



RAILROAD COMMISSION OF TEXAS

HEARINGS DIVISION

OIL AND GAS DOCKET NO. 08-0314977

COMPLAINT OF EMMETT A. WILLIAMS THAT PENNANT DEVELOPMENT AND PRODUCTION, LLC (OPERATOR NO. 651797), FINLEY RESOURCES INC. (OPERATOR NO. 268602) AND DIAMONDBACK E&P, LLC (OPERATOR NO. 217012) DO NOT HAVE A GOOD FAITH CLAIM TO OPERATE THE KEARNEY, MARTIN (20440) LEASE, WELL NOS. 2 AND 116, WORSHAM (DELAWARE SAND) FIELD, REEVES COUNTY, TEXAS

AMENDED PROPOSAL FOR DECISION

HEARD BY: Clayton Hoover, Administrative Law Judge
Robert Musick, P.G., Technical Examiner

WRITTEN BY: Kristi M. Reeve, Administrative Law Judge

PROCEDURAL HISTORY:

Complaint Filed -	September 17, 2018
Response Filed -	October 17, 2018
Notice of Hearing -	December 12, 2018
Hearing Date -	January 7, 2019
Transcript Received and Record Closed -	January 16, 2019
Proposal for Decision Issued -	September 23, 2019
Amended PFD Issued -	October 10, 2019

APPEARANCES:

For Complainant Emmett A. Williams –
Mike Brothers
Dorothy Brothers

For Respondents Pennant Development and Production, LLC, Finley Resources Inc., and Diamondback E&P, LLC –
Kelli Kenney, Attorney
Paul Tough, Attorney
Marc Dingler, Deputy General Counsel, Diamondback E&P, LLC
Andrew Waller, Landman, Diamondback E&P, LLC

Table of Contents

I.	Statement of the Case	3
II.	Jurisdiction and Notice	4
III.	Applicable Legal Authority.....	4
IV.	Discussion of Evidence.....	6
	Summary of Complainant's Evidence and Argument.....	6
	Summary of Respondent Operators' Evidence and Argument.....	7
V.	Examiners' Analysis	8
VI.	Recommendation, Proposed Findings of Fact and Proposed Conclusions of Law	9

I. Statement of the Case¹

Emmett A. Williams (“Williams”) filed a complaint (“Complaint”) with the Commission claiming no operator has a good faith claim to a continuing right to operate the Kearney, Martin (20440) Lease, Well Nos. 2 and 116, in the Worsham (Delaware Sand) Field, in Reeves County, Texas (“Lease”). Specifically, Williams alleges the underlying contractual lease has expired by its own terms. Williams listed the following three operators in the Complaint: Pennant Development and Production, LLC, Finley Resources Inc., and Diamondback E&P, LLC (collectively, “Respondent Operators”). In response to the complaint, Respondent Operators requested a hearing on the merits.

Williams asserts no operator has a perpetual possessory right to a mineral estate. It is Williams opinion that all the recorded deeds reference an expired document; that Respondent Operators are playing a shell game with their production; that there's speculation on the holdings; and that they're not producing minerals. Williams further argues that a lessee under the oil and gas lease has an implied covenant to re-contemplate, develop and produce those minerals.²

Respondent Operators contend they are the current lessees and operators of the tract where the Lease is located in Section 16 in Reeves County, Texas. Respondent Operators state Williams is basing its argument on a 1957 lease from Martin Kearney, which covers the east 280 acres of the Section. Respondent Operators point out that in the 1960s the entire section was pooled, with drilling and production in this location anywhere from the very early 1960s to present day. Respondent Operators assert the mineral lease has been held by continuous production on this section.³

Pennant Development and Production, LLC (“Pennant”) is the regulatory responsible operator of the Lease. On September 17, 2018, ALJ Hoover sent a letter to Pennant and Williams regarding Williams’ Complaint. Counsel for Respondent Operators included Finley Resources Inc. and Diamondback E&P, LLC in its answer, as all are operating under the same pooled lease. However, the sole issue before the Commission is whether Pennant has a good faith claim to operate the Lease, as the term is defined in Statewide Rule 15.

The Administrative Law Judge and Technical Examiner (collectively “Examiners”) respectfully submit this Proposal for Decision (“PFD”) and recommend the Railroad Commission of Texas (“Commission”) find record evidence demonstrates that Williams failed to carry the required burden of proof to show by a preponderance of the evidence that the mineral lease has terminated. Respondent Operators, on the other hand, provided a reasonably satisfactory showing of a good faith claim to operate the Lease. It is recommended that the Commission deny Williams’ request and dismiss the Complaint.

¹ The hearing transcript in this case is referred to as “Tr. at [page:line].” Complainant’s exhibits are referred to as “Complainant Ex. [exhibit no].” Respondent’s exhibits are referred to as “Respondent Ex. [exhibit no].”

² Tr. at 11:10 to 11:18.

³ Tr. at 12:15 to 13:23.

II. 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 December 12, 2018, the Hearings Division of the Commission sent a Notice of Hearing (“Notice”) to Williams and Respondent Operators setting a hearing date of January 7, 2019. Consequently, the 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.⁴ The hearing was held on of January 7, 2019, as noticed. Williams and Respondent Operators appeared and participated at the hearing.

