

OIL & GAS DOCKET NO. 03-0251480

**ENFORCEMENT ACTION AGAINST STERLING EXPL. & PROD. CO., LLC¹
(OPERATOR NO. 819006) FOR VIOLATIONS OF STATEWIDE RULES ON THE STATE
TRACT 194 LEASE, WELL NO. 5 (RRC NO. 109886), MATAGORDA BAY, NE (MIOCENE
1400) FIELD, MATAGORDA COUNTY, TEXAS**

APPEARANCES:

FOR MOVANT:

Reese Copeland

MOVANT:

Enforcement Section
Railroad Commission of Texas

FOR RESPONDENT:

Richard F. Bergner
Robert Charles Cheatham

RESPONDENT:

Sterling Expl. & Prod. Co., LLC

PROPOSAL FOR DECISION

PROCEDURAL HISTORY

DATE COMPLAINT FILED:	May 9, 2007
DATE OF NOTICE OF HEARING:	June 1, 2007
DATE OF HEARING:	July 19, 2007
HEARD BY:	James M. Doherty, Hearings Examiner
DATE RECORD CLOSED:	July 30, 2007
DATE PFD CIRCULATED:	August 28, 2007

STATEMENT OF THE CASE

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

¹ According to the P-5 Master Inquiry Remarks Inquiry database, respondent's full name as reflected by records of the Secretary of State is Sterling Exploration & Production Co., L.L.C. For organizational purposes, the name was shortened to conform to Commission technological constraints.

1. Whether the respondent Sterling Expl. & Prod. Co., LLC (“Sterling”) 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 State Tract 194 Lease, Well No. 5 (RRC No. 109886) (“subject well”), Matagorda Bay, NE (Miocene 1400) Field, Matagorda County, Texas;
2. Whether Sterling violated Statewide Rule 14(b)(3) [Tex. R.R. Comm’n, 16 TEX. ADMIN. CODE §3.14(b)(3)] by failing to perform an approved H-15 test (Test on an Inactive Well More than 25 Years Old) on the State Tract 194 Lease, Well No. 5 (RRC No. 109886), Matagorda Bay, NE (Miocene 1400) Field, Matagorda County, Texas;
3. Whether Sterling 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 well or otherwise place the well into compliance with Statewide Rules 14(b)(2) and 14(b)(3);
4. Whether, pursuant to Texas Natural Resources Code §81.0531, Sterling should be assessed administrative penalties of not more than \$10,000 per day for each offense committed regarding the subject well; and
5. Whether any violations of Statewide Rules 14(b)(2) and 14(b)(3) by Sterling 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 July 19, 2007. Reese Copeland, Staff Attorney, appeared representing the Enforcement Section of the Office of General Counsel (“Enforcement”). Richard F. Bergner, attorney, and Robert Charles Cheatham appeared representing Sterling and presented evidence. Enforcement’s certified hearing file was admitted into evidence. The record was held open until July 30, 2007, to allow the parties time to file certain late-filed exhibits relating to the issue of why a mechanical integrity test allegedly performed on the subject well by Sterling on November 4, 2005, was not approved by the Commission.

APPLICABLE LAW

Statewide Rule 14(b)(2) requires that a well be plugged after 12 months of inactivity, unless a plugging extension has been obtained. A plugging extension will be approved for a well only if the well is in compliance with all Commission rules and the operator has a good faith claim of right to operate the well.

Statewide Rule 14(b)(3) provides that the operator of any well more than 25 years old that becomes inactive shall plug or test such well to determine whether the well poses a potential threat of harm to natural resources, including surface and subsurface water, oil and gas.

DISCUSSION OF THE EVIDENCE

Matters Officially Noticed

The examiner has officially noticed from the Commission's Master Inquiry database that the Form P-5 organization report of Sterling was due to be renewed on July 1, 2007, and was delinquent on the date of the hearing.² The examiner has also officially noticed from the On-Schedule Leases, Wells, Wellbores by Operator and the On-Schedule Wells by Lease databases that the State Tract 194 Lease, Well No. 5 (RRC No. 109886) is coded as a "Bay/Estuary" well. The Location Data database identifies the survey for this well as "Matagorda Bay, State Tract 194." Official notice has also been taken of the Permit Numbers and Wells Within Well Bore database, which shows that the subject wellbore initially was completed on September 7, 1978, and the 14(b)(2) Well History Inquiry database, which shows that a plugging extension for the subject well was denied on September 11, 2006, based on a H-15 test that was not approved.

