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OIL & GAS NEWSLETTER

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MSU Extension has a web page that contains information regarding oil and gas leasing, mineral rights and other related informational topics at
http://msue.anr.msu.edu/program/info/oil_and_gas

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Crude oil supplies appear stable for the future

Despite widespread conflict in the Middle East, world supplies and prices of crude oil are stable.

Curtis Talley Jr., Michigan State University Extension

It was not that long ago that even a rumor of conflict in the Middle East sent crude oil futures prices soaring. Despite current widespread conflict in the traditional oil producing areas of the Middle East, crude oil supplies are increasing and prices are declining.

The major developments that have changed the world of energy production are horizontal drilling and hydraulic fracturing. For many years, shales were known to contain hydrocarbons, but production was not economical. Now the Marcellus, Bakken and Barnett shales are world class producers of crude oil or natural gas due to hydraulic fracturing.

Why are crude oil supplies forecast to be stable for the foreseeable future?

1. The U.S. is now a leading producer of energy in the world

The U.S. produces more liquid petroleum (11 million barrels/day) than Russia or Saudi Arabia. "The increase in domestic crude oil production of 3.6 million barrels a day in less than four years, has reversed almost four decades of decline", according to "The Shale Boom Shifts into Higher Gear", published by the *Wall Street Journal*, on May 31, 2015. Spurred by the use of hydraulic fracturing or fracking in shale rock deposits, U.S. oil production has jumped from 5.0 million barrels per day in 2004 to an average of 9.3 million in 2015, according to the Energy Information Administration (EIA), the analytical arm of the Department of Energy as reported in the *U.S. Field Production of Crude Oil Weekly Report*.

2. Drilled wells that are shut-in (not producing) will be developed and add to supply

The drop in crude oil prices from $95 a barrel three years ago to less than $60 a barrel today have prompted U.S. shale oil producers to reduce drilling. These prices have also delayed the development of drilled wells that have yet to be fractured and produced. According to “The Shale Boom Shifts into Higher Gear”, published by the *Wall Street Journal*, on May 31, 2015, it is likely that as oil prices rise, these wells will be completed, adding to the supply.

3. New well drilling and development technology

Lower oil prices are driving drillers and well developers to find new efficiencies. The surge in oil production has come from horizontally drilled wells targeting the well bore at the most productive geologic layers, from multiple well pads, with laterals up to 15,000 feet long. “Leading edge operators report that they can produce more profitably today at a price of $65 a barrel than they could at $95 a barrel three years ago”, according to “The Shale Boom Shifts into Higher Gear”, published by the *Wall Street Journal*, on May 31, 2015. Despite idle rigs and laid off workers, U.S. onshore production has gone up since last fall, not down.

4. OPEC has no plans to cut production

Despite the invasion of ISIS into Iraq, its oil production was 3.8 million barrels per day in May. If this level is sustained, it will set a national record. Saudi Arabia produced 10.3 million barrels per day in May, which is up over 600,000 barrels per day since it decided to continue pumping at current levels to maintain market share. Saudi Arabia’s oil minister stated “Even if prices were to fall to $20 a barrel, we don’t think we will reduce exports. We will increase oil production”, according to “Saudi Arabia, Iraq Push OPEC Over Oil Cap,” published by the *Wall Street Journal* on June 11, 2015. OPEC is also aware that Iran plans to add up to one million barrels per day to the global market in the event of a nuclear deal.

5. Despite low prices, supplies of crude oil in storage are at historic highs

February crude oil inventories show that total utilization of crude oil was 60 percent of storage capacity in the United States compared with 48 percent at the same time last year. Capacity was about 67 percent full in Cushing, Oklahoma (the delivery point for West Texas Intermediate futures contracts), compared with 50 percent at this point last year. From September 2013 to September 2014, crude oil storage capacity was increased by 19 million barrels at Cushing.

The Wall Street Journal reported in March of 2015 that “U.S. crude oil supplies are at their highest level in more than 80 years, according to data from the Energy Information Administration”, according to “Crude, Crude Everywhere and Nowhere to Put It” by Nicole Friedman, published in the *Wall Street Journal* on March 6, 2015. Crude oil is being stored in tanks, underground salt caverns and leased tankers. It is against the law to export U.S. crude, which leaves few alternatives, other than to store any excess.

