

April 22, 2008

OIL AND GAS DOCKET NO. 01-0252082

ENFORCEMENT ACTION AGAINST JPW ENERGY, L.L.C. (OPERATOR NO. 427871) FOR VIOLATIONS OF STATEWIDE RULES ON THE E.J. PRUITT -E- (01404) LEASE, WELL NO. 18, PRUITT FIELD, AND E.J. PRUITT E5 (13965) LEASE, WELL NOS. 28, 29, 30, 32 AND 49, SE PRUITT (OLMOS) FIELD, ATASCOSA COUNTY, TEXAS.

APPEARANCES:

For Railroad Commission of Texas:

Susan German, Staff Attorney, Enforcement Section, Office of General Counsel

For Respondent JPW Energy, L.L.C.

Phil Watkins, Attorney, President

PROPOSAL FOR DECISION

PROCEDURAL HISTORY

COMPLAINT FILED:	June 18, 2007
DATE CASE HEARD:	January 24, 2008
PFD PREPARED BY:	Mark Helmueller, Hearings Examiner
RECORD CLOSED:	April 18, 2008
PFD CIRCULATION DATE:	April 22, 2008
CURRENT STATUS:	Protested

STATEMENT OF THE CASE

This was a Commission-called hearing on the recommendation of the District Office to determine the following:

1. Whether respondent should be required to plug or otherwise place in compliance with Statewide Rule 14, the E.J. Pruitt -E- (01404) Lease, Well No. 18, Pruitt Field, and E.J. Pruitt E5 (13965) Lease, Well Nos. 28, 29, 30, 32 and 49, SE Pruitt (Olmos) Field, Atascosa County, Texas;
2. Whether the respondent violated provisions of Title 3, Oil and Gas, Subtitles A, B, and C, Texas Natural Resources Code, Chapter 27 of the Texas Water Code, and Commission rules and laws pertaining to safety or prevention or control of pollution by failing to comply with

said statutes and Statewide Rule 14 for the E.J. Pruitt -E- (01404) Lease, Well No. 18, Pruitt Field, and E.J. Pruitt E5 (13965) Lease, Well Nos. 28, 29, 30, 32 and 49, SE Pruitt (Olmos) Field, Atascosa County, Texas;

3. Whether the respondent should be assessed administrative penalties of not more than \$10,000.00 per day for each offense committed regarding said wells;
4. Whether any violations should be referred to the Office of the Attorney General for further civil action pursuant to Tex. Nat. Res. Code Ann. §81.0534.

Susan German, Staff Attorney, appeared at the hearing representing the Railroad Commission of Texas, Office of General Counsel, Enforcement Section (“Enforcement”). Phil Watkins, President, appeared on behalf of JPW Energy, L.L.C. (“JPW”) and presented evidence at the hearing. Enforcement's hearing file was admitted into evidence.

Enforcement recommended JPW be ordered to properly plug the E.J. Pruitt -E- (01404) Lease, Well No. 18, Pruitt Field, and E.J. Pruitt E5 (13965) Lease, Well Nos. 28, 29, 30, 32 and 49, SE Pruitt (Olmos) Field (hereinafter “Pruitt Leases/Pruitt wells”) and pay a total administrative penalty of \$12,000.00. The administrative penalty is broken down as follows: \$2,000.00 each for six violations of Statewide Rule 14(b)(2). The examiner agrees with the recommended penalty and recommends that JPW be allowed to plug or otherwise bring into compliance with Commission rules the violations of Statewide Rule 14(b)(2).

DISCUSSION OF THE EVIDENCE

Organization and Permit Records

Commission records show that at the time of the hearing, respondent had an active Commission Form P-5 (Organization Report) which was filed with the Commission on October 24, 2007. The Organization Report lists Phil Watkins as JPW's President, Mark Stephen Cichowski as its Vice President, and Brenda M. Wilson as its Treasurer. Commission records show that JPW is recognized as the operator of 25 wells with a total depth of 125,163 feet. JPW submitted a \$50,000 letter of credit as its financial assurance with the most recent Organization Report filing.

JPW was recognized as the operator of the Pruitt Leases after filing Commission Form P-4s (Certificate of Compliance and Transportation Authority) which were approved by the Commission on August 2, 2001.