Enforcement

The Form P-5 organization report of Sterling shows that Sterling is a limited liability company, its sole manager is Matagorda Operating Company ("Matagorda"), and Robert Charles Cheatham ("Cheatham") is President and Secretary of Matagorda. At the hearing, Cheatham testified that he had named himself "CEO" of Sterling and that he is the owner of Sterling and Matagorda.

Sterling designated itself operator of the State Tract 194 Lease, Well No. 5 (RRC No. 109886) by filing a Form P-4 (Certificate of Compliance and Transportation Authority) approved October 20, 2003, effective October 1, 2003. No production reports have been filed with the Commission for this well since November 2001, and production reports for the period March 1996 through October 2001 reported zero production for the well. The last reported production for the subject well was in February 1996. The well does not have a Statewide Rule 14(b)(2) plugging extension. The Commission's estimate of the cost to the State to plug the well is \$250,000.

The subject wellbore initially was completed on September 7, 1978, and is more than 28 years old. A required H-15 test (Test on an Inactive Well More than 25 Years Old) for the well was due in May 2005, and no approved test has been performed since that date. Sterling filed a Form H-15 reporting that a mechanical integrity test of the well was performed on November 4, 2005, but this Form H-15 was not approved because the District Office was not notified of the alleged test, and the test was not witnessed by a representative of the Commission.

² Robert Charles Cheatham testified at the hearing that Sterling's Form P-5 renewal was awaiting transfer of 19 offshore wellbores from Sterling to Jefferson Block 24 Oil & Gas, LLC. The transfer of these wells from Sterling to Jefferson was approved by the Commission on July 19, 2007, the same day as the hearing in this docket. Sterling's Form P-5 remained delinquent as of August 27, 2007.

The subject well was severed by the Commission on August 5, 2005, based on a delinquent H-15 test, on February 21, 2006, based on a H-15 test that was not approved, on August 16, 2006, based on Form P-5 delinquency, and on December 12, 2006, based on a Rule 14(b)(2) violation, and the certificate of compliance for the well has not been re-issued.

On five occasions between October 3, 2006, and March 23, 2007, the District Office sent Sterling correspondence, notices, or copies of memoranda requesting Sterling's voluntary compliance with Rule 14(b)(2) with respect to the subject well, and Sterling has not achieved such compliance. On October 18, 2006, Sterling sent the District Office correspondence stating Sterling's intention to restore the well to production by workover during the last quarter of 2006. The well has not been worked over or restored to production, and, according to a certification of the Commission's Secretary, no Plugging Record (Form W-3) or Cementing Affidavit (Form W-15) has been filed or approved for the well.

An affidavit of Ramon Fernandez, P.E., Field Operations, stated that a well that is in violation of Statewide Rule 14, by having been inactive for one year, must be plugged in accordance with the technical requirements of Statewide Rule 14 in order to prevent pollution of usable quality surface or 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.

The Fernandez affidavit stated also that any inactive well that is greater than 25 years of age must be plugged or tested to determine whether the well poses a potential threat of harm to natural resources, including surface and subsurface water, oil and gas. Casing leaks and/or fluid levels above the base of usable quality water indicate a possible pollution hazard. Without the required test and supporting documentation (Form H-15), the Commission cannot determine if the well poses a threat to natural resources.

Enforcement recommended that a penalty be assessed against Sterling in the amount of \$12,000, comprised of one "bay well" violation of Rule 14(b)(2) at \$10,000 and one violation of Rule 14(b)(3) at \$2,000.

Sterling

Robert Charles Cheatham testified that Sterling acquired the subject well from Main Energy, Inc., in 2003. Main had intended to plug the well, but Cheatham believed the well could be produced. Cheatham claimed that Sterling performed a H-15 test on the subject well on September 8, 2004, and again on November 5, 2005, under the supervision of a former officer of Sterling who has now left the company. Although not professing to have personal knowledge of the facts surrounding the test allegedly performed in November 2005, Cheatham stated that company procedure dictated that the District Office be notified when Sterling had scheduled a H-15 test. According to Cheatham, there have been situations where the District Office was notified of scheduled tests of bay or offshore wells, and the District Office chose not to witness the test. However, Cheatham had not examined the well file to see if it contained any documentation of notification to the District Office of the alleged test in November 2005.³

Cheatham testified further that Sterling's business affairs had been in a state of confusion as a result of personnel who left the company last year and during the first quarter of 2007 and his own hospitalization and rehab during 2007. However, he claimed that the former personnel have now been replaced, and Sterling is back to "full steam." According to Cheatham, the subject well needs to be plugged because reworking the well would not be economical. He stated that Sterling expects to plug the well within the next two months, when plugging equipment can be lined up to do the job. Cheatham took issue with the Commission's estimate of the cost to plug the well, and estimated that the well can be plugged for a cost of \$100,000.

