

OIL & GAS DOCKET NO. 03-0244983

**ENFORCEMENT ACTION AGAINST NUECES PETROLEUM CORPORATION
(OPERATOR NO. 616055) FOR VIOLATIONS OF STATEWIDE RULES ON THE A.
MERCHANT EST. (09449) LEASE, WELL NOS. 1 AND 2, HULL FIELD, LIBERTY
COUNTY, TEXAS**

APPEARANCES:

FOR MOVANT:

Susan German
Bill Drury

MOVANT:

Enforcement Section
Railroad Commission of Texas

FOR RESPONDENT:

Ken Howard

RESPONDENT:

Nueces Petroleum Corporation

PROPOSAL FOR DECISION

PROCEDURAL HISTORY

DATE OF ORIGINAL COMPLAINT:	December 2, 2005
DATE OF NOTICE OF HEARING:	March 24, 2006
DATE OF HEARING:	June 22, 2006
HEARD BY:	James M. Doherty, Hearings Examiner
DATE RECORD CLOSED:	June 29, 2006
DATE PFD CIRCULATED:	July 24, 2006

STATEMENT OF THE CASE

This proceeding was called by the Commission on the recommendation of the District Office to determine the following:

1. Whether the respondent Nueces Petroleum Corporation (“Nueces”) should be required to plug or otherwise place in compliance with Statewide Rule 14(b)(2) [Tex. R.R. Comm’n., 16 TEX. ADMIN. CODE §3.14(b)(2)] the A. Merchant Est. (09449) Lease (“subject lease”), Well Nos. 1 and 2 (“subject wells”), Hull Field, Liberty County, Texas;

2. Whether Nueces has violated Statewide Rule 3 [Tex. R.R. Comm'n., 16 TEX. ADMIN. CODE §3.3] on the A. Merchant Est. (09449) Lease by failing to post identification signs at Well Nos. 1 and 2;
3. Whether Nueces has 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 plug the subject wells or otherwise place the subject lease and wells in compliance with Statewide Rules 3 and 14(b)(2);
4. Whether, pursuant to Texas Natural Resources Code §81.0531, Nueces should be assessed administrative penalties of not more than \$10,000 per day for each offense committed regarding the subject lease and wells; and
5. Whether any violations of Statewide Rules 3 and 14(b)(2) by Nueces should be referred to the Office of the Attorney General for further civil action pursuant to Texas Natural Resources Code §81.0534.

A hearing was held on June 22, 2006. Susan German, Staff Attorney, appeared representing the Enforcement Section of the Office of General Counsel ("Enforcement"). Ken Howard, consultant, appeared to represent Nueces and presented evidence. Enforcement's certified hearing file was admitted into evidence. The record was held open until June 29, 2006, to receive information as to whether any bankruptcy trustee had been appointed in a pending Chapter 11 bankruptcy proceeding wherein Nueces is the debtor and the effect of the pending bankruptcy proceeding on this docket.

APPLICABLE LAW

Statewide Rule 3(2) requires that an identification sign be posted at each well site, showing the name of the property, the name of the operator, and the well number. Statewide Rule 14(b)(2) requires that a well be plugged after 12 months of inactivity, unless a plugging extension has been obtained.

DISCUSSION OF THE EVIDENCE

Matters Officially Noticed

The examiner has officially noticed Commission organization report and financial assurance databases showing that Nueces has an active Form P-5 organization report and financial assurance in the amount of \$50,000 in the form of a letter of credit.

Enforcement

The most recent Form P-5 organization report shows that Nueces is a corporation. Nueces' officers listed on this Form P-5 are Lee Lance, President, and Jamie Lloyd, Vice President, Operations. Nueces designated itself operator of the subject lease and wells by filing a Form P-4 (Certificate of Compliance and Transportation Authority), which was approved March 27, 2002, effective March 1, 2002.

On the occasion of 5 District Office inspections between May 18, 2005, and May 31, 2006, the identification signs required by Statewide Rule 3 to be posted at the site of Well Nos. 1 and 2 on the subject lease were missing. Five District Office inspections of the subject lease made between May 18, 2005, and May 31, 2006, disclosed that Well Nos. 1 and 2 were inactive. Production from the subject lease was last reported to the Commission in November 2003. No Plugging Record (Form W-3) or Cementing Affidavit (Form W-15) has been filed or approved for the subject wells, and no plugging extensions for the wells are in effect.

A plugging extension for Well No. 1 expired on December 31, 2005, and a plugging extension for Well No. 2 was canceled on January 12, 2005. The estimated cost to the State to plug the subject wells is \$32,947. On five occasions between May 25, 2005, and October 4, 2005, the District Office sent Nueces correspondence, notices, or copies of memoranda requesting voluntary compliance with Statewide Rules 3 and/or 14(b)(2) on the subject lease.

In the event of a pollution or safety violation or other emergency, incorrect, illegible or missing signs may cause delays in containing and remediating the violation or emergency and threaten the public health and safety.

