

June 20, 2002

OIL AND GAS DOCKET NO. 10-0226332

ENFORCEMENT ACTION AGAINST DYNE OIL & GAS, INC. FOR VIOLATIONS OF STATEWIDE RULES ON THE VENTURE (01559) LEASE, WELL NOS. 1, 4, 5, 6, 7, 8, 9, 11 AND 13, PANHANDLE HUTCHISON COUNTY FIELD, HUTCHISON COUNTY, TEXAS.

APPEARANCES:

FOR MOVANT:

Scott Holter, Staff Attorney

FOR RESPONDENT:

Lloyd Muennick, Attorney
Greg Hill, President
Billy Gilman, Petroleum Engineer

MOVANT:

Railroad Commission, Enforcement Section

RESPONDENT:

Dyne Oil & Gas, Inc.
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PROPOSAL FOR DECISION

PROCEDURAL HISTORY

DEFAULT CASE HEARD:	January 25, 2001
DEFAULT HEARING REOPENED:	March 9, 2001
REOPENED HEARING HELD:	April 2, 2001
CONSOLIDATED HEARING HELD:	January 28, 2002
CONSOLIDATED HEARING HEARD BY:	Mark Helmueller, Hearings Examiner
RECORD CLOSED:	February 19, 2002
PROPOSAL FOR DECISION PREPARED BY:	Mark Helmueller, Hearings Examiner
PROPOSAL FOR DECISION CIRCULATED:	June 20, 2002
CURRENT STATUS:	Protested

STATEMENT OF THE CASE

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

1. Whether the respondent should be required to plug or otherwise place in compliance with Statewide Rule 14, the Venture (01559) Lease, Well Nos. 1, 4, 5, 6, 7, 8, 9, 11 and 13, Panhandle Hutchison County Field, Hutchison County, Texas;
2. Whether the respondent 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 comply with said statutes and Statewide Rules 13 and 14;
3. Whether the respondent should be assessed administrative penalties of not more than \$10,000.00 per day for each offense committed regarding said leases and 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.

INTRODUCTION

Dyne Oil & Gas, Inc. (hereinafter "Dyne") appeared through its attorney and offered evidence at all proceedings but the first default hearing. Scott Holter, Staff Attorney, appeared representing the Railroad Commission of Texas, Enforcement Section. The Enforcement hearing files were admitted into evidence. The record was initially left open until September 15, 2001.

A request to submit additional evidence concerning Dyne's organization status was filed by Enforcement on December 3, 2001. On January 2, 2002, Dyne filed exhibits which asserted that it attempted to bring the lease into compliance through a transfer to another operator. Based on the additional exhibits filed by both parties, a further hearing was held on January 28, 2002. The parties to submitted written closing statements on February 19, 2002.

In its closing argument, Enforcement recommended that Dyne be ordered to pay an administrative penalty of \$28,000.00. This penalty consists of: \$18,000.00 for 9 violations of Rule 14(b)(2) at \$2,000.00 per violation and \$10,000.00 in enhanced penalties based on the entry of final orders in Oil & Gas Docket Nos. 10-0223724 and 10-0224181. Dyne argued that no administrative penalty should be imposed for any of the violations.

The examiner agrees with the standard penalty recommended by Enforcement for the violations of Rule 14(b)(2), but believes that the enhancement for was not sought in the complaint or at the hearing and is therefore not warranted. Accordingly, the examiner recommends an administrative penalty of \$18,000.00.

