

OIL & GAS DOCKET NO. 09-0246039

ENFORCEMENT ACTION AGAINST ROY FARRELL, JR. DBA FARRELL OIL COMPANY (OPERATOR NO. 263474) FOR VIOLATIONS OF STATEWIDE RULES ON THE KYLE (29558) LEASE, WELL NO. 3 AND TANK BATTERY, KYLE (CANYON CHARGED 4200) FIELD, HARDEMAN COUNTY, TEXAS

APPEARANCES:

FOR MOVANT:

Susan German
Bill Drury

MOVANT:

Enforcement Section
Railroad Commission of Texas

FOR RESPONDENT:

Rex H. White, Jr.
Roy Farrell, Jr.

RESPONDENT

Roy Farrell, Jr.
DBA Farrell Oil Company

PROPOSAL FOR DECISION

PROCEDURAL HISTORY

DATE OF ORIGINAL COMPLAINT:

February 8, 2006

DATE OF NOTICE OF HEARING:

July 21, 2006

DATE OF HEARING:

September 14, 2006

HEARD BY:

James M. Doherty, Hearings
Examiner

DATE RECORD CLOSED:

October 16, 2006

DATE PFD CIRCULATED:

November 13, 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 Roy Farrell, Jr. DBA Farrell Oil Company ("Farrell") 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 Kyle (29558) Lease, Well No. 3, Kyle (Canyon Charged 4200) Field, Hardeman County, Texas;

2. Whether Farrell has violated Statewide Rule 3 [Tex. R.R. Comm'n, 16 TEX. ADMIN. CODE §3.3] on the Kyle (29558) Lease by failing to post identification signs at the lease entrance and tank battery;
3. Whether Farrell has violated Statewide Rule 46(g)(2) [Tex. R.R. Comm'n, 16 TEX. ADMIN. CODE §3.46(g)(2)] on the Kyle (29558) Lease by failing to maintain an operable pressure observation valve on the tubing of Well No. 3;
4. Whether Farrell 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 failing to place the subject lease and well into compliance with Statewide Rules 3, 14, and 46;
6. Whether, pursuant to Texas Natural Resources Code §81.0531, Farrell should be assessed administrative penalties of not more than \$10,000 per day for each offense committed regarding the subject lease and well; and
7. Whether any violations of Statewide Rules 3, 14, and 46 by Farrell 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 September 14, 2006. Susan German, Staff Attorney, appeared representing the Enforcement Section of the Office of General Counsel ("Enforcement"). Rex H. White, Jr., attorney, and Roy Farrell, Jr. appeared to represent Farrell and presented evidence. Enforcement's certified hearing file was admitted into evidence. The record of the hearing was held open until October 16, 2006, at Farrell's request, to permit Farrell an opportunity to late-file exhibits demonstrating, as pertinent to this docket, that: (1) Farrell had renewed his Form P-5 organization report and filed the required financial assurance; (2) Farrell had filed and obtained approval of a Form W-3A (Notice of Intention to Plug and Abandon) for the Kyle (29558) Lease, Well No. 3; and (3) Farrell had entered into a plugging contract for the plugging of the Kyle (29558) Lease, Well No. 3.

APPLICABLE LAW

Statewide Rule 3(1) requires that an identification sign be posted at lease entrances, showing the name of the property, the name of the operator, and the number of acres in the property. Statewide Rule 3(2) requires that an identification sign be posted at tank batteries, showing the name of the property, the name of the operator, the Commission lease number for the formation from

which oil in the tank is produced, and where oil from more than one formation is commingled in the same tank, the number of the Commission permit that authorized the commingling of the oil.

Statewide Rule 14(b)(2) requires that a well be plugged after 12 months of inactivity, unless a plugging extension has been obtained.

Statewide Rule 46(g)(2) provides that for any fluid injection well, the wellhead shall be equipped with a pressure observation valve on the tubing and for each annulus of the well.

