



RAILROAD COMMISSION OF TEXAS

HEARINGS DIVISION

PROPOSAL FOR DECISION

OIL & GAS DOCKET NO. 7B-0275548

COMMISSION CALLED HEARING TO PROVIDE DMR OPERATING, INC. AN OPPORTUNITY TO SHOW CAUSE WHY THE PLUGGING EXTENSION FOR THE MITCHELL, G.H. (23006) LEASE, WELL NO. 2C BIG HOLE (ATOKA "C") FIELD, PALO PINTO COUNTY, TEXAS SHOULD NOT BE REVOKED PURSUANT TO 16 TEX. ADMIN. CODE § 3.15(h) AND DMR ORDERED TO IMMEDIATELY PLUG THE INACTIVE WELL

APPEARANCES

FOR DMR OPERATING, INC.

Stephen A. Fox, Attorney at Law
J. D. McClure, DMR Operating, Inc.
Lisa Barfield, Petro Energy Group

FOR THE RAILROAD COMMISSION OF TEXAS

Reese B. Copeland, Attorney, Enforcement Section
Sheila Weigand, Investigator, Office of General Counsel

ALSO APPEARING

Joe E. Mitchell, Mineral estate owner

PROCEDURAL HISTORY

Date of request for hearing:	March 24, 2012
Date of notice of hearing:	April 11, 2012
Dates of hearing:	May 24, 2012 August 24, 2012
Heard by:	Terry J. Johnson, Legal Examiner Andres J. Trevino, Technical Examiner
Date record closed:	August 24, 2012

SUMMARY

Operator requests a hearing to challenge a determination that it lacks a good faith claim to operate the subject lease. The record demonstrates that the operator does not hold a good faith claim. It is recommended that the Commission order the operator to plug the subject wellbore.

OPERATOR'S CASE

TWO FOR ONE

J. D. McClure is the principal of DMR Operating, Inc. (DMR). Mr. McClure testified that he acquired the Mitchell, G.H (23006) lease in 1995 as the result of a law suit.

"The man that owned the gathering system for us defrauded us out of a lot of money and we sued him and the company that owned the gathering system at that time for defrauding us. [. . .]They gave us the gathering system and all the assets we could find, which was almost nothing but this one well."

The well was No. 2C, completed in the Big Hole (Atoka "C") field at a depth of 4184' to 4200'. The wellbore, however, was actually a dual completion. Another well, the Mitchell, G.H. (21659), Well No. 2, is completed in the slightly deeper Big Hole (Congl. 4232) formation.

The record operator of Well No. 2 is WRH & Associates, Inc. (WRH). WRH is a defunct entity that for decades had filed no production reports for its Mitchell (21659) lease, a failure that resulted in the selection of Well No. 2 for state-funded plugging in 2009.

In advance of plugging, District 7B field operations personnel inspected the lease site in the Fall of 2009. This inspection found piping connections that appeared to show commingled production of Well No. 2 and Well No. 2C. After determining that DMR held no permit authorizing commingled production, the District 7B Field Office directed DMR to obtain a Rule 26 commingling permit. By letter dated October 28, 2009, the District Office notified DMR that, in the absence of a commingling permit, the Mitchell, G.H (23006) lease would be severed.¹ DMR could have requested a hearing to challenge this action, but did not. In Mr. McClure's view, it was not worth the cost. Instead, DMR just stopped working the lease.

"It was going to be shut in, so why have a hearing? The Railroad Commission wanted me to hire a consultant and a lawyer to

¹ A severance bars both production and transportation of oil from a lease.

straighten this matter out. Now how can I do that at \$100 a month?
That's why we didn't do it."

[...]

"We thought the letter said 'cease operations'".

The severance was issued on December 7, 2009 and has remained in effect since that date.

In April 2010, DMR retained a consultant and began the process of obtaining a permit to commingle the production of Well No. 2 with Well No. 2C. Because WRH was the record operator of Well No. 2, the first step in the process required DMR to obtain Commission approval to transfer regulatory responsibility of the Mitchell (21659) lease from WRH to DMR.

