among agencies as follows:

> There is no reason, absent an occlusive statutory bar, for an administrative agency to be obtuse to the genuine concerns of other administrative agencies which possess concurrent jurisdiction over the same subject matter. This is especially so where the controversy is multidimensional and legitimately touches the competence of more than one agency. In that context, administrative agencies should never be encouraged to engage in internecine struggles for jurisdictional hegemony. The unilateral and possessive assumption of jurisdiction by one agency to the exclusion of another, perhaps more suitable, agency creates the risk that, although a many-sided controversy may be laid to rest in whole or in part from the vantage of a single administrative agency, in the process other important interests may be mishandled or neglected.

Hinfey, 391 A.2d at 907-08. "These precepts, prudently applied, serve as well to circumvent collisions between administrative agencies occupying similar areas and to avoid conflicts in agency decisions over the same subject matter." *Id.* at 908.

potential for interfering with DNR's responsibilities, it must choose the approach that avoids or at least minimizes that interference.[36]

Applying these principles here, it is apparent that an AOGCC order under its compulsory unitization powers to force the working interest owners to combine their interests in the initial participating areas would directly contravene DNR's determination that the separate participating area approach of the PBUA furthered the state's interests.[37] Moreover, an assertion by the AOGCC of the power to unilaterally realign the contractual arrangements of working interest owners in unit plans approved by the DNR has the potential to undermine DNR's authority to negotiate such plans on terms that reflect the best interests of the state. DNR may, for example, face unwarranted difficulties in negotiating unit plans for state oil and gas leases if state leaseholders view them as merely advisory or contingent and subject to unilateral modification by the AOGCC. More generally, unilateral action by the AOGCC invalidating the PBUA also may undermine the state's efforts to promote oil and gas development: if the holders of state leases cannot be assured that the agreements they reach with DNR will be honored by the AOGCC, it increases the risks and thus the costs of doing business with the state. And, for the policy reasons given previously, DNR "on a comparative scale, is in the best position by virtue of its statutory status, administrative competence

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[36] "[A]n agency, faced with alternative methods of effectuating the policies of the statute it administers, (1) must engage in a careful analysis of the possible effects those alternative courses of action may have on the functioning and policies of other statutory regimes, with which a conflict is claimed; and (2) must explain why the action taken minimizes, to the extent possible, its intrusion into policies that are more properly the province of another agency or statutory regime." *New York Shipping Association*, 854 F.2d at 1370.

[37] An order compelling the integration of the two participating areas would also conflict generally with DNR's decision to promulgate 11 AAC 83.351(a), which provides in part that "[s]eparate participating areas may be established to distinguish between an oil rim and a gas cap."

and regulatory experience," *Hinfrey*, 391 A.2d at 908, to approve unit plans that protect the best interests of the state, and particularly its economic interests, when state oil and gas leases are involved.

In sum, even if the AOGCC's statutory authority extended so far as to enable it to compel reunitization of oil and gas interests already subject to a unit plan approved by DNR, the courts are likely to consider an exercise of that authority under these circumstances to be an abuse of agency discretion. Because the AOGCC clearly has alternatives to compulsory unitization in carrying out its statutory responsibilities that do not directly conflict with the statutory responsibilities delegated to DNR, the AOGCC must choose one of those alternatives.

CONCLUSION

For all of the foregoing reasons, the AOGCC's compulsory unitization powers do not extend to oil and gas interests that are already subject to a unit plan entered into and approved by DNR under AS 38.05.180(p).

Very truly yours,

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