DISCUSSION OF THE EVIDENCE

Matters Officially Noticed

The examiner has officially noticed Commission organization report and financial assurance databases showing that the Form P-5 organization report of Farrell, which had been delinquent since July 1, 2002, was renewed on October 23, 2006, and that Farrell has on file with the Commission financial assurance in the amount of \$50,000 in the form of a letter of credit. The examiner has also officially noticed the Commission's On-Schedule Leases, Wells, Wellbores by Operator database establishing that Farrell is the operator of a total of seven wellbores. The examiner has further officially noticed the Commission's 14(b)(2) Well Inquiry by Application database establishing that the well involved in this docket has a plugging extension effective October 23, 2006. The examiner has also officially noticed a posthearing District Office inspection report for the subject lease dated October 5, 2006.

Enforcement

The most recent Form P-5 shows that Farrell is a sole proprietorship, and Roy Farrell, Jr. is owner. Farrell designated himself operator of the subject lease by filing Form P-4 (Certificate of Compliance and Transportation Authority), which was approved and effective on August 1, 1998.

On the occasion of four District Office inspections on September 26, 2005, October 13, 2005, March 22, 2006, and August 25, 2006 (hereinafter referred to as "the District Office inspections"), the identification signs required by Statewide Rule 3 to be posted at the lease entrance and tank battery on the subject lease were missing. A further District Office inspection on October 5, 2006, disclosed that the required sign had been posted at the lease entrance but not at the tank battery.

Well No. 3 on the subject lease was permitted as a saltwater disposal well by Permit No. 15334 dated June 12, 1998. The District Office inspections disclosed that the subject well was inactive. No injection activity for the well was reported to the Commission after December 31, 2001. No Plugging Record (Form W-3) or Cementing Affidavit (Form W-15) has been filed or approved for the well. The estimated cost to the State to plug the Kyle (29558) Lease, Well No. 3 is \$23,600.

The District Office inspections also disclosed that Well No. 3 on the Kyle (29558) Lease was equipped with tubing and casing, and the pressure observation valve on the tubing was inoperable. The last successful mechanical integrity test for this well was performed on August 24, 1998.

On September 27, 2005, September 28, 2005, November 28, 2005, and December 6, 2005, the District Office sent Farrell notices or correspondence advising Farrell of the alleged violations on the subject lease and requesting voluntary compliance.

An affidavit of Ramon Fernandez, Jr., P.E., Field Operations, states that 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, which is serious and may threaten the public health and safety. The same affidavit states that wells must be plugged as required by 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 zones or to flow to the surface. Uncased wells allow direct communication between zones and provide unimpeded access to the surface.

The Fernandez affidavit also states that without a working pressure observation valve on a well, pressure on the annulus cannot be detected, with resulting potential for leaks or discharges which may be a source of pollution to surface and subsurface waters.

Enforcement recommends that a total penalty of \$3,500 be imposed against Farrell for the alleged violations, calculated on the basis of two violations of Statewide Rule 3 at \$250 each, one violation of Statewide Rule 14(b)(2) at \$2,000; and one violation of Statewide Rule 46(g)(2) at \$1,000.

Farrell

Farrell conceded that he is the designated operator of the subject lease and well, and did not contest Enforcement's allegation that the involved violations were committed by Farrell. However, Farrell believes there are mitigating circumstances, and stated his intent to bring the lease and well into compliance.

Roy Farrell, Jr., acquired the subject well by transfer from his father. For a period of time, the well was used to dispose of saltwater from producing wells operated by Farrell. However, low oil prices made continued production of Farrell's oil wells uneconomical, and after December 2001, Farrell had no further use for the subject injection well.

With low oil prices starting in about 1988 and continuing thereafter, Farrell became financially distressed. A drilling program in the year 2000 was unsuccessful, when a dry hole was drilled. In 2001, two daughters of Roy Farrell, Jr., became seriously ill due to environmental problems in the area where the Farrells resided, and treatment cost Farrell \$130,000 in excess of his insurance coverage. A third daughter required an 18-month rehab program for an unrelated problem. At about the same time, Farrell suffered vandalism of one of his leases that resulted in the

loss of oil from valves which had been opened, causing Farrell further financial difficulty. Due to these various difficulties, Farrell had neither the time or the money to plug the subject well. Farrell did not have the financial standing to obtain bonding as an oil and gas operator in 2002, when his organization report became delinquent.