Commission Inspections

Commission inspections of the E.J. Pruitt -E- (01404) Leases were conducted on August 17, 2006, November 17, 2006, September 21, 2007, and November 15, 2007. These inspection reports

observed that Well No. 18 was inactive, but equipped for production. Commission records further document that the well was not in compliance with Statewide Rule 14(b)(2) after the plugging extension for the well was cancelled effective April 27, 2007 when JPW executed a Release of Oil, Gas and Mineral Lease for all of its Pruitt Leases. The last reported production for the well was in June 2005.

Commission inspections of the E.J. Pruitt E5 (13965) Lease were conducted on June 5, 2006, July 11, 2006, August 1, 2006, November 16, 2006, September 21, 2007, and November 15, 2007. These inspections observed that Well Nos. 28, 29, 30, 32, and 49 were equipped for production or injection but inactive. Commission records further document that the wells were not in compliance with Statewide Rule 14(b)(2) because the plugging extensions for the wells were cancelled effective April 27, 2007 when JPW executed a Release of Oil, Gas and Mineral Lease for all of its Pruitt Leases. The last reported production was in May 2005. Injection activity into Well No. 28 was reported through August 2005. The estimated cost to plug the subject wells is \$72,000.00.

An affidavit from Keith Barton states that the alleged violations pose a threat of pollution and safety. Unplugged wells in violation of Statewide Rule 14(b)(2) are a potential conduit for flows of oil or saltwater to zones of usable quality water or to the surface. Holes or leaks may develop in cased wells, allowing oil or saltwater to communicate with usable quality water zones or to flow to the surface.

Enforcement's Position

Enforcement argues that the Pruitt wells are out of compliance with Statewide Rule 14(b)(2) due to lack of production and the cancellation of the plugging extensions for the failure to submit evidence of a continuing right to operate the wells. Enforcement urges that JPW be ordered to bring the Pruitt wells into compliance with Commission rules, and pay an administrative penalty of \$12,000.00 for the violations.

JPW's Position

JPW acknowledges responsibility for the Pruitt Leases and the violations of Commission Rule 14(b)(2). JPW acquired the Pruitt wells as "stripper" wells. JPW asserts it acted in good faith to maintain the wells in compliance with Commission rules and therefore requests that no administrative penalty be levied against it for the violations.

In April 2003 recurring equipment problems began which were ultimately related to the electrical supply system for the Pruitt wells. Between April 2003 and June 2005 lightning strikes hit 8 pumping units burning out their motors. Because of the unusual number of incidents, JPW hired an electrician who advised that the problems were due to the high voltage of a transformer on the power company supply line which was shorting out equipment during storms. To correct this

problem, JPW purchased a new transformer at a cost of approximately \$16,000.00. JPW was prepared to install the transformer in March 2006 to restore production. However, at that time, the mineral owner advised that the lease had terminated for the lack of production in paying quantities. JPW took the position that it would not install the necessary equipment to restore production until an agreement was reached with the mineral owner.

JPW immediately began negotiations with the mineral owner. A key negotiating point was Pruitt's demand that JPW bring the production levels up to at least 40 bopd for all of the wells operated by JPW on the Pruitt properties.¹ JPW investigated the costs of reworking the wells or drilling new wells to meet this requirement. Negotiations continued through March 2007, but JPW and Pruitt were unable to arrive at an agreement. JPW ultimately executed a release of any rights in the Pruitt Leases on April 26, 2007. Several letters were sent after that date inquiring as to whether Pruitt had entered into a new lease agreement, and further offering to transfer operations.

JPW acknowledges it no longer possesses a right to operate the Pruitt Leases, but requested that it not be ordered to plug the wells as they are capable of production. JPW believed a transfer could be possible within 90 days of the hearing. However, as of the date of the issuance of this proposal for decision no documentation has been provided by JPW seeking to transfer the wells to another operator, or otherwise establishing that a transfer is imminent.

APPLICABLE AUTHORITY

Statewide Rule 14(b)(2) provides that the operator of a well must plug the well in accordance with Commission rules within one year after operations cease, unless an extension is granted. For wells transferred after September 1, 1997, the operator of a well for purposes of plugging liability is shown by an approved Form P-4 designating that person as operator.

EXAMINER'S OPINION

JPW's responsibility for the violations is not contested. JPW urges that it should not be ordered to pay an administrative penalty for the violations as it was engaged in good faith efforts to restore production for the wells which had ceased due to equipment failures. These efforts were fatally compromised when the mineral owner required that the lease agreements be renegotiated and production level raised.