A typical transfer is accomplished through the submission of a Form P-4 (Certificate of Compliance and Transportation Authority) that has been signed by both the outgoing and incoming operator. Since WRH was defunct and no signature available, Commission rules allowed DMR to submit a single-signature P-4 in support of the transfer.² A threshold condition for approval of a single-signature P-4, however, required DMR to demonstrate that it held a good faith claim to operate the Mitchell (21659) lease.

On May 12, 2010, DMR submitted a 1995 oil and gas lease (the base lease) that appeared to cover Well No. 2. This instrument was referred to Hearings Examiner Marshall F. Enquist for review. His review found that the agreement contained a cessation clause which automatically terminated the base lease after 60 days of non-production. After determining that Commission records showed that the Mitchell, G.H. (21659) lease had reported no production since January 1993, Examiner Enquist wrote to DMR asking the operator to explain how the base lease was still valid. DMR did not reply to his May 19, 2010 letter. On December 28, 2010, processing of the transfer was terminated.

HEARING

On August 30, 2011, Examiner Enquist notified DMR that the lessors of the 1995 base lease had filed a formal complaint and affidavit of non-production challenging DMR's right to operate under the 1995 lease. After a serial exchange of correspondence among Examiner Enquist, the lessors and DMR, Examiner Enquist determined that DMR had failed to demonstrate that it held a good faith claim to operate the properties. The case at hand is DMR's challenge to that determination.

² See, 16 TEX. ADMIN. CODE § 3.58(a)(4)

DISCUSSION

GOOD FAITH CLAIM

The record in the case contains no evidence that DMR is, or has ever been, record operator of the Mitchell, G.H. (21659) lease. Accordingly, the sole issue presented for resolution is whether DMR has a good faith claim to operate the Mitchell, G.H. (23006) lease.

The record also reflects that DMR and its consultant undertook protracted efforts to obtain the P-4 transfer of Well No. 2 as well as the difficulties they encountered after the unexpected discovery of an additional well on the Mitchell, G.H. (21659) lease that, because of this well's uncertain plugging history, would require DMR to pursue a separate permit authorizing subdivision of the lease acreage. The record additionally reflects Mr. McClure's claimed confusion about the procedures required for the transfer of Well No. 2 to DMR and his assumption that he did not need to respond to Examiner Enquist's letter because he thought his consultant was handling that matter as part of the effort to transfer the well and subdivide the lease. Further, the record contains facts--many of them in conflict--relating to whether the No. 2 and the No. 2C were commingled. None of this, however, is entitled to persuasive weight because none of it informs the determination of whether DMR holds a good faith claim to operate the Mitchell, G.H. (23006) lease.

PRODUCTION

DMR's good faith claim to operate the Mitchell, G.H. (23006) lease rests on proof that DMR is producing oil from the property. But according to Mr. McClure, even though it had been reporting oil production to the Commission since 1995, DMR never produced any oil from the lease.

Moreover, Mr. McClure--who testified that he had 50 years of experience in the oil industry--said he did not know the well on the lease has always been classified on Commission records as an oil well. "We didn't know it was an oil well, we thought it was a gas well," he said, "we never produced any oil." When asked why DMR has been reporting the production of oil since it took over the lease in 1995, Mr. McClure testified that he didn't want to report zero production.

"And normally with record keeping, you don't send the Railroad Commission [a] zero. So you could very well say they produced one barrel of oil--one barrel of condensate--this month, just to keep from putting zeros there. You say 'somebody stole it', 'it evaporated', they don't like that."

Mr. McClure's testimony supports the conclusion that the lease produced nothing at all.

(By Examiner Johnson)

Q: What do you mean by condensate?

A: It's the gas that comes out of the—the liquid that comes out of the natural gas as it changes temperature as it's coming to the surface.

Q: What do you do with that liquid?

A: You sell it with the oil.