In 2002, Roy Farrell, Jr., started a new business, other than as an oil and gas operator, and this business has done well. In April 2006, Farrell sold an oil and gas lease for \$126,000, and this has provided sufficient money to obtain a letter of credit to renew Farrell's organization report and financial assurance and to plug the subject well. Farrell has obtained approval from Herring Bank in Vernon, Texas, to issue a \$50,000 letter of credit and anticipated filing for renewal of his Form P-5 organization report and financial assurance during the week following the hearing. Farrell also anticipated filing a Form W-3A (Notice of Intention to Plug and Abandon) for the Kyle (29558) Lease, Well No. 3 as soon as possible following the hearing.¹

Roy Farrell, Jr. testified that he had set aside enough money to renew his organization report and plug the subject well, and other wells in need of plugging, but he was not able to do this much and also pay an administrative penalty. Farrell recognized that the penalty recommended by Enforcement is consistent with the recommended standard penalty schedule for enforcement cases, but argues that these are guidelines only, and the Commission should exercise its discretion to reduce the recommended penalty in the particular circumstances of this case.

EXAMINER'S OPINION

Enforcement's evidence plainly establishes that the alleged violations were committed by Farrell, and this evidence is not disputed or rebutted by any of Farrell's evidence. The only disputed issues concern the amount of the administrative penalty, if any, that should be imposed and what needs to be ordered in the way of compliance.

In determining an appropriate administrative penalty, Texas Natural Resources Code §81.0531 requires that the Commission consider the respondent's history of previous violations, the seriousness of the violations, any hazard to the health or safety of the public, and the demonstrated good faith of the respondent.

¹ On October 23, 2006, the Commission approved renewal of Farrell's Form P-5 organization report, which is now active. On the same date, the Commission approved Farrell's filing of financial assurance in the amount of \$50,000 in the form of a letter of credit. On October 13, 2006, Farrell late-filed an exhibit consisting of an approved Form W-3A (Notice of Intention to Plug and Abandon) for the Kyle (29558) Lease, Well No. 3. The District Office made a posthearing inspection of the Kyle (29558) Lease on October 5, 2006. The identification sign missing from the lease entrance at the time of the hearing had been properly posted, but no sign was posted at the tank battery. The October 5, 2003, inspection report made no mention of the inoperable pressure observation valve on Well No. 3 and reported that the lease and well were in compliance with Statewide Rule 46. When Farrell's Form P-5 and financial assurance were approved on October 23, 2006, a Statewide Rule 14(b)(2) plugging extension was approved for the Kyle (29558) Well No. 3.

There is no evidence of any prior final enforcement orders entered against Farrell for violations of Commission rules. There is also no proof that the violations committed by Farrell caused any actual harm to any member of the public. There is evidence on both sides of the issue of whether Farrell has demonstrated good faith. On the one hand, Farrell did not resolve any of the involved violations prior to the hearing, although he was requested to do so by the District Office in September, November, and December 2005. Farrell's testimony concerning his financial circumstances does not make his case particularly unique in the enforcement case context, but may provide a partial explanation for Farrell's delay in achieving compliance. On the other hand, at the hearing, Farrell accepted responsibility for the involved violations and pledged to achieve compliance. The evidence shows that shortly after the hearing, Farrell posted the identification sign required by Statewide Rule 3 at the lease entrance of the subject lease and apparently resolved the Statewide Rule 46 problem on the lease having to do with a previously inoperable pressure observation valve on Well No. 3. Farrell also renewed his Form P-5 organization report and filed financial assurance in the amount of \$50,000, which is twice the amount that Farrell was required by law to file², to ensure that the subject well will be plugged without the use of State funds. When Farrell's Form P-5 organization report and financial assurance were approved on October 23, 2006, a plugging extension for the Kyle (29558) Lease, Well No. 3 was also approved.

On balance, the examiner believes that the evidence weighs in Farrell's favor on the good faith issue. The penalties recommended by Enforcement are consistent with the recommended standard penalty schedule for enforcement cases, but the penalty schedule provides that: (1) the schedule is provided solely as a guideline; (2) the amount of any proposed penalty is to be determined on an individual case-by-case basis for each violation by the hearings examiner after consideration of all evidence submitted at the hearing; and (3) the final amount of the penalty imposed is determined by the action of a majority of the Commissioners. In the circumstances of this case, the examiner does not believe that the full amount of the penalty recommended by Enforcement is warranted.

