



# RAILROAD COMMISSION OF TEXAS

## HEARINGS DIVISION

### PROPOSAL FOR DECISION

**OIL & GAS DOCKET NO. 08-0298460**

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**THE APPLICATION OF ROFF OPERATING COMPANY, LLC PURSUANT TO STATEWIDE RULE 50 FOR APPROVAL OF ITS FORM H-13 EOR POSITIVE PRODUCTION RESPONSE CERTIFICATION FOR THE EAST MILAGRO UNIT (40636), PROJECT NO. F-18339, BREEDLOVE (SPRABERRY) FIELD, MARTIN COUNTY, TEXAS**

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**HEARD BY:** Peggy Laird, P.G. – Technical Examiner  
Ryan M. Lammert– Administrative Law Judge

**APPEARANCES:**

Clark Jobe

**REPRESENTING:**

Roff Operating Company, LLC

### PROCEDURAL HISTORY

Application (Form H-12) Approved:	November 29, 2010
Application (Form H-13) Filed:	June 30, 2015
Application (Form H-13) Denied:	June 30, 2015
Request for Hearing:	July 31, 2015
Notice of Hearing:	November 23, 2015
Date of Hearing:	December 21, 2015
Proposal For Decision Issued:	September 14, 2016

### STATEMENT OF THE CASE

Pursuant to Statewide Rule 50 (16 Tex. Admin. Code § 3.50), Roff Operating Company, LLC ("Roff") seeks Commission certification of an enhanced oil recovery (EOR) positive oil production response for its East Milagro Unit (40636), Project No. F-18339, in the Breedlove (Spraberry) Field, Martin County, Texas. Roff's application on Form H-13 was administratively denied by Commission staff because it did not meet the time constraints provided by Statewide Rule 50. Roff's evidence shows the project

demonstrated a positive production response within the three-year time period required by Rule 50. Roff requested a hearing on the matter, which Commission staff did not protest. The Examiners recommend denial of the application for failure to comply with the statutory filing deadline.

### **APPLICABLE LAW**

Texas Tax Code § 202.054 (g) states: Subject to the provisions of Subsections (b) and (h) of this section, the recovered oil tax rate applies to oil on which a tax is imposed by this chapter for the 10 years beginning the first day of the month following the date the commission certifies that, in the case of an enhanced recovery project including a co-production project, a positive production response has occurred or, in the case of an expansion, other than related to a co-production project, incremental production has occurred, if the application for certification is filed: (1) not later than three years from the date the commission approves the project if the project is designated as a new or existing project other than a co-production project that uses a secondary recovery process; or (2) not later than five years from the date the commission approves the project if the project is designated as a new or existing project that uses a tertiary recovery process or is a co-production project.

Statewide Rule 50(g)(2)(A) states: The operator of an EOR project that meets the requirements of this section shall demonstrate to the Commission a positive oil production response before the operator can receive Commission certification of such a positive production response. The certification date may be any date desired by the operator, subject to Commission approval, following the date on which a positive oil production response first occurred. The operator shall apply for a positive production response certificate within three years of project approval for secondary projects, and within five years of project approval for tertiary projects, to qualify for the recovered oil tax rate. The oil produced from the designated area of a new EOR project or incremental oil produced from the designated area of an expanded EOR project after the date of certification of a positive production response is eligible for the recovered oil tax rate. The operator shall apply to the comptroller pursuant to the Tax Code, '202.052 and '202.054, to qualify for the recovered oil tax rate.

Statewide Rule 50(g)(2)(C) states: The application for the positive production response certificate shall be processed administratively. If the Commission representative denies administrative approval, the applicant shall have the right to a hearing upon request. After hearing, the examiner shall recommend final action by the Commission.

### **DISCUSSION OF THE EVIDENCE**

Mr. Clark Jobe, the attorney representing Roff, appeared and presented evidence for the captioned docket. The Breedlove (Spraberry) Field ("the Field") was discovered in 1962 at a depth of 8,350 feet. Roff distinguished this field as being

separate from and not consolidated into the Spraberry (Trend Area). The Field is developed with vertical wells which have produced 3.2 million barrels ("bbls") of oil. There are sixteen producing wells, according to the December 2015 oil proration schedule.

Roff filed its original Form H-12: New or Expanded Enhanced Oil Recovery Project and Area Designation Approval Application, on November 29, 2010. The Form H-12 was filed before the Commission's hearing on the unitization application for the East Milagro Unit ("EMU"). The EMU application was approved by Final Order 08-0267719 dated February 22, 2011. According to the Form H-12, Roff estimated an additional 350,000 bbls of oil would be produced from the EMU as a result of its secondary recovery project. Subsequent to the issuance of Final Order 08-0267719, Roff supplemented its original Form H-12 application on February 25, 2011. On March 3, 2011, Commission staff administratively approved Roff's H-12 application effective from the date of the original H-12 application, or November 29, 2010.<sup>1</sup>

Roff began active operation of the enhanced oil recovery project on January 6, 2012, and obtained a positive response from the waterflood operation on December 15, 2012. Roff had until November 29, 2013, to submit Form H-13: Positive Production Response Certification Application, demonstrating a positive production response to the project. Roff filed its Form H-13 application on June 30, 2015, more than three years after the effective date of the Form H-12. Commission staff administratively denied the Form H-13 application on June 30, 2015.