Inactive wellbores must be plugged in order to prevent pollution of usable quality surface and subsurface waters. Any wellbore, cased or otherwise, is a potential conduit for flow from oil or saltwater zones 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. Uncased wells allow direct communication between zones and provide unimpeded access to the surface.

Nueces

Nueces does not dispute any of Enforcement's allegations. However, Nueces currently is the debtor in possession in a Chapter 11 reorganization proceeding, styled Case No. 05-44617, *In Re:*

Nueces Petroleum Corporation, Debtor, in the United States Bankruptcy Court for the Southern District of Texas, Houston Division.¹ According to its consultant, Nueces may be required to bring the wells into compliance under supervision of the Bankruptcy Court.

EXAMINER'S OPINION

The violations of Statewide Rules 3 and 14(b)(2) alleged by Enforcement are not disputed by Nueces and are clearly proved by the evidence.

The pendency of Nueces' Chapter 11 bankruptcy proceeding does not prohibit the prosecution of this action to enforce Commission rules related to safety and the prevention or control of pollution. Such actions by a governmental unit are exempted from the automatic stay provisions of 11 U.S.C. §362(a). *See* 11 U.S.C. §362(b)(4). Where there is a pending bankruptcy proceeding, the Commission may order compliance with its safety and environmental regulations, and fix the amount of suitable penalties for violations of its rules related to safety and the prevention or control of pollution, but may not order payment of penalties. *In Re: Commonwealth Oil Ref. Co.*, 805 F.2d 1175 (5th Cir. 1986), cert. denied, 483 U.S. 1005 (1987).

Enforcement recommends that the penalty for Nueces' violations of Statewide Rules 3 and 14(b)(2) be fixed at \$4,500, consisting of two violations of Statewide Rule 3 at \$250 each and two violations of Statewide Rule 14(b)(2) at \$2,000 each. The examiner agrees with this recommendation. These penalties conform to standard penalties in the recommended standard penalty schedule for enforcement cases. Violations of Statewide Rules 3 and 14(b)(2) present a threat to public safety and a threat of pollution of usable quality water. Such violations are thus deemed serious. According to Enforcement's complaint, no prior final Commission orders have been entered against Nueces for violations of Commission rules. However, Nueces cannot be said to have acted in good faith, because it failed to respond to multiple requests from the District Office for voluntary compliance.

The examiner also recommends that Nueces be ordered to plug the subject wells or otherwise bring the wells into compliance with Statewide Rules 3 and 14(b)(2).

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

¹ The examiner has officially noticed that Nueces' bankruptcy petition was filed on September 9, 2005. Nueces is a debtor in possession, and no bankruptcy trustee has been appointed. It does not appear that the Commission previously was notified of this bankruptcy proceeding. On June 26, 2006, Enforcement filed copies of Nueces' Plan of Reorganization and Disclosure Statement in the bankruptcy case, and these documents were admitted into evidence. The Disclosure Statement stated that Earnest Frank Hill, Jr. (aka E. Frank Hill, Jr.) was Nueces' "initial Director" and "directs the over all corporate strategy." The Disclosure Statement stated also that Earnest Frank Hill, Jr., makes all final decisions for Nueces. The Disclosure Statement stated also that Frank Hill is the owner of 1,000 shares of stock (voting rights only) of Nueces, and no other owners were named.

FINDINGS OF FACT

1. Nueces Petroleum Corporation (“Nueces”) was given at least ten (10) days notice of this hearing by certified mail, addressed to Nueces’ most recent Form P-5 organization report address. Ken Howard, consultant for Nueces, appeared at the hearing representing Nueces and presented evidence.
2. Nueces is a corporation. Its officers, as listed on its most recent Form P-5 organization report approved April 7, 2006, are Lee Lance, President, and Jamie Lloyd, Vice President. Earnest Frank Hill, Jr. (aka E. Frank Hill, Jr.) was Nueces’ initial director and directs overall corporate strategy and makes all final decisions for the company.
3. As officers, Lee Lance and Jamie Lloyd were persons in a position of ownership or control of Nueces at the time the violations involved in this docket were committed. As a director and the person directing overall corporate strategy and making all final decisions, Earnest Frank Hill, Jr. (aka E. Frank Hill, Jr.) was a person in a position of ownership or control of Nueces at the time the violations involved in this docket were committed.
4. The violations involved in this docket were violations of Commission rules related to safety and the prevention or control of pollution.
5. Nueces’ Form P-5 organization report is in active status, and Nueces has filed financial assurance in the amount of \$50,000 in the form of a letter of credit.
6. As the result of petition filed on September 9, 2005, Nueces was, at the time of the hearing in this docket, the debtor in possession in a pending Chapter 11 reorganization proceeding styled Case No. 05-44617, *In Re: Nueces Petroleum Corporation, Debtor*, in the United States Bankruptcy Court for the Southern District of Texas, Houston Division.
7. Nueces designated itself to the Commission as the operator of the A. Merchant Est. (09449) Lease (“subject lease”), Well Nos. 1 and 2 (“subject wells”), Hull Field, Liberty County, Texas, by filing Form P-4, approved March 27, 2002, effective March 1, 2002.
8. On the occasion of 5 District Office inspections between May 18, 2005, and May 31, 2006, the identification signs required by Statewide Rule 3 to be posted at the sites of the subject wells were missing.
9. The subject wells have been inactive for more than one year, have not been plugged, and do not have Statewide Rule 14(b)(2) plugging extensions.
 - a. On the occasion of 5 District Office inspections between May 18, 2005, and May 31, 2006, the subject wells were inactive.
 - b. No production has been reported to the Commission for the subject wells since November 2003.