Statewide Rule 14(b)(2) does not require an operator to immediately plug wells after production ceases. An operator initially has 12 months from the last reported production to either plug a nonproducing well or bring it back into production. Additionally, a plugging extension is automatically granted if an operator has a valid organization report and the well or lease is in

¹ JPW is also the operator of record for six wells on the E.J. Pruitt D2 (13964) Lease.

compliance with all other Commission rules. Plugging extensions are also subject to a requirement that the operator provide documentation of a current right to operate when requested by the Commission.

The Pruitt Wells did not require plugging extensions until June 2006 for the producing wells, and August 2006 for the injection well. Plugging extensions were initially granted for the Pruitt wells, but were ultimately cancelled effective April 27, 2007 when JPW executed a Release of Oil, Gas and Mineral Lease for all of its Pruitt Leases.

JPW asserts that it engaged in a good faith attempt to resolve both the equipment failures and legal issues and therefore should not be penalized for violating Statewide Rule 14(b)(2). The testimony and corroborating documentation establishing why production ceased, the attempts to negotiate a resolution with the mineral owner, and the cost of restoring production included significantly more insight and detail of the circumstances surrounding these issues than is established in the typical Enforcement case. However, the time line of events outlined by JPW predates the period during which the wells were out of compliance with Statewide Rule 14(b)(2). There is no evidence in the record that JPW took additional actions after April 27, 2007 to bring the wells into compliance with Commission rules other than inquiries to counsel for Mr. Pruitt which advised that JPW would agree to transfer operations to a new company. Ultimately, while the history which led to the violations is compelling, it does not establish a good faith attempt by JPW to rectify the violations of Statewide Rule 14(b)(2) from the time the plugging extensions were cancelled through the hearing in this docket.

Accordingly, it is recommended that the administrative penalty of \$12,000.00 requested by Enforcement be ordered against JPW for six violations of Statewide Rule 14(b)(2) and that JPW be further ordered to bring the violations into compliance.

The examiner does not recommend that JPW be required to plug the wells as its only method of obtaining compliance with Commission rules. The wells have reported production within the past 3 years. Further, as discussed extensively above, it appears that complications over securing the right to operate the wells, and equipment failure issues are the cause of the cessation of production as opposed to the depletion of reserves.

Based on the record in this docket, the examiner recommends adoption of the following Findings of Fact and Conclusions of Law:

FINDINGS OF FACT

1. Respondent JPW Energy L.L.C., (“JPW”) was given at least 10 days notice of this proceeding by certified mail, addressed to its most recently provided address.

2. JPW has an active Commission Form P-5 (Organization Report) which was filed with the Commission on October 24, 2007. The Organization Report lists Phil Watkins as JPW's President, Mark Stephen Cichowski as its Vice President, and Brenda M. Wilson as its Treasurer. Commission records show that JPW is recognized as the operator of 25 wells with a total depth of 125,163 feet. JPW submitted a \$50,000 letter of credit as its financial assurance with the most recent Organization Report filing.
3. JPW was recognized as the operator of the E.J. Pruitt -E- (01404) Lease and E.J. Pruitt E5 (13965) Lease, Well Nos. 28, 29, 30, 32 and 49 after filing Commission Form P-4s (Certificate of Compliance and Transportation Authority) which were approved by the Commission on August 2, 2001.
4. The E.J. Pruitt -E- (01404) Lease, Well No. 18 is currently inactive, has been inactive for more than 12 months, and has not been properly plugged.
 - a. Commission inspection reports dated on August 17, 2006, November 17, 2006, September 21, 2007, and November 15, 2007 found the well inactive and equipped for production.
 - b. Commission records report no production from the well since July 1, 2005.
5. The E.J. Pruitt E5 (13965) Lease, Well Nos. 29, 30, 32 and 49 are currently inactive, have been inactive for more than 12 months, and have not been properly plugged.
 - a. Commission inspection reports dated on June 5, 2006, July 11, 2006, August 1, 2006, November 16, 2006, September 21, 2007, and November 15, 2007 found the wells inactive and equipped for production.
 - b. Commission records report no production from the wells since June 1, 2005.
6. The E.J. Pruitt E5 (13965) Lease, Well No. 28 is currently inactive, has been inactive for more than 12 months, and has not been properly plugged.
 - a. Commission inspection reports dated on June 5, 2006, July 11, 2006, August 1, 2006, November 16, 2006, September 21, 2007, and November 15, 2007 found the well inactive and equipped for injection.
 - b. Commission records report no injection activity since August 31, 2005.
7. No plugging extensions were in effect for the Pruitt Wells at the time of issuance of the proposal for decision. The plugging extensions were cancelled effective April 27, 2007 when the Commission received a copy of a Release of Oil, Gas and Mineral Lease executed by JPW for all of its Pruitt Leases.
8. Usable quality groundwater in the area may be contaminated by migrations or discharges of

saltwater and other oil and gas wastes from the subject well. Unplugged well bores constitute a cognizable threat to the public health and safety because of the probability of pollution.