PROCEDURAL SUMMARY

On October 13, 2000, based on a referral from the District Office, Enforcement filed a

complaint against Dyne for violations of Rule 14(b)(2) on the Venture Lease. Postal records confirm that Dyne received the Complaint and Notice of Opportunity of Hearing on October 20, 2000. The complaint sought administrative penalties of \$36,000.00 for nine violations of Rule 14(b)(2) (failure to timely plug) and an additional nine violations of Rule 14(b)(2)(E) (failure to conduct required well tests). On November 30, 2000, an amended complaint and notice was sent to Dyne setting a hearing date of January 25, 2001. The amended complaint dropped the nine violations of Rule 14(b)(2)(E), but still alleged nine violations of Rule 14(b)(2) and sought administrative penalties of \$18,000.00.¹

Subsequent to the service of the original complaint, the Commission entered orders against Dyne in Oil & Gas Docket Nos. 10-0223724 and 10-0224181 assessing \$74,000.00 in penalties. The order in Docket No. 10-0224181 became final on November 5, 2000 after Dyne did not file a request for rehearing. The order in Docket No. 10-0223724 became final on December 5, 2000 when the Commission denied Dyne's request for rehearing.

Dyne did not appear at the hearing set for January 25, 2001. A default order was prepared, but Dyne filed a request to reopen the hearing before the default order was signed. The request to reopen the hearing was granted and a hearing was set for April 2, 2001.

At the reopened hearing, Dyne acknowledged that all nine wells on the Venture Lease were in violation of Rule 14(b)(2). Dyne claimed that it was attempting to restore production in six of the wells. Dyne also indicated that it was negotiating an agreement to pay the \$74,000.00 administrative penalty and resolve all outstanding violations. Finally, Dyne represented that it was obtaining blanket financial security which would be in place by September 1, 2001. Accordingly, the examiner left the record open for the submission of additional evidence on the issue of compliance.

On August 15, 2001, Dyne was advised by Enforcement that it had breached the settlement agreement because it had failed to plug Well No. 6 on the Gray Lease. Due to the breach of the settlement agreement, Dyne's organization report was revoked on August 29, 2001.

In August 2001², Dyne also submitted to Enforcement documents in support of a continued good faith claim to operate the Venture Lease in order to obtain approval to transfer the lease to another operator. On August 28, 2001, Enforcement advised that the documents did not establish a good faith claim of a continued right to operate. These documents were not provided to the examiner and Enforcement did not advise the examiner of its position that the documents submitted did not establish a good faith claim of a continued right to operate the Venture Lease.

On December 3, 2001, Enforcement submitted a request to late-file exhibits concerning Dyne's organization status. On December 28, 2002, the examiners advised that having received no objections to Enforcement's request, the evidence would be admitted and the record was closed. On January 2, 2002, Dyne submitted correspondence claiming that it had attempted to transfer the

¹The complaint was never amended to request the prior penalty enhancement of \$10,000.00.

²The exact date in August on which Dyne submitted documentation of its continuing good faith claim to operate the Venture Lease is in dispute and is not clear from the documents submitted to the examiner.

Venture Lease to another operator. Dyne asserted that the P-4 was not approved based on a determination by the Enforcement Staff Attorney prosecuting this docket that Dyne did not establish a right to operate the Venture Lease to the Staff Attorney's satisfaction.

POSITIONS OF PARTIES

Commission records indicate that Dyne filed its initial organization report in February 1979. On March 20, 2002, Dyne restored its organization status by: 1) submitting evidence that it plugged Well No. 6 on the Gray (01708) Lease as required by the Final Order entered in Docket No.10-0224181; 2) transferring three leases to other operators to bring its total well count under 100; and 3) filing a letter of credit of \$50,000.00 to meet its financial security requirements. All of the violations alleged in the complaint have been resolved. However, the parties dispute the time period that the wells were not in compliance with Rule 14(b)(2). As previously noted, the parties also disagree on the amount of any administrative penalties.

Enforcement submitted Commission records showing that Dyne designated itself as the operator of the Venture Lease by filing a Commission Form P-4 (Producer's Transportation Authority and Certificate of Compliance) effective April 1, 1979. .

On September 18, 2000, Dyne filed requests for plugging extensions on the Venture Lease. The plugging extensions were denied as several wells required fluid level tests as reported on Commission Form H-15 (Test on Inactive Well More Than 25 Years Old). Additionally, Dyne's financial institution would not honor the check Dyne submitted as payment for the required fees.