Cheatham claimed that when a H-15 test of the subject well was performed in November 2005, Sterling believed it had done everything that was required, and requested that no punitive action be taken against Sterling.

EXAMINER'S OPINION

The subject well has been inactive for more than 11 years and has been without a plugging extension since at least September 11, 2006. Enforcement proved that the well required a H-15 test as of May 2005, and no approved test has been performed since that date. Statewide Rule 14(b)(3)(A) and (B) require that notification be given by the operator to the District Office at least 48 hours before a mechanical integrity test is conducted so that the test can be witnessed by District Office personnel. The Form H-15 filed by Sterling purporting to report the results of a mechanical

³ The record was held open until July 30, 2007, to permit the parties to file copies of records relating to the reason for District Office disapproval of the Form H-15 filed by Sterling and the issue of whether Sterling provided notification to the District Office prior to the H-15 test. Enforcement submitted copies of official records of the District Office reflecting that the Form H-15 was disapproved based on "No Notification" and a copy of a February 1, 2006, facsimile transmission from Sterling to the District Office stating that Sterling inadvertently failed to provide notification of the H-15 test to the District Office. Sterling submitted copies of certain of its business records relating to the H-15 test confirming that no notification was provided.

integrity test of the subject well on November 4, 2005, could not be approved because no notification was provided to the District Office that the test was scheduled and the test was not witnessed. Sterling's professed ignorance of the fact that the Form H-15 relating to the test on November 4, 2005, was not approved, and the claim that Sterling believed that it had done all that was required to achieve compliance, are not credible. A plugging extension was denied for the subject well on September 11, 2006, based on the delinquent H-15 status of the well. A notice of severance was issued to Sterling on December 5, 2006, severing the subject well because of the non-approved H-15 test, and a further notice of severance was issued on March 23, 2007, because the well was in violation of Rule 14(b)(2). Furthermore, written communications from the District Office to Sterling on October 3 and December 5, 2006, and March 23, 2007, notified Sterling that the well was non-compliant with Rule 14(b)(2). It is not plausible that Sterling believed that it had done all that was required to achieve compliance.

The evidence shows that the subject well is more than 25 years old, has been inactive for more than one year, has not had an approved H-15 test, does not have a plugging extension, and has not been plugged. Accordingly, violations by Sterling of Statewide Rules 14(b)(2) and 14(b)(3) have been established. The remaining issues are: (1) the amount of administrative penalties that should be imposed; and (2) the nature of compliance that should be ordered.

In determining the amount of the penalty to be imposed against Sterling, the Commission is required by Texas Natural Resources Code §81.0531 to consider the operator's previous violations, the seriousness of the violations, any hazard to the health or safety of the public, and the demonstrated good faith of the person charged. According to Enforcement's complaint in this docket, Sterling has no history of prior final enforcement orders entered against it for violations of Commission rules. On the other hand, the involved violations are serious, and present a hazard to the health and safety of the public, because of the threat of pollution of usable quality water presented by inactive, untested, and unplugged wellbores.

Sterling cannot be said to have acted in good faith because it failed to achieve voluntary compliance in response to multiple requests from the District Office. The penalties recommended by Enforcement, based on one "bay well" violation of Rule 14(b)(2) at \$10,000, and one violation of Rule 14(b)(3) at \$2,000, are the standard penalties provided by the recommended standard penalty schedule for enforcement cases. Accordingly, Enforcement's penalty recommendation is adopted by the examiner.

The examiner also recommends adoption of an order requiring that the subject well be plugged. This well is more than 28 years old and has been inactive for more than 11 years. Sterling has been the operator of the well since 2003 and has never produced the well. According to Mr. Cheatham's testimony at the hearing, Main Energy, Inc., had made the decision to plug the well prior to the 2003 transfer to Sterling, and Sterling now concedes that the well needs to be plugged because it would not be economical to rework the well in an attempt to restore it to production.

