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I. Case Law Developments

The one noteworthy development in Utah's oil and gas jurisprudence this year was the case of *J.P. Furlong Co. v. Bd. of Oil, Gas and Mining*.¹ In *Furlong*, the Supreme Court of Utah addressed a non-operator lessee's

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¹ 2018 UT 22, 424 P.3d 858 (Utah 2018).

challenge to a decision by the Board of Oil, Gas and Mining (“the Board”) to impose a joint operating agreement (“JOA”) between the non-operator, J.P. Furlong Company (“Furlong”), and the operator of the existing Board-approved drilling unit, EP Energy E&P Company, L.P. (“EPE”).² All but Furlong and two others in the drilling unit voluntarily pooled their interests and signed an industry-standard A.A.P.L. Model Form 610 JOA appointing EPE as unit operator.³

Furlong owned only a small fraction of the unit interest⁴ but refused to agree to the JOA the other unit owners entered. Instead, Furlong insisted on numerous modifications that called for EPE to adopt different operations and accounting procedures specific to Furlong’s minority interest.⁵ Furlong demanded the following seven revisions to the JOA proposed by EPE: (1) a no recording covenant; (2) a requirement that EPE account for and pay overriding royalties that burdened Furlong’s interest, in contrast to each lessee bearing its own revenue burdens as adopted by other unit owners; (3) an expansion of the industry custom “gross negligence or willful misconduct” operator liability standard to include *any* contractual breach of the JOA; (4) a condition that EPE deliver a supplemental authorization to each owner prior to any large expenditure; (5) an elimination of the operator’s right to make a ‘cash call’ for advanced funding of operations; (6) an extension of the statute of limitations for certain JOA contract claims; and (7) a restriction on EPE’s pricing procedure when utilizing its affiliates for JOA operations.⁶

EPE rejected nearly all of Furlong’s proffers and maintained that it would not change the JOA’s standard procedures to accommodate Furlong. As negotiations stalled, EPE sought a Board order to force pool Furlong and the remaining holdouts, asking the Board to impose the same JOA terms on the non-consenters agreed to by the consenting unit owners (without adopting any of Furlong’s proposed modifications). The Board found EPE’s application just and reasonable, relying on the common use of EPE’s JOA form in that unit and across the industry.⁷ Furlong argued on

² *Id.* at ¶1, 424 P.3d at 859.

³ *See id.* at ¶ 7, 424 P.3d at 860.

⁴ *Id.* at ¶ 6, 424 P.3d at 859 (“Furlong has an interest in only 1.04 percent of Tract 6, and just 0.12 percent of the drilling unit.”)

⁵ *See id.* at ¶¶ 13-19, 424 P.3d at 861-62.

⁶ *Id.*

⁷ *Id.* at ¶ 20, 424 P.3d at 862.

appeal that the Board's decision was not supported by substantial evidence⁸ and based on a misapplication of Utah law for failing to "balance the interests of competing parties."⁹ The court held the Board's decision was just and reasonable and supported by substantial evidence.¹⁰ The court also explained that the Board was not required to conduct an 'interest-balancing' test in deciding whether to impose the JOA.¹¹

The court first considered Furlong's claim that the Board's decision was not just and reasonable because it lacked sufficient evidentiary support, citing Utah's standard that "[a] decision is supported by substantial evidence if there is a quantum and quality of relevant evidence that is adequate to convince a reasonable mind to support a conclusion."¹² This threshold does not call for courts to reweigh evidence or determine whether the contested decision was correct; instead, the court focuses only on whether the decision was reasonable in light of relevant facts and circumstances under which it was made.¹³

The crux of Furlong's appeal arose from the Board's failure to explain why each of Furlong's specific changes to the JOA was not incorporated. The court acknowledged the Board could have provided more detail to support its conclusion; however, "recognizing that the Board could have crafted an order that better explained the Board's reasoning does not translate into a basis for concluding that the Board lacked substantial evidence for its decision that the JOA it imposed was just and reasonable."¹⁴ The court went on to distinguish the facts at hand from those in *McElhaney v. City of Moab*,¹⁵ which held an agency decision was not just and reasonable because it did not offer *any* factual support, leaving the court unable to determine what evidence, if any, the agency considered in its ruling.¹⁶ Unlike in *McElhaney*, the Board explained that adopting EPE's

⁸ *See id.* (Under Utah Code § 63G-4-403(4)(g), the court can set aside agency action is made upon a factual determination "not supported by substantial evidence when viewed in light of the whole record before the court.").

