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DANA AVANT LEWIS
INTERIM DIRECTOR

RAILROAD COMMISSION OF TEXAS

HEARINGS DIVISION

OIL AND GAS DOCKET NO. 01-0308173

THE COMPLAINT OF KEITH KNAPP THAT NORTH TEXAS ENERGY, INC. (614190) DOES NOT HAVE A GOOD FAITH CLAIM TO OPERATE THE BALCH, M. W. (08171) LEASE, WELL NOS. 1, 2, 3, 4, 6, 7, 10, 11, 12, 13, AND 14, MINERVA-ROCKDALE FIELD, MILAM COUNTY, TEXAS

AMENDED PROPOSAL FOR DECISION

HEARD BY:

Kristi M. Reeve, Administrative Law Judge
Robert Musick, P.G., Technical Examiner

APPEARANCES:

For Complainant Keith Knapp –
Mr. Keith Knapp
Mr. Phillip Baldwin, Jr., Attorney

For Respondent North Texas Energy, Inc. –
Mr. Kevin Jones, CEO
Mr. Gregory M. Klipp, Attorney

PROCEDURAL HISTORY:

Complaint Filed – December 5, 2017
Notice of Hearing – February 8, 2018
Hearing on the Merits – March 21, 2018
Transcript Received – March 27, 2018
Proposal for Decision Issued – August 15, 2018

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Summary

Keith Knapp (“Knapp” or “Complainant”), filed with the Commission a complaint letter challenging North Texas Energy, Inc.’s (“North Texas” or “Respondent”) good faith claim to a continued right to operate the Balch, M. W. (08171) Lease, Well Nos. 1, 2, 3, 4, 6, 7, 10, 11, 12, 13, and 14, Minerva-Rockdale Field, Milam County, Texas (“Lease”). Specifically, Complainant alleges that the Lease was “abandoned and turned back over to the land owner and mineral owner [***] and that without a lease cannot be produced again [***] these wells should be plugged as they are abandoned.”⁵ In response to the Complaint, North Texas requested a hearing on the merits.

The issues before the Commission are whether North Texas has a good faith claim to operate the Lease, as that term is defined in Statewide Rule 15, and if it does not, should be ordered to plug and abandon the Lease in accordance with Statewide Rule 14.

At the hearing on the merits, Knapp testified that he had signed an agreement with Respondent on October 27, 2015, and that by such written document Respondent agreed that the Balch, M. W. Lease was terminated.⁶ Knapp also testified that he consulted with Blaine Rabel at the Commission who explained to him that he could not take possession of the wells because he was not an operator and that he had no intention of taking regulatory responsibility for any wells on the Lease.⁷

Gregory Klipp introduced the testimony of Kevin Jones, the CEO of North Texas, to show that the 2015 agreement contractually transferred plugging and P-4 regulatory responsibility to Mr. Knapp and that North Texas no longer claimed an interest in the Lease.⁸ Mr. Jones also testified that there is another well on the Lease he believes was also include in the 2015 agreement that is not on the proration schedule, as the well was drilled, not completed and remains unplugged.⁹

The Administrative Law Judge and Technical Examiner (collectively “Examiners”) respectfully submit this Proposal for Decision (“PFD”) and recommend the Railroad Commission (“Commission” or “RRC”) find that North Texas does not have a good faith claim to operate the Lease and order the Lease plugged and abandoned in accordance with Statewide Rule 14. The Examiners find that while there may be a bona fide contractual dispute between the parties as to plugging liability, such a dispute is contractual and thus outside the jurisdiction of the Commission, and the dispute does not defeat Respondent’s obligation as the regulatory responsible operator to plug the wells.

⁵ Complaint Letter

⁶ Exhibit A-1, Addendum to M. W. Balch Lease Agreement

⁷ Transcript, Page 14, lines 8-14

⁸ Transcript, Page 31, lines 23-25 and Page 32, lines 1-3

⁹ Transcript, Page 44, lines 21-25 and Page 45, lines 1-12

Jurisdiction and Notice

Sections 81.051 and 81.052 of the Texas Natural Resources Code provide the Commission with jurisdiction over all persons owning or engaged in drilling or operating oil or gas wells in Texas, and the authority to adopt all necessary rules for governing and regulating persons and their operations under the jurisdiction of the Commission.

On February 8, 2018, the Hearings Division of the Commission sent a Notice of Hearing (“Notice”) to Complainant and Respondent setting a hearing date of March 21, 2018. Consequently, all parties received more than 10 days’ notice. The Notice contains: (1) a statement of the time, place, and nature of the hearing; (2) a statement of the legal authority and jurisdiction under which the hearing is to be held; (3) a reference to the particular sections of the statutes and rules involved; and (4) a short and plain statement of the matters asserted.¹⁰ The hearing was held on March 21, 2018, as noticed. Complainant and Respondent appeared at the hearing.