- c. No Plugging Record (Form W-3) or Cementing Affidavit (Form W-15) has been filed or approved for the subject wells.
 - d. A plugging extension for Well No. 1 expired on December 31, 2005, and a plugging extension for Well No. 2 was canceled on January 12, 2005.
10. The estimated cost to the State to plug the subject wells is \$32,947.
 11. On five occasions between May 25, 2005, and October 4, 2005, the District Office sent Nueces correspondence, notices, or copies of memoranda requesting voluntary compliance with Statewide Rules 3 and/or 14(b)(2) on the subject lease. Nueces did not respond by placing the subject lease and wells into compliance.
 12. In the event of a pollution or safety violation or other emergency, incorrect, illegible or missing signs may cause delays in containing and remediating the violation or emergency and threaten the public health and safety.
 13. Inactive wellbores must be plugged in order to prevent pollution of usable quality surface and subsurface waters. Any wellbore, cased or otherwise, is a potential conduit for flow from oil or saltwater zones 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. Uncased wells allow direct communication between zones and provide unimpeded access to the surface.
 14. No evidence was presented that prior final enforcement orders have been entered against Nueces for violation of Commission rules.
 15. Nueces has not demonstrated good faith in that it failed to respond to multiple requests from the District Office to resolve the violations that are the subject of this docket.

CONCLUSIONS OF LAW

1. Proper notice of hearing was timely issued to appropriate persons entitled to notice.
2. All things necessary to the Commission attaining jurisdiction have occurred.
3. Nueces Petroleum Corporation (“Nueces”) was and is the operator of the A. Merchant Est. (09449) Lease (“subject lease”), Well Nos. 1 and 2 (“subject wells”), Hull Field, Liberty County, Texas, as defined by Commission Statewide Rules 14, 58 and 79 [Tex. R.R. Comm’n., 16 TEX. ADMIN. CODE §3.14, 3.58, and 3.79] and Chapters 85 and 89 of the Texas Natural Resources Code.
4. As operator, Nueces had the primary responsibility for complying with Statewide Rules 3 and 14(b)(2) [Tex. R.R. Comm’n., 16 TEX. ADMIN. CODE §§3.3 and 3.14(b)(2)], Chapters 89 and 91 of the Texas Natural Resources Code, and other applicable statutes and Commission rules respecting the subject lease and wells.

5. Nueces violated Statewide Rule 3 [Tex. R.R. Comm'n., 16 TEX. ADMIN. CODE §§3.3] on the subject lease by failing to post and maintain the required identification signs at the sites of the subject wells. Nueces has been out of compliance with Statewide Rule 3 since at least May 18, 2005.
6. Nueces violated Statewide Rule 14(b)(2) [Tex. R.R. Comm'n., 16 TEX. ADMIN. CODE §§3.14(b)(2)] by failing to timely plug the subject wells. Nueces has been out of compliance with Statewide Rule 14(b)(2) since at least December 31, 2005, with respect to Well No. 1 and since January 12, 2005, with respect to Well No. 2.
7. The documented violations committed by Nueces constitute acts deemed serious and a hazard to the public health, and demonstrate a lack of good faith within the meaning of Texas Natural Resources Code §81.0531.
8. This is an enforcement action by a governmental unit to enforce its rules related to safety and the prevention or control of pollution, and, pursuant to 11 U.S.C. §362(b)(4) is exempted from the automatic stay provisions of 11 U.S.C. §362(a).
9. As officers of Nueces at the time Nueces violated Commission rules related to safety and the prevention or control of pollution, Lee Lance and Jamie Lloyd, and any organization in which they, or either of them, may hold a position of ownership or control, are subject to the restrictions of Texas Natural Resources Code §91.114(a)(2).
10. As a director of Nueces and the person directing overall corporate strategy and making all final decisions for Nueces at the time Nueces violated Commission rules related to safety and the prevention or control of pollution, Earnest Frank Hill, Jr. (aka E. Frank Hill, Jr.), and any organization in which he may hold a position of ownership or control, are subject to the restrictions of Texas Natural Resources Code §91.114(a)(2).

RECOMMENDATION

The examiner recommends that the Commission adopt the attached final order providing: (1) that Nueces Petroleum Corporation shall plug or otherwise place into compliance with Commission rules the A. Merchant Est. (09449) Lease, Well Nos. 1 and 2, Hull Field, Liberty County, Texas; and (2) that an administrative penalty in the amount of \$4,500 is assessed against Nueces Petroleum Corporation.

Respectfully submitted,

James M. Doherty
Hearings Examiner