

Background

At the August 11, 2010 meeting, the staff presented to the Board details of proposed changes to the lease form. A copy of that presentation is included in your binders. The new lease form was developed after reviewing other states lease forms, the federal lease form, lease forms of large private landowners as well as considering best practices in the industry and issues that have arisen in the past.

At the August 11, 2010 meeting, the board authorized the staff to distribute the proposed new lease form for public comments.

Accordingly, we posted the new lease form on the department's website and requested that written comments be submitted by a certain date. At the request of one party, was subsequently extended an additional 2 to 3 months.

Written comments were received from 15 parties. Copies of those comments are included in your binders.

The staff reviewed and carefully considered each comment submitted. Based upon the comments received, the staff agreed that some changes were appropriate while other changes received were not in the best interest of the state.

There were 20 comments received from industry that we would like to present to you.

Comments That Do Warrant Changes to the Lease Form

1. Parties commented that the bonding requirements in the new lease form were too onerous.

The current lease form does not provide for bonding. The new lease form provides for a bond of not less than \$1,000,000.00 for the plugging and abandonment of wells drilled and damages caused by Lessee's operations. The bond amount shall be increased, if deemed necessary at the discretion of the Board.

Industry commented that the bond requirement was too high and should be reduced. The staff decided that the original bond be reduced to \$500,000.00 but that it could be increased if enumerated circumstances warranted it. The staff is recommending to the Board that the bond be reduced to \$500,000.00.

See paragraph 4, page 9

2. The additional cash payment for additional state-owned acreage is too onerous.

This provision does not exist in the present lease form. If state acreage was advertised and awarded as 20 acres and subsequently, it was claimed to be 35 acres, the Lessee would be liable to the state for additional bonus consideration for the newly discovered 15 acres. Industry requested clarification and the staff revised the initial language by making this provision apply to acreage existing at the time the lease was granted but not included. It shall exclude lands that erode while the lease is in effect, as well as, lands adjudicated to the State after the lease is granted.

See paragraph 1, page 4

3. Parties commented that requiring the release of deep rights at the end of the primary term is too soon.

This provision does not exist in the present lease form. Currently, if a well is producing on the leased premise, beyond the primary term, all depths are maintained by Lessee as long as the lease is in effect. Staff agreed that, due to the complications of deep drilling, additional time should be given for lessees to explore the deep production potential. This provision has been revised to allow Lessee the right to explore their deep production potential until two years beyond the primary term for additional rental payments if exercised.

See paragraph 3(e)(vi), page 7

4. Parties commented that the definition of pollution should be more narrowly described.

This provision is not satisfactorily defined in the present lease form. It reads as follows: Lessee further agrees that it will comply with all minimum water quality standards validly adopted by said governmental authorities with respect to oil pollution and noxious chemicals and waste being introduced into affected water areas. Industry suggested clarification and staff accommodated by adopting the following definition:

“Pollution” shall be deemed to include, without limitation, the intrusion of oil, natural gas, liquid or liquefied hydrocarbons, or carbon dioxide into any

segment of the environment not previously containing same or any environmental damage or contamination covered by La. R.S. 30:29 or La. R.S. 30:2015.1.

See paragraph (ix) , page 4; para 15(a), page 22, 23

5. Parties requested that insurance not be required until operations commence on the leased premises.

Operations are defined three times in the lease, none of which includes preparatory work, which can cause damage for which the required security would not be applicable if limited as requested by industry.

The language, in part, is written as follows,:

Lessee shall, at its sole expense, provide and maintain in full force and effect during the term of this Lease a general comprehensive liability insurance with Lessor as a named insured party in an amount not less than One Million Dollars (\$1,000,000.00) for each occurrence

See paragraph 16 , page 23, 24

6. Parties commented that the provisions for minimum royalties to be paid during concursus proceedings is overly burdensome.

Staff agreed that this language needed clarification and changes have been made to clear up the confusion. However, the staff did not agree that the basic premise of paying royalties into an escrow account or court registry should be changed. Under the present lease form, language therein, provides for reduction of ½ of the royalties. Having the funds paid into an escrow account protects the interests of the ultimately determined mineral owner/owners.

See paragraph 18, page 24

7. Parties commented that some terminology definitions should either be reworded or eliminated.

This has been done. Actually, we have taken all definitions appearing throughout the present lease form and placed them all together.

See pages 2, 3 and 4

8. Parties commented that liquidated damage penalties should be enforced only after notice.

*Staff agreed and the new lease form provides for thirty days written notice.
See paragraph 7(b) , page 16*

Comments Regarding Issues that Cannot be Addressed in the Lease Form

9. Parties commented that any data provided to the staff of OMR should not be a public record.

The present lease form does not allow any information provided by a Lessee to be held confidential. Any further exemption would require statutory authority which does not exist at present. However, it is not possible to exempt documents from the public records act via contract.

See paragraph 10(b) , page 18

10. Parties commented that audit records should not be public records.

The present lease form does not allow any information provided by a Lessee to be held confidential. Any further exemption would require statutory authority which does not exist at present. However, it is not possible to exempt documents from the public records act via contract.

See paragraph 20(a) , page 25

11. Parties requested that the environmental standards be discussed with industry representatives.

Staff agreed with this request and previously scheduled a meeting with the 15 parties who submitted written comments.