Enforcement recommends a penalty of \$250 each for two violations of the identification sign requirements of Statewide Rule 3. The evidence shows that one of these violations had been corrected as of October 5, 2003, and the other was continuing. The examiner recommends a penalty of \$250 for the missing sign at the tank battery on the subject lease, and a penalty of \$200 for the corrected sign violation at the lease entrance.

Enforcement recommends a penalty of \$1,000 for one violation of Statewide Rule 46(g)(2) relating to an inoperable pressure observation valve on Well No. 3 on the subject lease. The evidence shows that this violation was corrected prior to the posthearing District Office inspection on October 5, 2006. The examiner recommends a penalty of \$750 for this violation.

Enforcement recommends a penalty of \$2,000 for one violation of Statewide Rule 14(b)(2). At the hearing, Farrell acknowledged responsibility for the plugging of Well No. 3 on the subject

² The examiner has officially noticed the Commission's On-Schedule Leases, Wells, Wellbores by Operator database showing that Farrell is the operator of 7 wellbores. The Statewide Rule 78(g) "blanket bond" requirement for an operator of 7 wellbores is \$25,000.

lease and indicated that he had set aside money to plug the well when the services of a plugging contractor were available. Farrell has filed an approved Form W-3A (Notice of Intention to Plug and Abandon) for this well. A plugging extension was approved for the well when Farrell renewed his Form P-5 organization report and financial assurance, approved October 23, 2005. Farrell filed approved financial assurance in an amount that is twice the amount required by Statewide Rule 78(g)(1) to ensure that plugging of the subject well with State funds will not be necessary. The examiner recommends a penalty of \$1,000 for the time the subject well was out of compliance with Statewide Rule 14(b)(2).

The total penalty recommended by Enforcement is \$3,500. The total penalty recommended by the examiner is \$2,200.

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. Roy Farrell, Jr. DBA Farrell Oil Company (“Farrell”) was given at least ten (10) days notice of this hearing by certified mail, addressed to Farrell’s most recent Form P-5 organization report address. Farrell appeared at the hearing and presented evidence.
2. Farrell is a sole proprietorship, and Roy Farrell, Jr. is the owner.
3. As owner, Roy Farrell, Jr. was a person in a position of ownership or control of Farrell 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. Farrell’s Form P-5 organization report was delinquent between July 1, 2002, and October 23, 2006. On October 23, 2006, the Commission approved a Form P-5 renewal, and Farrell’s Form P-5 is now active. Farrell has filed approved financial assurance in the amount of \$50,000 in the form of a letter of credit.
6. Farrell designated himself to the Commission as the operator of the Kyle (29558) Lease, Well No. 3, Kyle (Canyon Charged 4200) Field, Hardeman County, Texas, by filing a Form P-4 (Certificate of Compliance and Transportation Authority) approved and effective on August 1, 1998.
7. On the occasion of District Office inspections on September 26, 2005, October 13, 2005, March 22, 2006, and August 25, 2006 (hereinafter referred to as “the District Office inspections”), the identification signs required by Statewide Rule 3 to be posted at the lease entrance and storage tank on the subject lease were missing. A posthearing inspection on October 5, 2006, disclosed that the required identification sign had been posted at the lease entrance, but the sign at the storage tank was still missing.

8. The Kyle (29558) Lease, Well No. 3 was permitted as a saltwater disposal well by Permit No. 15334 dated June 12, 1998.
9. On the occasion of the District Office inspections of the subject lease, Well No. 3 was equipped with tubing and casing, and the pressure observation valve on the tubing was inoperable.
10. The subject well has been inactive for more than one year and has not been plugged.
 - a. The District Office inspections disclosed that the subject well was inactive.
 - b. No injection activity has been reported to the Commission for the well since December 31, 2001.
 - c. No Plugging Record (Form W-3) or Cementing Affidavit (Form W-15) has been filed or approved for the subject well.
11. When Farrell's Form P-5 organization report and financial assurance renewal were approved on October 23, 2006, a plugging extension for Well No. 3 on the subject lease was also approved.
12. The estimated cost to the State to plug the Kyle (29558) Lease, Well No. 3 is \$23,600.
13. On September 27, 2005, September 28, 2005, November 28, 2005, and December 6, 2005, the District Office sent Farrell notices or correspondence advising Farrell of the involved violations on the subject lease and well and requested voluntary compliance.
14. In the event of a pollution or safety violation or other emergency, incorrect, illegible, or missing identification signs may cause delays in containing or remediating the violation or emergency.
15. Inactive wells must be plugged as required by Statewide Rule 14 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 zones or to flow to the surface. Uncased wells allow direct communication between zones and provide unimpeded access to the surface.
16. Without a working pressure observation valve on a well, pressure on the annulus cannot be detected, with resulting potential for leaks or discharges which may be a source of pollution to surface and subsurface waters.
17. No prior final enforcement orders have been entered against Farrell for violations of Commission rules.
18. Farrell has demonstrated some good faith.