Applicable Legal Authority

Complainant alleges the Commission’s current operator of record, Respondent, does not have a good faith claim to operate the Lease. A “good faith claim” is defined in the Texas Natural Resources Code and in Commission rule as:

A factually supported claim based on a recognized legal theory to a continuing possessory right in the mineral estate, such as evidence of a currently valid oil and gas lease or a recorded deed conveying a fee interest in the mineral estate.¹¹

Statewide Rule 15 provides the requirements for inactive wells.¹² An inactive well is defined as:

An unplugged well that has been spudded or has been equipped with cemented casing and that has had no reported production, disposal, injection, or other permitted activity for a period of greater than 12 months.¹³

Statewide Rule 15 requires the plugging of inactive wells. Statewide Rule 15(d) states:

(d) Plugging of inactive land wells required.

¹⁰ See TEX. GOV’T CODE §§ 2001.051, 052; 16 TEX. ADMIN. CODE §§ 1.42, 1.45.

¹¹ TEX. NAT. RES. CODE § 89.002(11); 16 TEX. ADMIN. CODE § 3.15(a)(5).

¹² Statewide Rule 15 refers to 16 TEX. ADMIN. CODE § 3.15.

¹³ 16 TEX. ADMIN. CODE § 3.15(a)(6).

- (1) An operator that assumes responsibility for the physical operation and control of an existing inactive land well must maintain the well and all associated facilities in compliance with all applicable Commission rules and orders and within six months after the date the Commission or its delegate approves an operator designation form must either:
 - (A) restore the well to active status as defined by Commission rule;
 - (B) plug the well in compliance with a Commission rule or order;
or
 - (C) obtain approval of the Commission or its delegate of an extension of the deadline for plugging an inactive well.¹⁴

So for an inactive well, an operator must plug it, obtain a plugging extension, or restore it to active status.

Statewide Rule 15(e) allows plugging extensions only if five specified criteria are met as follows:

- (1) the Commission or its delegate approves the operator's Application for an Extension of Deadline for Plugging an Inactive Well (Commission Form W-3X);
- (2) the operator has a current organization report;
- (3) the operator has, and on request provides evidence of, a good faith claim to a continuing right to operate the well;
- (4) the well and associated facilities are otherwise in compliance with all Commission rules and orders; and
- (5) for a well more than 25 years old, the operator successfully conducts and the Commission or its delegate approves a fluid level or hydraulic pressure test establishing that the well does not pose a potential threat of harm to natural resources, including surface and subsurface water, oil, and gas.¹⁵

Thus, absent a good faith claim to operate, wells are not eligible for extensions to the plugging requirements in Statewide Rule 14 and 15 according to Statewide Rule 15(e).

¹⁴ 16 TEX. ADMIN. CODE § 3.15(d).

¹⁵ 16 TEX. ADMIN. CODE § 3.15(e).

Texas Natural Resource Code § 89.002 defines how and when an operator assumes regulatory responsibility of a well and how and when an operator ceases to be the regulatory responsible operator. Texas Natural Resource Code § 89.002(a)(2) states:

“Operator” means a person who assumes responsibility for the physical operation and control of a well as shown by a form the person files with the commission and the commission approves. [***] In the event of a sale or conveyance of an unplugged well or the right to operate an unplugged well, a person ceases being the operator for the purpose of Section 89.011 only if the well was in compliance with commission rules relating to safety or the prevention of pollution at the time of the sale or conveyance and once the person who acquires the well or right to operate the well:

(A) specifically identifies the well as a well for which the person assumes plugging responsibility on forms required and approved by the commission;

(B) has a commission-approved organization report as required by Section 91.142;

(C) has a commission-approved bond, letter of credit, or cash deposit under Sections 91.103-91.107 covering the well; and

(D) places the well in compliance with commission rules.¹⁶

Statewide Rule 58 states the required form and process for becoming the regulatory responsible operator of a well.¹⁷ Statewide Rule 58(a)(1) states:

Each operator who seeks to operate any well subject to the jurisdiction of the Commission shall file with the commission’s Austin office a commission form P-4 (certificate of compliance and transportation authority) for each property on which the wells are located [***].¹⁸

In sum, if the Wells are inactive, they must be plugged or have plugging extensions. If Respondent does not have a good faith claim to operate the Wells, then it is not eligible for plugging extensions. If Respondent and Complainant have not filed and had approved a Commission Form P-4 transferring the Lease to Complainant, then Respondent remains the regulatory responsible operator of the Lease and Wells. In that case, an order for Respondent to plug the Wells is warranted.