Roff has reported production of 214,499 bbls of oil produced on the EMU from May 2011 through September 2015.<sup>2</sup> If the Form H-13 had been timely filed, Roff reports it would have been eligible for a severance tax incentive for 184,016 barrels of oil. If the Form H-13 application is approved effective from date of filing, June 30, 2015, Roff would lose the tax incentive for two years and ten months, amounting to 158,437 bbls of oil. Roff determined that this loss constitutes eighty-six percent of the eligible tax break from December 2012 to June 2015.<sup>3</sup>

Mr. Jobe stated that Roff was a small company with twelve employees, and proposed the lapse in timely filing the Form H-13 was because of inexperience, as this is Roff's first secondary recovery project. He indicated that the Form H-13 application was filed less than three years after the date that a positive response to the waterflood operation was obtained, and suggested that Roff may have been confused regarding the required filing date for the Form H-13. Mr. Jobe stated that Roff accepts that they failed to comply with the statutory filing deadline, and would not find it adverse if the Form H-13 is approved effective from the application date of June 30, 2015, and forward. In support of Roff's request, Mr. Jobe cited the Commissioners' discussion in

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<sup>1</sup> Exhibit No. 12

<sup>2</sup> Exhibit No. 10

<sup>3</sup> Exhibit Nos. 10 and 12 – subtracting production from December 2012 to June 2015 from the sum of production from December 2012 through September 2015

open conference and Final Order 8A-0296035, dated December 15, 2015, in which the Commission certified a Form H-13 that was submitted outside of the statutory time periods.<sup>4</sup>

### **EXAMINERS' ANALYSIS**

The Examiners agree with Roff that the secondary recovery project convincingly demonstrated a positive production response in December 2012, about two years into the three year period required to demonstrate such a response, and that the response has been sustained. The Examiners further agree that, in general, such secondary recovery projects are necessary to prevent waste of hydrocarbons and to protect correlative rights.

However, the Examiners do not find that either the Texas Tax Code or Statewide Rule 50 provide for an exception, variance, or extension of this filing period. The Examiners, therefore, cannot conclude that Roff met the requirements of Statewide Rule 50(g)(2)(A) for its positive production response certification. Roff argues the Commission has broad discretion under the Texas Tax Code to interpret Statewide Rule 50. Nonetheless, the Examiners cannot reach a finding of fact that Roff's petition meets the requirements of the Texas Tax Code or Statewide Rule 50. The Examiners recommend Roff's application be denied.

The Examiners' analysis of this matter is separated in several components: (1) the requirements of Texas Tax Code § 202.054(g); (2) the Commission's implementation of Statewide Rule 50; and (3) the precedent set by prior Commission action cited by Roff.

#### ***Requirements of Texas Tax Code § 202.054(g)***

As described on page 2 above, the present matter is governed by the Texas Tax Code §202.054(g) and Statewide Rule 50(g)(2)(A), which provide a severance tax reduction for successful secondary and tertiary recovery programs. The Texas Tax Code and Statewide Rule 50 require an applicant to apply for a positive production response certification within three years of project approval of a secondary recovery process. Pursuant to Texas Tax Code §202.054(g), the recovered oil tax rate applies...if the application is filed...not later than three years from the date the Commission approves the project if the project is designated as a new or existing project... that uses a secondary recovery process. According to the Code Construction Act, "[w]ords and phrases shall be read in context and construed according to the rules of grammar and common usage."<sup>5</sup> The words ...not later than three years from the date the Commission approves the project... in Tax Code § 202.054(g) are clear and, in common usage, imply an absolute cut-off date. Further, Statewide Rule 50 clearly states that "...the operator

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<sup>4</sup> Exhibit Nos. 15 and 16

<sup>5</sup> Texas Gov't Code §311.011

shall apply for a positive production response certificate within three years of project approval for secondary projects..." The Code Construction Act states use of the word "shall" imposes a duty.<sup>6</sup> In this case, Roff had a duty to file its Form H-13 no later than November 29, 2013. Roff filed its Form H-13 application on June 30, 2015, exceeding the three year limit to file after project approval for its secondary recovery project.

### ***Implementation of Statewide Rule 50***

The Commission implements its responsibilities under Texas Tax Code § 202.054(g) and Statewide Rule 50(g)(2)(A) by the administration of three forms, each initiated by operator action and followed by a Commission action. Two of these forms are relevant to this case:

#### **Form H-12, New or Expanded Enhanced Oil Recovery Project and Area Designation Approval Application**

**Operator Action:** Submit Form H-12 to request Commission approval of the EOR project as a prerequisite to eligibility for the EOR severance tax rate reduction. Form H-12 must be submitted before injection activities begin. Roff met this requirement.

**Commission Action:** If the H-12 is approved, the operator will be issued a Project and Area Designation Approval. The H-12 approval date starts the clock on subsequent requirements.