⁹ *Id.* at ¶ 24, 424 P.3d at 862.

¹⁰ *Id.* at ¶ 31 424 P.3d at 864.

¹¹ *Id.* at ¶ 39, 424 P.3d at 865.

¹² *Id.* at ¶ 25, 424 P.3d at 862 (quoting *Provo City v. Utah Labor Comm'n*, 2015 UT 32, ¶ 8, 345 P.3d 1242 (Utah 2015)).

¹³ *See id.*

¹⁴ *Id.* at ¶ 27, 424 P.3d at 863.

¹⁵ 2017 UT 65, 423 P.3d 1284 (Utah, September 21, 2017).

¹⁶ *See Furlong* at ¶¶ 27-28, 424 P.3d at 863 (*citing McElhaney* at ¶ 41).

JOA had a legitimate basis, which the court relied on to uphold the Board's decision.¹⁷

The court also rejected Furlong's claim that the Board was required to balance the interest of the parties in deciding whether to impose the JOA on Furlong. The applicable statute does not mandate, or even recommend, a balancing test.¹⁸ Yet, Furlong argued that Utah precedent in *Harken* required the Board to conduct an interest-balancing assessment.¹⁹ In *Harken*, the court ruled that because spacing orders issued by the Board must be just and reasonable under the statute, "spacing orders are dependent not only on a variety of factual determinations, but also on the need to balance the competing interests of affected parties and on the general requirement that they be reasonable."²⁰ The court here denied that *Harken* established a new statutory test for agency decision-making. Rather, "*Harken* stands for the unremarkable proposition that to be just and reasonable, in some cases the Board *may* have to 'balance the competing interests of affected parties.'"²¹

II. Legislative and Regulatory Developments

A. Legislative Developments

The Utah 2018 General Session produced a number of bills affecting the oil and gas industry.²²

Senate Bill 191, effective March 26, 2018, addresses the hot topic of state preemption and local authority to regulate oil and gas development. The bill clarifies that the state holds exclusive jurisdiction over oil and gas activity throughout Utah. It adds an express condition that local rules

¹⁷. See *id.* ¶ 33, 424 P.3d at 864 ("Although we can sympathize with Furlong's desire to get more explanation from the Board, we cannot conclude that the Board's decision lacked substantial evidentiary support. Nor can we conclude that the Board imposed a JOA that was unjust or unreasonable when the record confirmed that it was based upon the industry accepted model form and was materially the same agreement that the other non-operators in the drilling pool voluntarily agreed to.").

¹⁸. See *id.* ¶ 39, 424 P.3d at 865.

¹⁹. See *id.* at ¶37, 424 P.3d at 865 (citing *Harken Southwest Corp. v. Board of Oil, Gas and Mining*, 920 P.2d 1176 (Utah 1996)).

²⁰. See *id.* (quoting *Harken*, 920 P.2d at 1179).

²¹. *Id.* at ¶ 39, 424 P.3d at 865 (emphasis added) (citation omitted).

²². This section is intended to summarize each bill's key components and should not be considered an exhaustive summary of any particular bill or resolution.