III. Applicable Legal Authority

Williams alleges the Commission’s current operator of record, Pennant, 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.⁵

The applicable Commission rule in this case is Statewide Rule 15 (or “Rule 15”), which provides inactive well requirements.⁶ 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.⁷

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

(d) Plugging of inactive land wells required.

(1) An operator that assumes responsibility for the physical operation and control of an existing inactive land well must maintain the well

⁴ See Tex. Gov’t Code §§ 2001.051, 052; 16 Tex. Admin. Code §§ 1.42, 1.45.

⁵ Tex. Nat. Res. Code § 89.002(11); 16 Tex. Admin. Code § 3.15(a)(5).

⁶ Statewide Rule 15 refers to 16 Tex. Admin. Code § 3.15.

⁷ 16 Tex. Admin. Code § 3.15(a)(6).

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.⁸

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

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.⁹

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).

⁸ 16 Tex. Admin. Code § 3.15(d).

⁹ Emphasis added.

IV. Discussion of Evidence

Summary of Complainant's Evidence and Argument

Williams, who brought this complaint to Pennant's good faith claim, asserts that the Lease has expired from lack of production and/or pursuant to the terms thereof. Williams presented the oral testimony of Mike Brothers to this effect.

Mr. Brothers asserts:¹⁰

1. Each productive depth should be represented by a separate mineral lease and that each lease should contain current requirements beyond a royalty rates, such as a Pugh Clause, depth parameter, an expiration date and production deadline with delay rentals;
2. Today's technologies and associated discoveries of these now producible minerals are "being held hostage by a lease from 1957, from the middle of the last century; that the depths now available to produce did not exist then and, therefore they should be addressed and assigned with a new lease created;"¹¹
4. The "various leases have been bought, sold, speculated, borrowed against and generally profited in the millions of dollars. It's entirely unjust and should, after all this activity and monetary exclusion on our part be terminated;"¹²
5. "The lease was not in the lessor's favor at its inception;"¹³ and
6. "Pennant's production has dropped to under 10 barrels a month for more than five years. It couldn't possibly be profitable in any way, shape or form. Finley's production has dropped 90 to 95 percent in the last two years. They're the only two operators that are currently producing any minerals on this land, and Diamondback has not yet begun production."¹⁴

In conclusion, Mr. Brothers stated, "We ask the Commission to terminate this lease document and allow us to do business in the 21st century."¹⁵

¹⁰ Tr. at 80:23-83:22.

¹¹ Tr at 81:8-12.

¹² Tr. at 82:16-20.

¹³ Tr. at 83:1-2.

¹⁴ Tr. at 83:4-11.

¹⁵ Tr. at 83:20-22.

Summary of Respondent Operators' Evidence and Argument

In support of Respondent Operators' argument that Pennant has a good faith claim to operate the Lease, Respondent Operators presented twenty-four (24) exhibits through its witness, Mr. Andrew Waller, Land Manager, Delaware Basin with Diamondback E&P, LLC. Respondent Operators' exhibits consisted of the following:¹⁶

1. Map of Section 16 with cold and gridlines to designate Martin Kearney Lease and the Unit and Pooling Agreement;
2. Map of Section 16 without gridlines, showing wells operated by Respondent Operators;
3. Oil Proration Schedule for the Worsham (Delaware Sand) Field;
4. Gas Proration Schedule for the Worsham-Bayer (Atoka) Field;
5. Oil, Gas and Mineral Lease dated June 28, 1957 by Martin Kearney as Lessor to El Paso Natural Gas Company, the east 280 acres of Section 16, Block C-4, PSL survey, with a primary term of 5 years, a 60-day rework clause, and with the ability to pool the lease with other lands and any production on the pooled acreage being treated as production of the lease;
6. Designation of Unit and Pooling Agreement executed by the parties beginning June 10, 1966 to June 20, 1966 and the Texas General Land Office on July 28, 1966, effective August 16, 1966;
7. Lease Amendment to the Oil, Gas and Mineral Lease dated June 28, 1957, between Martin Kearney and Mobile Oil Corporation (the current owner and holder of the 1957 Lease), amending paragraph 3B of the 1957 Lease;
8. Commission Form 2 *Well Record* for the Martin Kearney Lease, Well No. 116, filed December 1960;
9. Commission Form W-2 *Oil Well Potential Test Completion or Recompletion Report and Log* for the Martin Kearney Lease, Well No. 116, reclass, filed February 1967;
10. Commission Form *Gas Well Production Report* for the Martin Kearney Lease, Well No. 116 showing monthly production reported for January 1961 to April 1965 and annual reports by month from December 1966 through 1992;
11. Commission Online System Oil & Gas Production Data Query from January 1993 to December 2018 for the Martin Kearney Lease;
12. Commission Online System Oil & Gas Data Query showing the Finely Resources, Inc. Monsanto-McKellar Unit Lease, Well No. 1L (Gas Id No. 040630) and Monsanto McKellar Unit Lease, Well No. 1U (Gas Id No. 198854) completed in the Worsham-Bayer (Ellenburger) Field;
13. Commission Form 2 *Well Record* for the Monsanto-McKellar Unit, Well No. 1 (Gas Id No. 040630), filed December 1966;
14. Annual Production records for the Monsanto-McKellar Unit from June 1967 to December 1992;
15. Commission Online System Oil & Gas Production Data Query from January 1993 to October 2018 for the Monsanto-McKellar Unit;

¹⁶ Respondent Operators Ex. 1-24.