#### **Form H-13, EOR Positive Production Response Certification Application**

**Operator Action:** Form H-13 must be filed to request Commission certification that a positive production response has occurred. The operator is permitted to file once a positive production response occurs. However, the form must be filed no later than three years from project and area designation (Form H-12) approval. The operator is responsible for monitoring the project timing.

**Commission Action:** Commission certification of the H-13 positive production response entitles the operator to apply to the Comptroller of Public Accounts for a reduced severance tax rate for a period of time. Commission staff does not and is not responsible for notifying operators of the pending expiration of the Form H-13 filing period.

The following time line unfolded with regard to Roff and Commission actions:

*November 29, 2010:* The Commission receives Roff's Form H-12 for the EMU EOR Project.

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<sup>6</sup> Texas Gov't Code §311.016(2)

*February 22, 2011:* The Commission entered an order approving the EMU EOR Project in Docket No. 08-0267719.

*February 25, 2011:* Roff supplemented its Form H-12 application with a copy of Final Order 08-0267719 and injection well permit approvals.

*March 3, 2011:* Commission staff administratively approves Roff's Form H-12 with an effective date of November 29, 2010. Staff assigned it Project No. F-18339 and directed Roff to file Form H-13 within three years.

*December 15, 2012:* Roff observes a positive production response from the EMU EOR Project (No. F-18339).

*November 29, 2013:* The statutory deadline for filing Form H-13 passes for the EMU EOR Project (No. F-18339).

*June 30, 2015:* The Commission receives Roff's Form H-13 for the EMU EOR Project (No. F-18339).

*June 30, 2015:* Commission staff administratively denies Roff's Form H-13.

### ***Precedent***

Roff offered a previous case as precedent in which the Commission certified an applicant's Form H-13. On December 15, 2015, the Commission found in Oil & Gas Docket No. 8A-0296035 that Parallel Petroleum LLC's Form H-13 was technically complete and met the positive production response requirements of Statewide Rule 50.<sup>7</sup> In the Parallel case, a positive production response was not observed within the statutory time period, and occurred a few months after the three-year statutory deadline. The Commission concluded in the Parallel case that the application was technically complete, and therefore met the requirements of Statewide Rule 50. The Commission determined the appropriate certification date was March 10, 2015, when Parallel filed the Form H-13.

The present case presents a different issue than in the docket referenced by Roff. In this case, Roff acknowledges they filed the Form H-13 late, and does not disagree that they failed to comply with the statutory filing deadline. Roff is requesting the Commission reach a similar decision as in Docket No. 8A-0296035. Roff stated they would not find it adverse if the Form H-13 is approved effective from the application date of June 30, 2015.<sup>8</sup> Roff accepts they would lose the tax incentive for two years and ten

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<sup>7</sup> Exhibit Nos. 15 and 16.

<sup>8</sup> Recording 35:13/37:02

months, amounting to 158,437 bbls of oil, or eighty-six percent of the eligible tax break from December 2012 to June 2015.

The Examiners do not find that either the Texas Tax Code or Statewide Rule 50 provide for an exception, variance, or extension of this filing period. The Examiners, therefore, cannot conclude that Roff met the requirements of Statewide Rule 50(g)(2)(A) for its positive production response certification.

Based on evidence presented, the Examiners recommend the following Findings of Fact and Conclusions of Law.

### **FINDINGS OF FACT**

1. Notice of this hearing was given to all parties entitled to notice.
2. The Commission approved Roff's application (Form H-12) for the EMU water flood project, effective November 29, 2010.
3. According to the provisions of the Texas Tax Code and Statewide Rule 50(g)(2)(A), Roff had until November 29, 2013 to apply for a positive production response certificate.
4. The secondary recovery project demonstrated a positive production response on December 15, 2012, within the three-year time frame established by Statewide Rule 50. This is not disputed.
5. Roff submitted a Form H-13, EOR Positive Production Response Certification Application, on June 30, 2015, approximately 2½ years after the positive production response was observed and eighteen months after the November 29, 2013, statutory deadline expired.
6. On June 30, 2015, Commission staff denied Roff's Form H-13 application because "the Form H-12 on file has expired."
7. On July 31, 2015, Roff requested the matter be set for a hearing.
8. Roff does not dispute its failure to submit Form H-13 in a timely manner.

### **CONCLUSIONS OF LAW**

1. Resolution of the subject application is a matter committed to the jurisdiction of the Railroad Commission of Texas. Tex. Nat. Res. Code § 81.051.
2. All notice requirements have been satisfied. 16 Tex. Admin. Code § 1.45.

3. Roff Corporation did not meet the requirements of Texas Tax Code § 202.054(g) or Statewide Rule 50(g)(2)(A) for positive production response certification.
4. Statewide Rule 50 does not provide the Examiners with direction or discretion to amend the filing periods or otherwise recommend the certification sought by Roff.

**EXAMINERS' RECOMMENDATION**

Based on the above findings of fact and conclusions of law, the Examiners recommend that Roff Operating Company, LLC's application for positive production response certification for the EMU secondary recovery water flood project be denied.

Respectfully submitted,



Peggy Laird, P.G.  
Technical Examiner



Ryan M. Lammert  
Administrative Law Judge