- a. At the hearing in this docket, Farrell accepted responsibility for bringing the subject lease and well into compliance with Commission rules and pledged to do so.
- b. On or before October 5, 2006, Farrell corrected one of the involved Statewide Rule 3 violations by posting the required identification sign at the entrance of the subject lease and also corrected the involved Statewide Rule 46(g)(2) violation. Farrell has filed an approved Form W-3A (Notice of Intention to Plug and Abandon) for the subject well, and the well was brought into compliance with Statewide Rule 14(b)(2) when a plugging extension was approved for the well effective upon renewal of Farrell's Form P-5 organization report and financial assurance on October 23, 2006.
- c. Following the hearing in this docket, Farrell renewed his Form P-5 organization report and filed approved financial assurance in the amount of \$50,000, which is twice the amount required of Farrell pursuant to Statewide Rule 78(g)(1).

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. Roy Farrell, Jr. DBA Farrell Oil Company ("Farrell") was and is the operator of the Kyle (29558) Lease, Well No. 3, Kyle (Canyon Charged 4200) Field, Hardeman 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, Farrell had the primary responsibility for complying with Statewide Rules 3, 14, and 46 [Tex. R.R. Comm'n, 16 TEX. ADMIN. CODE §§3.3, 3.14, and 3.46], Chapters 89 and 91 of the Texas Natural Resources Code, and other applicable statutes and Commission rules respecting the subject lease and well.
5. Farrell violated Statewide Rule 3 [Tex. R.R. Comm'n, 16 TEX. ADMIN. CODE §3.3] on the subject lease by failing to post identification signs at the lease entrance and storage tank. The subject lease was out of compliance with Statewide Rule 3 at least during the period from September 26, 2005, to October 3, 2006, with respect to the required identification sign at the storage tank. Compliance with Statewide Rule 3 as to the required identification sign at the lease entrance was achieved on or before October 5, 2006.
6. Farrell violated Statewide Rule 14(b)(2) [Tex. R.R. Comm'n, 16 TEX. ADMIN. CODE §3.14(b)(2)] by failing to plug the subject well within one year after operations ceased. The subject well was out of compliance with Statewide Rule 14(b)(2) between December 31, 2002, and October 23, 2006. Compliance with Statewide Rule 14(b)(2) was achieved as of October 23, 2006.
7. Farrell violated Statewide Rule 46(g)(2) [Tex. R.R. Comm'n, 16 TEX. ADMIN. CODE §3.46(g)(2)] by failing to maintain a working pressure observation valve on the tubing of the

Kyle (29558) Lease, Well No. 3. The subject well was out of compliance with Statewide Rule 46(g)(2) at least from September 26, 2005, to August 25, 2006. Compliance with Statewide Rule 46(g)(2) was achieved on or before October 5, 2006.

8. The documented violations committed by Farrell constitute acts deemed serious and a hazard to the public health within the meaning of Texas Natural Resources Code §81.0531.
9. Farrell demonstrated good faith within the meaning of Texas Natural Resources Code §81.0531 by correcting all of the involved violations, except for the violation of Statewide Rule 3 [Tex. R.R. Comm'n, 16 TEX. ADMIN. CODE §3.3] pertaining to the required identification sign at the storage tank on the subject lease, on or before October 5, 2006.
10. As owner of Farrell Oil Company at the time Farrell violated Commission rules related to safety and the prevention or control of pollution, Roy Farrell, Jr., 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 Roy Farrell, Jr. DBA Farrell Oil Company be ordered to place the Kyle (29558) Lease into compliance with Statewide Rule 3 and to pay an administrative penalty of \$2,200.00.

Respectfully submitted,

James M. Doherty
Hearings Examiner