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

FINDINGS OF FACT

1. Sterling Expl. & Prod. Co., LLC (“Sterling”) (Operator No. 819006) was given at least ten (10) days notice of this hearing by certified mail addressed to Sterling’s most recent Form P-5 organization report address. Sterling appeared at the hearing and presented evidence.
2. Sterling is a limited liability company. Its sole manager is Matagorda Operating Company (“Matagorda”), and Robert Charles Cheatham is President and Secretary of Matagorda. Robert Charles Cheatham is also the owner of Matagorda and Sterling.
3. Robert Charles Cheatham was a person in a position of ownership and control of Sterling 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. Sterling’s Form P-5 organization report was due for renewal on July 1, 2007, and at the time of the hearing was delinquent.
6. Sterling designated itself operator of the State Tract 194 Lease, Well No. 5 (RRC No. 109886) (“subject well”), Matagorda Bay, NE (Miocene 1400) Field, Matagorda County, Texas, by filing a Form P-4 (Certificate of Compliance and Transportation Authority) approved October 20, 2003, effective October 1, 2003.
7. The subject well is in Matagorda Bay and is classified by the Commission as a bay well.
8. The subject well has been inactive for more than twelve months, does not have a Statewide Rule 14(b)(2) plugging extension, and has not been plugged.
 - a. No production reports have been filed with the Commission for this well since November 2001, and production reports for the period March 1996 through October 2001 reported zero production for the well. The last reported production for the subject well was in February 1996.
 - b. A Statewide Rule 14(b)(2) plugging extension for the subject well was denied on September 11, 2006, based on a H-15 test that was not approved.
 - c. No Plugging Record (Form W-3) or Cementing Affidavit (Form W-15) has been filed or approved for the well.

9. The subject wellbore initially was completed on September 7, 1978, and is a wellbore more than 25 years old subject to the testing requirements of Statewide Rule 14(b)(3). A required H-15 test for the wellbore was due in May 2005, and no approved test has been performed since that date. A Form H-15 filed by Sterling reporting a mechanical integrity test of the well on November 4, 2005, was not approved because Sterling did not provide notification to the District Office that the test was scheduled and the test was not witnessed by District Office personnel.
10. On five occasions between October 3, 2006, and March 23, 2007, the District Office sent Sterling correspondence, notices, or copies of memoranda requesting Sterling's voluntary compliance with Rule 14(b)(2) with respect to the subject well, and Sterling has not achieved such compliance.
11. A well that is in violation of Statewide Rule 14, by having been inactive for one year, must be plugged in order to prevent pollution of usable quality surface or 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.
12. Any well that is greater than 25 years old must be plugged or tested to determine whether the well poses a potential threat of harm to natural resources, including surface and subsurface water, oil and gas. Casing leaks and/or fluid levels above the base of usable quality water indicate a possible pollution hazard.
13. No prior final enforcement orders have been entered against Sterling for violations of Commission rules.
14. Sterling has not demonstrated good faith because it did not achieve voluntary compliance with Statewide Rules 14(b)(2) and 14(b)(3) in response to multiple requests by the District Office for such compliance.

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. Sterling Expl. & Prod. Co., LLC (“Sterling”) (Operator No. 819006) was and is the operator of the State Tract 194 Lease, Well No. 5 (RRC No. 109886) (“subject well”), Matagorda Bay, NE (Miocene 1400) Field, Matagorda County, Texas, as defined by 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, Sterling had the primary responsibility for complying with Statewide Rules 14(b)(2) and 14(b)(3) [Tex. R.R. Comm’n, 16 TEX. ADMIN. CODE §§3.14(b)(2) and 3.14(b)(3)], Chapters 89 and 91 of the Texas Natural Resources Code, and other applicable statutes and Commission rules respecting the subject well.
5. Sterling violated Statewide Rule 14(b)(2) by failing to plug the subject well within one year after operations ceased and by failing otherwise to bring the well into compliance with Statewide Rule 14(b)(2). The subject well has been out of compliance with Statewide Rule 14(b)(2) since at least September 11, 2006.
6. Sterling violated Statewide Rule 14(b)(3) with respect to the subject well by failing to conduct an approved H-15 test (Test on an Inactive Well More than 25 Years Old) on the well. The well has been out of compliance with Statewide Rule 14(b)(3) since at least May 2005.
7. The documented violations committed by Sterling constitute acts deemed serious and a hazard to the public health and safety within the meaning of Texas Natural Resources Code §81.0531.
8. Sterling did not demonstrate good faith within the meaning of Texas Natural Resources Code §81.0531.
9. As a person in a position of ownership and control of Sterling at the time Sterling violated Commission rules related to safety and the prevention or control of pollution, Robert Charles Cheatham, and any organization subject to the Commission’s jurisdiction 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 Sterling be ordered to pay an administrative penalty in the amount of \$12,000. The examiner recommends further that Sterling be ordered to plug the State Tract 194 Lease, Well No. 5 (RRC No. 109886), Matagorda Bay, NE (Miocene 1400) Field, Matagorda County, Texas.

Respectfully submitted,

James M. Doherty
Hearings Examiner