¹⁶ TEX. NAT. RES. CODE § 89.002(a)(2).

¹⁷ Statewide Rule 58 refers to 16 TEX. ADMIN. CODE § 3.58.

¹⁸ 16 TEX. ADMIN. CODE § 3.58(a)(1).

Discussion of Evidence

Complainant had no witness other than himself and offered two exhibits. Respondent provided testimony of one witness and offered one exhibit.

Summary of Complainant's Evidence and Argument

Knapp asserts North Texas does not have a good faith claim, the wells are inactive and should be plugged by North Texas. Knapp provided a copy of the Addendum to M. W. Balch Lease Agreement executed October 27, 2015 ("2015 Agreement").

Knapp, who brought the complaint on behalf of himself as the land and mineral owner, testified about the execution of the 2015 Agreement which terminated the mineral lease. He also testified that there has been no production since 2015. His understanding is that the mineral lease has terminated and that he does not, and cannot, have any regulatory or plugging responsibility for any wells on the Lease because he has never been an operator, a fact he verified by consulting with Blaine Rabel at the Commission.¹⁹

Summary of Respondent's Evidence and Argument

Kevin Jones, the CEO of North Texas testified that North Texas had agreed to the termination of the lease following many issues with Knapp concerning access to the property, but that the plugging and regulatory responsibility for the wells on the Lease was contractually transferred to Mr. Knapp by the 2015 Agreement.²⁰ The 2015 Agreement states in part:

4. An amount of \$5000 shall be paid to Keith Knapp and no further obligation shall be owed. With this agreement, the M. W. Balch shall be terminated (null and void) and NTE is no longer responsible for any and all requirements and/or covenants, express or implied contained within the Lease.²¹

Examiners' Analysis

The issues before the Commission are whether North Texas holds a good faith claim to a continuing right to operate the Lease and if not, should be ordered to plug the Wells in accordance with Statewide Rule 14.

The Commission's authority to determine a good faith claim arises from the *Magnolia* case. In discussing the Commission's authority to grant a drilling permit, the

¹⁹ Transcript, Pages 18-19

²⁰ Transcript, Page 32, Lines 7-23

²¹ Exhibit A-1, Addendum to M. W. Balch Lease Agreement, Section 4.

Texas Supreme Court stated, "The function of the Railroad Commission in this connection is to administer the conservation laws. When it grants a permit to drill a well it does not undertake to adjudicate questions of title or rights of possession. These questions must be settled in the courts."²² The Court concluded, "Of course, the Railroad Commission should not do the useless thing of granting a permit to one who does not claim the property in *good faith*."²³

In the context of the right to continue operation of a lease, the Commission looks to the operator's lease and the production history from the Lease. In this case, the parties agree that the operator's lease terminated in October 2015, by written agreement. North Texas does not claim any interest in the Lease and does not dispute that the Lease has not produced since 2014.²⁴

Tex. Nat. Res. Code § 89.002 and Statewide Rule 58 provide that an operator remains the regulatory responsible operator until such time a Commission Form P-4 to transfer the lease is approved by the Commission. In this case, Respondent is the current operator of record for the Wells and Lease. No other operator has filed a Commission Form P-4 and no subsequent Commission Form P-4 has been approved. Consequently, Respondent continues to be responsible for regulatory compliance on the Lease and Wells. Respondent's contractual arrangements are immaterial as to this point.

The ALJ finds, that while there may be uncertainty and/or disagreement as to the intent of the parties under the 2015 Agreement the applicable statute and rules are clear as to who has the regulatory responsibility to plug the wells. Anything further is a contractual matter between the parties and is beyond the jurisdiction of the Commission to interpret.²⁵

The evidence presented clearly establishes that North Texas holds no good faith claim and should be ordered to plug the Wells and abandon the Lease in accordance with Statewide Rule 14.

Recommendation, Proposed Findings of Fact and Proposed Conclusions of Law

Based on the record in this case and evidence presented, the Examiners recommend the Commission find that North Texas Energy, Inc. does not have a good faith claim and order the Wells/Lease plugged and abandoned in accordance with

²² Magnolia Petroleum Co. v. Railroad Commission, 170 S.W. 2d 189, 191 (Tex. 1943)

²³ Id. At 191 (emphasis added).

²⁴ Transcript, Page 18, lines 15, 16

²⁵ Magnolia Petroleum Co. v. Railroad Commission, 170 S.W. 2d 189, 191 (Tex. 1943)

Statewide Rule 14. The Examiners recommend the Commission adopt the following Findings of Fact and Conclusions of Law.