Q: But you don't produce oil.

A: No, I don't sell any oil.

Q: What do you do with the liquid that's produced?

A: It usually evaporates.

Q: Where do you store it until it evaporates?

A: In that 210-barrel tank, just like you store oil.

When asked whether there was anything in the two tanks on the lease, Mr. McClure answered in the negative.

“Not to my knowledge. We're not putting anything in them. Normal gas production, you get condensate, right? If we'd made any condensate it would have gone into those [tanks].”

Mr. McClure also testified that DMR had sold no condensate since taking over the lease in March 1995. “Never had any to sell,” he said. This testimony is consistent with photographic evidence introduced at hearing: the tanks, long ago perforated by rust, were incapable of holding liquid.

In sum, the record evidence supports the conclusion that DMR does not have a good faith claim to operate the subject lease.

CONCLUSION AND RECOMMENDATION

Despite DMR's false reports of oil production from the Mitchell, G.H (23006) lease, Well No. 2C is an inactive well.³ As operator of record, DMR is required to either plug the well or obtain a plugging extension.⁴ In order to obtain a plugging extension, DMR must hold

³ TEX. NAT. RES. CODE § 89.002(a)(12)

⁴ 16 TEX. ADMIN. CODE §§ 3.14(b)(2), 3.15

a good faith claim to a right to operate the lease.⁵ It does not. Neither has DMR commenced plugging operations.

Accordingly, it is recommended that the Commission adopt the findings and conclusions set out below and enter an order directing DMR Operating, Inc. to plug the subject well and to do all other things required to bring the subject lease into compliance with the requirements of law.

FINDINGS OF FACT

1. DMR Operating, Inc. (DMR) holds Operator Number 221514.
2. Since March 1995, DMR has been the record operator of the Mitchell, G.H. (23006) lease, in Palo Pinto County, Texas.
3. The Mitchell, G.H. (23006) is completed as an oil lease.
4. The Mitchell, G.H. (23006) lease has one well, the No. 2C
5. For the period March 1995 through and including November 2009, DMR filed production reports with the Commission showing production of oil from the Mitchell, G.H. (23006) lease.
6. For the period March 1995 through and including November 2009, the Mitchell, G.H. (23006) lease in fact produced no oil.
7. Well No. 2C on the Mitchell, G.H. (23006) lease is, and remains, an inactive well.
8. A December 2, 1995 oil and gas lease between DMR and lessors G.H. Mitchell, Joe E. Mitchell and Jerry R. Mitchell (Mitchell base lease) governs acreage assigned to the Mitchell, G.H. (23006) lease.
9. The Mitchell base lease contains a 60-day cessation clause that terminates the lease after 60 days of non-production.
10. The Mitchell, G.H. (23006) lease did not produce from March 1995 through and including November 2009, a period of 14 years and 8 months.
11. DMR does not hold a good faith claim to operate the Mitchell, G.H. (23006) lease.


CONCLUSIONS OF LAW


1. Resolution of the subject dispute is a matter within the jurisdiction of the Commission. TEX. NAT. RES. CODE § 85.051

⁵ TEX. NAT. RES. CODE § 89.023(a)(2); 16 TEX. ADMIN. CODE § 3.15(e)(3)

2. DMR Operating, Inc. is the record operator of the Mitchell, G.H. (23006) lease; Well No. 2C on that lease is an inactive well. TEX. NAT. RES. CODE § 89.002
3. DMR Operating, Inc. does not hold a good faith claim to operate the Mitchell, G.H. (23006) lease. 16 TEX. ADMIN. CODE § 3.15(a)(5)
4. DMR Operating, Inc. is required to plug Well No. 2C. TEX. NAT. RES. CODE § 89.011; 16 TEX. ADMIN. CODE § 3.14

RESPECTFULLY SUBMITTED on this the 1st day of November, 2013.


TERRY J. JOHNSON
Legal Examiner


ANDRES J. TREVINO
Technical Examiner