An inspection report from September 11, 2000 and production records were submitted to show that no production from Well Nos. 1, 4, 5, 6, 7, 8, 9, 11 and 13 on the Venture Lease was reported after March 1998. Enforcement argues that because the last reported production was in March 1998 and no plugging extensions were granted, that the wells on the Venture Lease were out of compliance with Rule14(b)(2) from April 1999 through September 2000.

Enforcement contends that Venture Lease was also out of compliance with Statewide Rule 14(b)(2) from September 2000 until February 11, 2002 with the exception of a one week period from August 23, 2001 through September 1, 2001. Enforcement also notes that when the order in Docket No.10-0224181 became final on November 5, 2000, Dyne was prohibited by §91.114(a) of the Texas Natural Resources Code from obtaining a plugging extension until it complied with the terms of the order. Dyne did not resolve this statutory bar until it entered into the settlement agreement on June 28, 2001 and paid all required fees.³

Enforcement also argues that later attempts by Dyne to transfer the Venture Lease to another operator were denied because Dyne still failed to provide evidence of its good faith claim of a right to operate the Venture Lease. Enforcement claims that it was not until the February 4, 2002 hearing called by the examiner, that Dyne submitted sufficient evidence to support its good faith claim to operate the Venture Lease.

³The order in Oil & Gas Docket No. 10-0223724 also acted as a statutory bar to granting Dyne's request for a plugging extension after it became final on December 5, 2000.

Dyne claims that the Commission deliberately delayed accepting the funds tendered for plugging extensions which would have brought the Venture Lease into compliance through September 1, 2001. Dyne also argues that Enforcement wrongly refused to lift the legal hold on the Venture Lease in August 2001. Dyne claims that correspondence was forwarded to Enforcement on August 8, 2001, noting that the same evidence presented at the July 19, 2001 hearing for the Oates Lease applied to the Venture Lease. Enforcement responded to this request on August 23, 2001, refusing to lift the hold. Dyne provided additional documentation on August 28, 2001, but again Enforcement refused to lift the hold.

Enforcement contends that administrative penalties in the amount of \$2,000.00 per well for each violation are appropriate based on the time period the leases were not in compliance with Rule 14(b)(2). Enforcement also notes that the violations were not resolved through Dyne restoring production or plugging the wells, but were corrected by transferring the leases to a new operator. Finally, Enforcement contends in the Closing Argument that a \$10,000.00 enhancement penalty should be added to the administrative penalty based on the \$74,000.00 in penalties assessed in Oil & Gas Docket Nos. 10-0223724 and 10-0224181.

Dyne argues that *Lawyers Surety Corporation v. State of Texas*, 753 S.W. 2d 703 (Tex.Civ.App. – Austin – 1988, no writ), supports its position that no penalty is appropriate. Dyne contends that the Commission admits in its Responses to Interrogatories in Oil and Gas Docket No. 10-0227703; *Enforcement Action Against Dyne Oil & Gas, Inc. for Violations of Statewide Rules on the Oates (00981) Lease, Well Nos. 1, 4, 6, 9d, 10d, 11, 12, 16, 17, 18, and 19, Panhandle Hutchison County Field, Hutchison County, Texas*, that no Commission rule permits a \$2,000.00 per well penalty on wells that will produce and are not causing pollution. Dyne claims that this response, coupled with the reasoning applied by the court in *Lawyers Surety*, precludes the Commission from imposing an administrative penalty where the Commission possesses neither a common law right to liquidated damages, nor any proof of actual damages.

APPLICABLE AUTHORITY

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.

The operator of a well must plug a well when required and in accordance with Commission rules. For Form P-4s filed prior to September 1, 1997, the operator, for purposes of plugging liability, is presumed to be the person who assumed responsibility for the physical operation and control of a well as shown on the approved Form P-4 designating that person as operator.

The primary controlling legal authority for assessing administrative penalties for violations of Commission Rules is Texas Natural Resources Code §81.0531 which provides in pertinent part:

- (a) If a person violates provisions of the title which pertain to safety or the prevention or control of pollution or the provisions of a rule, order, license, permit, or certificate which pertain to safety or the prevention or control of pollution and are issued under this title, the person may be assessed a civil penalty by the Commission.