Oil and gas leasing occurring in targeted areas

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In 2005, the price of West Texas Intermediate crude oil was approximately $70 per barrel. It is now approximately $46 per barrel. Current prices make it very challenging for oil and gas production companies to be profitable. Despite these economics, companies need to continuously search for new oil and gas supplies to replace what is being pumped today.

Recently, the author was contacted by a landowner that attended a public MSU Extension oil and gas leasing educational workshop in 2012 in Gladwin County and wanted some of the information that he recalled being presented at the meeting. He had never negotiated an oil and gas lease, but was currently in lease negotiations. His goal was to align the lease terms with his land usage and income goals. The company had already agreed to the following changes: the lease was changed to non-development and prohibited any surface disturbance to the land; the royalty was increased from 1/8 of the net income to 1/6 of the gross (>100% increase) and a $100/acre leasing bonus. The landowner was now going to hire a qualified oil and gas attorney to help him complete negotiations.

HOW DOES WHAT THIS LANDOWNER DID ALIGN WITH ADVICE FROM AN OIL AND GAS ATTORNEY?

Aaron Bowron is an oil and gas attorney that has volunteered to speak at MSU Extension oil and gas leasing and oil and gas industry public informational meetings. Here are some of his reminders: “Most clients in my experience prefer a non-developmental lease; i.e., they simply do not want a well on their property. For those that do not mind siting a well on their property, however, I often counsel that environmental and aesthetic concerns should be of paramount concern—perhaps even of greater importance to economic considerations when negotiating the terms of an oil and gas lease—given that a successful well may produce for decades. Many oil and gas companies are, perhaps contrary to general public perception, reputable and often accommodating to lessor’s legitimate environmental and aesthetic concerns. In this regard, the importance of sound legal advice when presented with an oil and gas lease cannot be overstated; many potential lessors have no familiarity with the oil and gas industry, and are generally unaware of what their concerns should be. Too often, potential lessors fixate on the financial dimensions of an oil and gas lease. While that is understandable, economic considerations alone should not drive the negotiating process”.

"As for economics, they obviously remain important, and my clients through legal counsel have successfully negotiated for and obtained greater royalties, lease-signing bonuses, and shut-in payments. When negotiating the terms of a lease, a critically important provision bearing on the economics is the Pugh clause. Without this clause, an oil and gas company can hold the entirety of the acreage under lease notwithstanding that only a portion thereof has been unitized or combined with other lands into a producing oil and gas unit. This effectively ties up lands or formations that otherwise could be re-leased".

Aaron K. Bowron is an attorney with Zirnhelt, Bowron & Wiggins, PLC, and offices in Oakland County. He counsels and represents both landowners and oil and gas companies throughout the state in drafting, negotiating and litigating oil and gas matters. He can be reached at abowron@sbcglobal.net or 810-287-2323.

Northern Michigan Mineral Owners Coalition to hold annual meeting

Northern Michigan Mineral Owners Coalition will be holding their Annual General Membership Meeting on October 10, 2015 at 7:00 PM. The meeting will be held at the Thunder Bay Resort; 27800 M-32; Hillman, MI 49746. Non-members are invited to attend by registering prior to the meeting by contacting NMMOC by email at nmmoc@att.net. In addition, an informational meeting introducing NMMOC to the public will be held from 5:00 to 6:30 PM at the same location.

Northern Michigan Mineral Owners Coalition is a coalition of mineral owners with property located in the northern half of the Lower Peninsula. By combining the acreage of a large number of mineral owners, the members seek to gain leverage in all aspects of the hydrocarbon resource development process. Membership in the coalition is open to all mineral rights owners. Additional information is available at our website, nmmoc.org or by contacting us at nmmoc@att.net.

Please Share Your Oil and Gas Experiences

The editor is very interested in hearing both your positive and negative experiences dealing with oil and gas leasing or production. All information is kept confidential and is combined with data from other landowners to analyze the effectiveness of the educational effort. Report your experiences to the editor by phone at 231-873-2129 or talleycu@anr.msu.edu e-mail.

This newsletter is intended for landowners and other members of the public with interest in the oil and gas industry. If you would like to be added to the e-mail list to receive this newsletter, please contact the editor. You can also contact your local county MSU Extension Office to obtain copies of the newsletter and other free oil and gas leasing information.