Comments That Are Not in the Best Interest of the State

12. Parties commented that approval prior to an assignment is too onerous.

The language in the present lease form merely states that prior approval by the Board is required. The language in the new lease form also provides that the original Lessee is not relieved of any of the obligations incurred under the lease. The language in the new lease form also provides that the assignee or

transferee be required to have financial security and insurance set forth as required in the lease.

See paragraph 8, page 16

13. Parties requested that the requirement to provide a final unit survey plat within 90 days of production be removed.

Staff agreed that removing this requirement is not in the state's best interest. A survey plat is needed to ensure that royalties are allocated to the proper funds. Ninety days after completion of the well is adequate time for an operator to procure a survey plat.

See paragraph 9(b), page 17

14. Parties requested that the requirements for shut-in payments during force majeure periods be removed.

The present lease form does not provide for shut-in payments during a force majeure event. Staff agreed that it is not in the state's best interest to change this requirement.

15. Parties requested the removal of the following language.

"In case of ambiguity, this Lease shall always be construed in favor of Lessor and against Lessee." Staff agreed that it is not in the state's best interest to change this language.

See paragraph 12, pages 19, 20

16. Parties requested the removal of the "keep whole" provision in the lease, which states "In no case should total royalty on residue gas and liquids extracted be less than the royalty which would be payable at the Lease on the unprocessed gas".

Staff agreed that it is not in the state's best interest to change this language. This provision ensures that the state will continue to receive the best possible price for its products.

See paragraph 12, pages 19, 20

17. Parties requested that the operator should not be required to verify the financial security of the assignee.

Staff agreed that it is not in the state's best interest to change this language. This requirement is necessary to ensure that leases are assigned to responsible parties only.

See paragraph 8(c), pages 16

18. Parties requested that unitization requirements should be removed from the lease form.

Staff agreed that it is not in the state's best interest to change this language. Unitization is needed to ensure that the state is fairly compensated for oil and gas production from its property and that the property will be fully developed.

See paragraph 3(e)(iii) , page 7

19. Parties requested that lease cancellation not be a remedy for drainage.

This is an obligation accepted by the Lessee to protect the Lessor. Staff agreed that it is not in the state's best interest to change this language.

See paragraph 5(c), page 11

20. Parties commented that state lease transfers and approvals should not be indefinite.

Staff agreed that it is not in the state's best interest to change this language. The commenting parties apparently misunderstand the language. Approval of transfers and assignments are not indefinite; they are conditional.

See paragraph 8(c), page 16

Recent Board Activity on Proposed New Lease Form

On April 11, 2012, the board adopted four new lease form provisions. In addition to the changes based upon the public comments, the staff has added those four

provisions to the new lease form. Those provisions were (1) an oil shut-in payment, (2) an increase to \$50 per acre for gas shut-in payments, (3) an increase of the primary term for inland leases to five years if an ultra-deep well is being drilled, and (4) reporting of royalty by well serial number.

On June 12, 2013 the board authorized the staff to complete the drafting of the revised oil and gas lease form that was previously discussed by the board. Since that time, the staff has met and reviewed the proposed new lease form. As stated during the board meeting, the new lease form is an effort to address some of the issues that have come before the board. Accordingly, the staff is proposing a few additional changes to the lease form. Those proposed changes are as follows.

Additional Proposed Changes

1. The force majeure language should be divided into two categories—traditional force majeure events and other suspending events.
2. Off lease operations and other non-drilling activities do not constitute drilling operations for the purpose of maintaining a lease. For example, one lessee attempted to use work on an off-site salt water disposal well to maintain the lease although there were no operations being conducted on the leased premises.
3. Marketing expenses are not allowable deductions from royalty. The definitions of deductions need to be clarified to ensure that unintended items are not deducted from royalty payments.
4. When a lease is not included in a unit, there should be one payor per lease. This provision has been included in operating agreements for a few years. This provision is needed to ensure that the state has been appropriately compensated for its production.

RESOLUTION

LOUISIANA STATE MINERAL AND ENERGY BOARD

LEGAL AND TITLE CONTROVERSY COMMITTEE

ON MOTION of Mr. Segura, seconded by Mr. Arnold, the following resolution was offered and adopted:

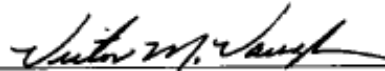
WHEREAS, a presentation by Staff was made in regard to the Proposed New Lease Form;

WHEREAS, after discussion and careful consideration by the State Mineral and Energy Board, a decision has been reached:

NOW, BE IT THEREFORE RESOLVED, that the Committee recommends that the State Mineral and Energy Board allow Staff the authority to present the Proposed New Lease Form to the public for comment.

CERTIFICATE

I hereby certify that the above is a true and correct copy of a Resolution adopted at a meeting of the Louisiana State Mineral and Energy Board in the City of Baton Rouge, Louisiana, on the 11th day of August, 2010, pursuant to due notice, at which meeting a quorum was present, and that said Resolution is duly entered in the Minute Books of said Louisiana State Mineral and Energy Board and is now in full force and effect.



LOUISIANA STATE MINERAL AND ENERGY BOARD