(b) The penalty may not exceed \$10,000 a day for each violation. Each day a violation continues may be considered a separate violation for purposes of penalty assessments.

(c) In determining the amount of the penalty, the commission shall consider the permittee's history of previous violations, the seriousness of the violation, any hazard to the health or safety of the public, and the demonstrated good faith of the person charged.

EXAMINER'S OPINION

Because both parties agree that all violations are now resolved, the only issue to be determined is the amount of any administrative penalty to be assessed against Dyne. Dyne claims that the \$2,000.00 penalty per well is not supported by any Commission rule. Dyne therefore claims that the *Lawyers Surety* case precludes an administrative penalty absent any common law right to liquidated damages, or proof of actual damages.

Time Period Out of Compliance

The dispute between the parties over how long the Venture Lease was out of compliance essentially boils down to Dyne's complaint that the prosecuting Staff Attorney failed to properly consider the evidence of a good faith claim to operate the Venture Lease, thereby delaying any transfer to a new operator. The record supports Dyne's position. The issue of whether Dyne had a good faith claim to operate is directly relevant to the issue in this docket of how long the wells were out of compliance. Given that this issue involved a contested case, the determination of the sufficiency of the evidence of a good faith claim should be resolved in the hearing by the Commission and not by the prosecuting attorney. Clearly the Staff Attorney should advocate Enforcement's position on any evidentiary issue, but where a contested case exists, it is the examiner's responsibility to prepare a proposal for decision and the Commissioners' role to ultimately determine the appropriate Commission action.

It was determined in the *Oates* docket in July 2001, and further admitted by Enforcement in February 2002, that Dyne's evidence supported a good faith claim to operate the Venture Lease. It is also the examiner's opinion that while the evidence submitted does not conclusively establish the validity of Dyne's claim, it is sufficient to support a good faith claim to operate the Venture Lease.

Dyne provided a Deed of Trust at the July 2001 *Oates* hearing identifying its rights under the original 1926 Venture Lease. Dyne also provided additional documentation in August 2001 asserting that the continuous operations and production clauses of the original lease applied to extend the original lease to the current time. It appears that this evidence was provided to the Staff Attorney no later than August 28, 2001. It also appears that Enforcement's opinion that the evidence was insufficient to establish a good faith claim to operate may have prevented Dyne from transferring the lease. This potentially impacted Dyne's ability to bring the Venture Lease into compliance through a transfer to a bonded operator. Accordingly, the time period the Venture Lease was not in compliance should be limited from April 1, 1999 to August 28, 2001.

Ultimately, however, the time period out of compliance does not alter the amount of the administrative penalty in this docket. It is undisputed that the Venture Lease was out of compliance from April 1, 1999 to August 31, 2000 a period of 17 months. The examiner also finds that the Venture Lease was not in compliance with Rule 14(b)(2) from September 1, 2000 through August 28, 2001 based on Dyne's admission at the hearing on April 2, 2001 that the wells were not in compliance with Rule 14(b)(2). This adds an additional 12 months to the time period out of compliance, bringing the total to 29 months. Such a lengthy period of noncompliance provides an appropriate basis for imposing the full recommended administrative penalty of \$18,000.00, consisting of \$2,000.00 per violation of Rule 14(b)(2) for the nine wells on the Venture Lease.

Statutory Basis for \$2,000.00 per Well Administrative Penalty

Dyne contends that *Lawyers Surety Corporation v. State of Texas*, 753 S.W. 2d 703 (Tex.Civ.App. – Austin – 1988, no writ), supports its position that no penalty is appropriate. In *Lawyers Surety*, the appellate court refused to allow the Commission to collect on a performance bond holding that the forfeiture provisions in the bond were not supported by a Commission Rule. The court further held that no statute, common law right, or proof of actual damages established a right to a penalty allowing the Commission to collect on the bond.

