House
Legislative
Analysis
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MINERAL RESOURCES: REGULATE PPC CHARGES

House Bills 4280 and 4281
Sponsor: Rep. Larry DeVuyst
Committee: Conservation and Outdoor Recreation

Complete to 10-7-99

A REVISED SUMMARY OF HOUSE BILLS 4280 AND 4281 AS INTRODUCED 2-16-99

The bills would amend Part 615 of the Natural Resources and Environmental Protection Act (NREPA), which regulates oil and gas wells, to establish new procedures regarding gas leases and the methods by which postproduction costs (PPCs) are deducted from a lessor's royalty. Among other provisions, the bills would limit allowable PPCs and establish penalties for failure to comply with these limits. The bills are tie-barred to each other, and would take effect 90 days after enactment.

Public Act 127 of 1998 specifies, among other things, that a person who enters into a gas lease must provide the lessor with certain detailed information regarding gas production operations, and an itemized accounting of all postproduction costs, monthly revenue statements that itemized all deductions taken from the lessor's royalty payments and the price received for gas that had been sold. Though enacted, Public Act 127 could not take effect, since it was tie-barred to a bill (House Bill 4259 of 1997) that was not enrolled. (A "tie-bar" is a provision that specifies that a bill cannot take effect unless other specified legislation is also enacted.) House Bill 4281 would amend Public Act 127 to repeal the tie-bar, so that the 1998 act could take effect.

PPC Charges. Further, House Bill 4281 would amend Part 615 (MCL 324.61503b) to specify that a person who enters into a gas lease as a lessee could not charge PPCs unless it was explicitly allowed in the lease, in which case the deduction would be limited to the following:

1. The reasonable costs of the removal of carbon dioxide (CO_2), hydrogen sulfide (H_2S), molecular nitrogen (N_2), or other constituents, except water, the removal of which would enhance the value of the gas for the benefit of the lessor and lessee.

2. Transportation costs, after the point of entry, into any of the following: an independent, nonaffiliated, third-party-owned pipeline system; a pipeline system owned by a gas distribution company or any subsidiary of the gas distribution company, which is regulated by the Public Service Commission (PSC); or an affiliated pipeline system, if the rates charged by it had been approved by the PSC, or if the rates charged were reasonable, as compared to independent pipeline systems, based on the pipeline system's location, distance, cost of service, and other pertinent factors.

House Bill 4281 would also specify that a lessee who entered into a gas lease prior to, or after, the effective date of the bill, and who charged the lessor for any portion of postproduction costs, would have to notify the lessor, in writing, that a specific itemized explanation of all postproduction costs that the lessee proposed to assess was available.

Unit Areas. The bill would also specify that a lessee could not charge PPCs incurred on gas produced from one drilling unit, pooled or communitized area, or unit area, against a lessor's royalty for gas produced from another drilling unit, pooled or communitized area, or unit area. (The bill would define "unit area" to mean the formation or formations that were unitized and surface acreage that was a part of the unitized lands, as described in either the plan for unit operations approved by order of the supervisor of wells, or in an applicable agreement providing for unit operations.

Division Orders. House Bill 4281 would also specify that a division order from a lessee could not alter or define the terms of a lease unless voluntarily agreed to by both parties. In addition, a lessee could not precondition royalty payments upon a lessor who signed a division order, or other document stipulating how production proceeds were distributed, except as provided under the bill. As a condition for the payment of royalties, a lessee or other payor would be entitled to receive a signed division order from the payee, containing only the following provisions, unless others had been voluntarily agreed to by both parties:

3. The effective date of the division order.

4. A description of the property from which the oil or gas was being produced, and the type of production.

5. The fractional or decimal interest in production, or both, claimed by the payee; the type of interest; the certification of title to the production share claimed; and, unless otherwise agreed to by the parties, an agreement to notify the payor at least one month in advance of the effective date of any change in the interest in production owned by the payee, and an agreement to indemnify and reimburse the payor for payments, if the payee did not have merchantable title to the production sold.

6. The authorization to suspend payment to the payee for production until the resolution of any title dispute or adverse claim that had been asserted regarding the production interest being claimed by the payee.

7. The name, address, and taxpayer identification number of the payee.

8. A statement that the division order did not amend any lease or operating agreement between the interest owner and the lessee or operator, or any other contracts for oil or gas purchases.

House Bill 4280 would amend Part 615 (MCL 324.61503c) to establish the following penalties for failure to comply with the provisions of the bills.

9. A knowing violation of the provisions would be punishable by a civil fine of up to $1,000. A default in the payment of a fine, costs, or an installment of the fine or costs, could be remedied by any means authorized under the Revised Judicature Act.

10. The attorney general, or the lessor of a gas lease, could bring an action in circuit court for injunctive relief or damages, or both.

11. Each day a violation continued would constitute a separate offense for five days only. In addition, a violation that affected more than one lessor with an interest in the same well, pooled unit, or unitized area, would constitute only one offense.

12. A lessor could recover PPC amounts in damages in situations where a court found that the PPCs had been deducted in violation of the provisions of House Bill 4281. However, if a court found that the position taken by the nonprevailing party in the litigation lacked a reasonable basis, then the party who prevailed could recover reasonable attorney fees.

13. A person could not bring an action without first giving the lessee a written, reasonably comprehensive, notice of the alleged violation, and allowing at least thirty days for the lessee to cure the alleged violation.

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■This analysis was prepared by nonpartisan House staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.