Findings of Fact

1. On or about December 5, 2017, Keith Knapp filed with the Commission a written complaint alleging that North Texas Energy, Inc. (Operator No. 614190) did not hold a good faith claim to operate the Balch, M. W. (08171) Lease, Well Nos. 1, 2, 3, 4, 6, 7, 10, 11, 12, 13, 14, and Well No. 18 (Drilling Permit No. 805487), Minerva-Rockdale Field, Milam County, Texas.
2. Keith Knapp is a surface and mineral owner.
3. Keith Knapp does not hold, and has never held, a valid Commission Form P-5 *Organization Report* with the Commission.
4. By letter mailed December 11, 2017, North Texas Energy, Inc. was notified of the Complaint.
5. North Texas Energy, Inc. requested a hearing on the merits.
6. On February 8, 2018, the Hearings Division of the Commission sent a Notice of Hearing ("Notice") via first-class mail to Keith Knapp and North Texas Energy, Inc. setting a hearing date of March 21, 2018. The Notice contains: (1) a statement of the time, place, and nature of the hearing; (2) a statement of the legal authority and jurisdiction under which the hearing is to be held; (3) a reference to the particular sections of the statutes and rules involved; and (4) a short and plain statement of the matters asserted. The hearing was held on March 21, 2018. Consequently, all parties received more than 10 days' notice. Complainant and Respondent appeared at the hearing.
7. North Texas Energy, Inc. has an active-ext Commission Form P-5 *Organization Report* with a cash deposit of \$50,000.00 as its financial assurance on file with the Commission.
8. North Texas Energy, Inc. designated itself to the Commission as the operator of the Balch, M. W. (08171) Lease, Well Nos. 1, 2, 3, 4, 6, 7, 10, 11, 12, 13, and 14, Minerva-Rockdale Field, Milam County, Texas, effective July 22, 2013, approved July 31, 2013. Respondent remains the operator of record for the Lease and Wells.
9. There has been no reported production from the Lease since December 2014.
10. North Texas Energy, Inc. designated itself to the Commission as the operator of the Balch, M. W. Lease, Well No. 18 (Drilling Permit No. 805487) Minerva-Rockdale Field, Milam County, Texas, by filing a Commission Form W-1 *Application for Permit to Drill, Recomplete, or Re-Enter*, submitted April 10, 2015,

approved April 28, 2015. The well was drill, not completed and not plugged. Respondent remains the operator of record for the Well.

11. North Texas Energy, Inc. claims no interest in the Lease or Wells.
12. The parties agree that the Addendum to M. W. Balch Lease Agreement executed October 27, 2015, terminated the lease.
13. A good faith claim is defined in Commission Statewide Rule 15(a)(5) as “a factually supported claim based on a recognized legal theory to a continuing possessory right in the mineral estate, such as evidence of a currently valid oil and gas lease or a recorded deed conveying a fee interest in the mineral estate.” [16 TEX. ADMIN. CODE § 3.15(a)(5)].
14. Operator is defined as a person who assumes responsibility for the physical operation and control of a well as shown by a form the person files with the commission and the commission approves. [TEX. NAT. RES. CODE § 89.002(a)(2).]

Conclusions of Law

1. Proper notice of hearing was timely issued to appropriate persons entitled to notice. See, e.g., TEX. GOV'T CODE §§ 2001.051, 052; 16 TEX. ADMIN. CODE §§ 1.42, 1.45.
2. The Commission has jurisdiction in this case. See, e.g., TEX. NAT. RES. CODE § 81.051.
3. It is undisputed that the existing lease between the parties terminated on October 27, 2015, by written agreement.
4. North Texas Energy, Inc. does not have a good faith claim to operate the Balch, M. W. (08171) Lease, Well Nos. 1, 2, 3, 4, 6, 7, 10, 11, 12, 13, 14, and Well No. 18 (Drilling Permit No. 805487), Minerva-Rockdale Field, Milam County, Texas.
5. North Texas Energy, Inc., as the regulatory operator of the Balch, M. W. (08171) Lease, Well Nos. 1, 2, 3, 4, 6, 7, 10, 11, 12, 13, 14, and Well No. 18 (Drilling Permit No. 805487), Minerva-Rockdale Field, Milam County, Texas, has the plugging obligation.

Recommendations

The Administrative Law Judge and Technical Examiner recommend the Commission find that North Texas Energy, Inc. does not have a good faith claim to operate the Balch, M. W. (08171) Lease, Well Nos. 1, 2, 3, 4, 6, 7, 10, 11, 12, 13, 14, and Well No. 18 (Drilling Permit No. 805487), Minerva-Rockdale Field, Milam County, Texas and Order North Texas Energy, Inc. to plug the Wells and abandon the Lease in accordance with Statewide Rule 14.

Respectfully Submitted,



Kristi Reeve
Administrative Law Judge



Robert Musick, P.G.
Technical Examiner