Dyne's observation that the \$2,000.00 administrative penalty amount is not supported by a Commission rule is correct. No Commission rule sets the amount of an administrative penalty. However, Dyne's argument ignores the explicit statutory authority provided to the Commission in Texas Natural Resources Code §81.0531 which allows the Commission to impose a penalty of up to \$10,000.00 per day, per violation. This distinguishes this case from the holding in the *Lawyers Surety* decision. Accordingly, the examiner rejects Dyne's argument challenging the validity of the administrative penalty.

Enhancement of Administrative Penalty for Prior Violations

Additionally, the examiner finds that Enforcement's belated attempt to seek the enhancement for prior final orders entered against Dyne should be rejected. There is no question that Enforcement may properly seek an enhanced penalty based on the prior final orders entered against Dyne under Texas Natural Resources Code §81.0531(c) which specifically requires the Commission "to consider the permittee's history of previous violations". However, Enforcement did not seek an enhanced penalty in the complaint, the first amended complaint, the default hearing, the April 2, 2001 hearing or the February 4, 2002 hearing. The first time Enforcement requests an enhancement related to the violations in the Venture Docket is in its February 19, 2002 closing argument. Such a late request, unaccompanied by supporting authority, and offered without seeking an appropriate amendment of the pleadings should be rejected. Further, the basis for the enhancement – the final orders the Commission entered orders against Dyne in Oil & Gas Docket Nos.10-0223724 and 10-022418 – occurred subsequent to the service of the original complaint. Absent the consent of the respondent to a trial amendment, the late notice of the request for this enhancement unduly prejudices the respondent's ability to defend itself from the allegations raised.

CONCLUSION

In conclusion, the examiner recommends that an administrative penalty for the 9 violations of Rule 14(b)(2) on the Venture Lease at \$2,000.00 per violation is \$18,000.00. The examiner also recommends that no enhancement penalty be added to this docket.

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 Dyne Oil & Gas, Inc. (“Dyne”) was given at least 10 days notice of the proceeding by certified, first-class mail, addressed to its most recent Form P-5 (Organization Report) addresses. Respondent appeared at the hearings and presented evidence.
2. Commission records indicate that Dyne filed its initial organization report in February 1979. Dyne’s organization report is currently active.
3. Dyne designated itself as the operator of the Venture Lease by filing a Commission Form P-4 (Producer's Transportation Authority and Certificate of Compliance) effective April 1, 1979.
4. Dyne last reported production on the Venture Lease in March 1998.
5. Dyne’s transfer of the Venture Lease to a bonded operator was approved by the Commission on February 11, 2002.
6. Dyne submitted evidence establishing a good faith claim to operate the Venture Lease on August 28, 2001.
7. Dyne provided a Deed of Trust at the July 2001 *Oates* hearing identifying its claim to operate under the original 1926 Venture Lease.
8. Dyne provided additional documentation asserting that the continuous operations and production clauses of the original lease kept the lease in effect.
9. On September 18, 2000, Dyne requested plugging extensions for the subject wells on the Venture Lease. The extensions were denied because the Dyne’s check was not honored by its financial institution.
10. Usable quality groundwater may be contaminated by migrations or discharges of saltwater and other oil and gas wastes from the subject wells. Unplugged wellbores 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. Dyne was the operator of the Venture Lease as defined by Statewide Rule 14 and Section 89.002 of the Texas Natural Resources Code and is a person as defined by Statewide Rule 79 and Chapters 85 and 89 of the Texas Natural Resources Code.
4. During the time period it was the operator of the subject leases, Dyne possessed the primary responsibility for complying with Rule 14 and with Chapter 89 of the Texas Natural Resources Code as well as other applicable statutes and Commission rules.
5. The Venture Lease was out of compliance with Statewide Rule 14 from April 1, 1999 through August 28, 2001.

RECOMMENDATION

The examiner recommends that the above findings and conclusions be adopted and the attached order approved, requiring that Dyne Oil & Gas, Inc., within 30 days from the day immediately following the date this order becomes final, to pay an administrative penalty in the amount of EIGHTEEN THOUSAND DOLLARS (\$18,000.00).

Respectfully submitted,

Mark Helmueller
Hearings Examiner