CONCLUSIONS OF LAW

1. Proper notice of hearing was timely issued to the appropriate persons entitled to notice.
2. All things necessary to the Commission attaining jurisdiction have occurred.
3. JPW is the operator of the E.J. Pruitt -E- (01404) Lease, Well No. 18, as defined by Statewide Rule 14 and §89.002 of the Texas Natural Resources Code.
4. JPW has the primary responsibility for complying with Rule 14, and Chapter 89 of the Texas Natural Resources Code as well as other applicable statutes and Commission rules relating to the E.J. Pruitt -E- (01404) Lease, Well No. 18.
5. Well No. 18 on the E.J. Pruitt -E- (01404) Lease is not properly plugged or otherwise in compliance with Rule 14 or Chapters 85, 89 and 91 of the Texas Natural Resources Code.
6. Well No. 18 on the E.J. Pruitt -E- (01404) Lease has been out of compliance with Rule 14 from April 27, 2007 to the present.
7. JPW is the operator of the E.J. Pruitt E5 (13965) Lease, Well Nos. 28, 29, 30, 32 and 49, as defined by Statewide Rule 14 and §89.002 of the Texas Natural Resources Code.
8. JPW has the primary responsibility for complying with Rule 14, and Chapter 89 of the Texas Natural Resources Code as well as other applicable statutes and Commission rules relating to the E.J. Pruitt E5 (13965) Lease, Well Nos. 28, 29, 30, 32 and 49.
9. Well Nos. 28, 29, 30, 32 and 49 on the E.J. Pruitt E5 (13965) Lease are not properly plugged or otherwise in compliance with Rule 14 or Chapters 85, 89 and 91 of the Texas Natural Resources Code.
10. Well Nos. 28, 29, 30, 32 and 49 on the E.J. Pruitt E5 (13965) Lease have been out of compliance with Rule 14 from April 27, 2007 to the present.
11. JPW does not possess a current right to operate the E.J. Pruitt -E- (01404) Lease, Well No. 18, or the E.J. Pruitt E5 (13965) Lease, Well Nos. 28, 29, 30, 32 and 49.
12. Phil Watkins, as JPW's President, was in a position of ownership or control of respondent, as defined by Texas Natural Resources Code Section 91.114, during the time period of the violation of Commission Rules committed by respondent.
13. Mark Stephen Cichowski, as JPW's Vice-President, was in a position of ownership or

control of respondent, as defined by Texas Natural Resources Code Section 91.114, during the time period of the violation of Commission Rules committed by respondent.

14. The violations of Commission Rule 14 committed by respondent are related to safety and the control of pollution.
15. As officers in a position of ownership or control of respondent at the time respondent violated Commission rules related to safety and the control of pollution, Phil Watkins, and Mark Stephen Cichowski and any other organization in which they may hold a position of ownership or control, shall be subject to the restrictions of Texas Natural Resources Code Section 91.114(a)(2) for a period of no more than seven years from the date the order entered in this matter becomes final, or sooner, if the conditions that constituted the violations herein are corrected or are being corrected in accordance with a schedule to which the Commission and the organization have agreed; and all administrative, civil, and criminal penalties and all cleanup and plugging costs incurred by the State relating to those conditions are paid or are being paid in accordance with a schedule to which the Commission and the organization have agreed.
16. The documented violations committed by JPW are a hazard to the public health.

RECOMMENDATION

The examiner recommends that the above findings and conclusions be adopted and the attached order approved, requiring JPW Energy, L.L.C., within 30 days of the entry of a Final Order in this matter to:

- 1) plug or otherwise bring Well No. 18 on the E.J. Pruitt -E- (01404) into compliance with Statewide Rule 14;
- 2) plug or otherwise bring Well Nos. 28, 29, 30, 32 and 49 on the E.J. Pruitt E5 (13965) Lease into compliance with Statewide Rule 14 and
- 3) pay an administrative penalty of \$12,000.00.

Respectfully submitted,

Mark Helmueller
Hearings Examiner