“comply with the state’s exclusive jurisdiction,”²³ providing that a municipality or county may not regulate surface activity deemed “incident to an oil and gas activity”²⁴ unless the municipality demonstrates that the new rule

(i) is necessary for the purposes of this chapter;²⁵ (ii) does not effectively or unduly limit, ban, or prohibit an oil and gas activity; and (iii) does not interfere with the state’s exclusive jurisdiction to regulate oil and gas activity, “as described in [newly-enacted] Section 40-6-2.5.”²⁶

The new Section 40-6-2.5 pronounces oil and gas activity as a matter of statewide concern for which the state has exclusive jurisdiction over “the whole field of potential regulation.”²⁷ This section also defines “oil and gas activity” as

any activity associated with the exploration, development, production, processing, and transportation of oil and gas as set forth in Title 40, Chapter 6, Board and Division of Oil, Gas and Mining, including: (i) drilling; (ii) hydraulic fracture stimulation; (iii) completion, maintenance, reworking, recompletion, disposal, plugging, and abandonment of wells; (iv) construction activities; (v) secondary and tertiary recovery techniques; (vi) remediation activities; and (vii) any other activity identified by the Board of Oil, Gas and Mining.²⁸

House Bill 27, effective May 8, 2018, introduces a few changes to Utah’s Underground Storage Tank Act (the “USTA”). In continuing the USTA for another ten years,²⁹ this bill increases the maximum amount of the director

²³ S.B. 191, 2018 Gen. Sess. (Ut. 2018) (amending Utah Code § 10-9a-102 and § 17-27a-102).

²⁴ *Id.* (amending Utah Code § 10-9a-102).

²⁵ The purposes of these chapters, which grant land use authority to local governments, include “health, safety and welfare,” and various other purposes as stated in § 10-9a-102(1) and § 17-27a-102(1).

²⁶ *See* § 10-9a-102(3)(b); § 17-27a-102(3)(b); § 40-6-2.5.

²⁷ S.B. 191, § 40-6-2.5.

²⁸ *Id.*

²⁹ *See* H.B. 27, 2018 Gen. Sess. (Ut. 2018) (amending Utah Code § 63I-1-219 (extending the Act’s repeal date to July 1, 2028)).

loans available from the Petroleum Storage Tank Trust Fund,³⁰ and mandates that any applicant for a director loan to upgrade or replace an underground storage tank participate in the USTA's Environmental Assurance Program.³¹

House Bill 419, effective May 8, 2018, introduces two notable efficiencies to Utah's statutory pooling scheme. First, it expands the Board's authority to issue retroactive pooling orders if no one objects *or* if the source(s) of objection(s) received "engaged in inequitable conduct prejudicing another party's correlative right."³² Second, this bill reduces administrative burdens on operators by establishing that, subject to certain exceptions,³³ the terms of an initial Board order to pool interests in a drilling unit (and the terms of any Board-approved unit JOA) will automatically apply to subsequent wells drilled in the unit.³⁴

B. Regulatory Updates

This March, the Utah Department of Air Quality ("DAQ") overhauled its permitting system for many oil and gas well site sources. The various rule changes³⁵ aim to streamline a 'permit by rule' structure that will replace the need to apply for an individual permit for each minor source related to oil and gas operations, which accounted for more than half of the DAQ's minor-source permits in recent years.³⁶ To maintain appropriate measurements to implement this new program, existing sources were required to register with the DAQ before July 1, 2018.³⁷

³⁰ *See id.* (increasing loan amounts available under § 19-6-409(8)(a)(i) from \$150,000 to \$300,000 for all tanks at any one facility, and § 19-6-409(8)(a)(ii) from \$50,000 to \$100,000 per tank).

³¹ *See id.* (amending 19-6-409(6)(b)(ii); *see also* Utah Code § 19-6-410.5 for the Environmental Assurance Program).

³² H.B. 419, 2018 Gen. Sess. (Ut. 2018) (amending § 46-6-6.5(11)(b)(ii)).

³³ *See id.* (enacting § 46-6-6.5(11)(b)(ii)).

³⁴ *See id.*

³⁵ *See* UTAH ADMIN. CODE r. 307-401, 307-504-10 (2018).

³⁶ *See Oil & Gas Source Registration (Air Quality)*, Utah Department of Environmental Quality Division of Air Quality, <https://deq.utah.gov/air-quality/oil-gas-source-registration-air-quality> (last visited Oct. 2, 2018).

³⁷ *See id.*