16. Commission Form G-1 *Gas Well Back Pressure Test, Completion or Recompletion Report, and Log* for the Monsanto-McKeller Unit, Well No. 1U, initial potential, filed April 2003;
17. Internal production reports of Finely Resources, Inc. for the c Unit 1U and 2H showing noncontinuous production from January 2003 to December 2017;
18. Commission Online System Oil & Gas Production Data Query from January 1993 to October 2018 for the Monsanto-McKeller Unit, Well No. 1U, showing continuous production from January 2003 to September 2017;
19. Commission Form G-1 *Gas Well Back Pressure Test, Completion or Recompletion Report, and Log* for the Monsanto-McKeller Unit, Well No. 2H, filed May 5, 2004;
20. Commission Online System Oil & Gas Production Data Query from January 1993 to October 2018 for the Monsanto-McKeller Unit, Well No. 2H showing continuous production from March 2003 to October 2018;
21. Assignment and Bill of Sale dated March 6, 2006, assignment Pennant is currently operating under;
22. Assignment and Bill of Sale dated April 13, 2010, assignment Finley is currently operating under;
23. Assignment, Bill of Sale and Conveyance dated October 1, 2015, assignment Finley is currently operating under; and
24. Assignment and Bill of Sale dated July 1, 2016, assignment Diamondback is currently operating under.

Mr. Waller stated the original mineral lease does not include any language regarding depth [as to production formation].¹⁷ Mr. Waller testified that in his opinion the mineral lease is still in effect and there has been continuous production to support that the lease is in effect and in its secondary term.¹⁸

V. Examiners' Analysis

The sole issue before the Commission is whether Pennant holds a good faith claim to a continuing right to operate the Lease. Respondent Operators appeared together, as the mineral lease in question is part of the foundation of their good faith claims to their leases. Statewide Rule 15(a)(5) defines good faith claim 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.

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 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

¹⁷ Tr. at 61:4-21.

¹⁸ Tr. at 60-61.

undertake to adjudicate questions of title or rights of possession. These questions must be settled in the courts.”¹⁹ 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.”²⁰

Respondent Operators presented documentary evidence and testimony to show that: (1) oil production began during the primary term and continued thereafter; (2) the pooled unit was properly formed by designation filed with the County Clerk in Reeves County; (3) that there has been continuous production since the completion of the original oil well in 1960 and has continued through the formation of such unit for deep gas production; (4) that the relevant Lease identified by Williams was included and properly described; and (5) that such Lease has been extended to the present and remains in effect as a result of continuous production.²¹

Williams’ testimony failed to refute the assertions made and evidence presented by Respondent Operators as to Pennant’s good faith claim to operate the Lease. Williams contended that the mineral lease had expired by virtue of lack of production and/or by its terms. However, no defect in title was established and Texas does not invalidate leases based on age of the contract and the advances in technology.²² It is well established in Texas that operations and production anywhere on a pooled unit will be considered as if the production or operations took place on each of the leases included in the unit for purposes of extending such leases in their secondary term.²³

For these reasons, the Examiners recommend the Commission dismiss Williams’ complaint.

VI. Recommendation, Proposed Findings of Fact and Proposed Conclusions of Law

Based on the record and evidence presented, the Examiners recommend that the Commission deny the relief requested in Williams’ complaint, find that Pennant provided a reasonably satisfactory showing of a good faith claim to operate the Lease, and adopt the following findings of fact and conclusions of law.

Findings of Fact

1. On or about September 10, 2018, Williams filed with the Commission a written complaint (“Complaint”) alleging that Pennant Development and Production, LLC

¹⁹ *Magnolia Petroleum Co. v. Railroad Commission*, 170 S.W. 2d 189, 191 (Tex. 1943).

²⁰ *Id.* at 191.

²¹ See Respondent Exhibits 1 through 24.

²² See *Magnolia Petroleum Co. v. Connellee*, 11 S.W.2d 158, 161–62 (Tex. Comm’n App. 1928) stating, “The fact that scientific progress and development has made possible a greater and more profitable utilization of casinghead gas than existed at the time the lease was executed is no ground for avoiding the plain terms of the contract by which lessee purchased the casinghead gas. This advantage was one which lessee has bought and paid for.”

²³ Smith and Weaver, Texas Law of Oil and Gas, Section 4.8.

("Pennant") did not hold a good faith claim to operate the Kearney, Martin (20440) Lease, Well Nos. 2 and 116, Worsham (Delaware Sand) Field, Reeves County, Texas.

2. By letter from the Administrative Law Judge on September 10, 2018, Pennant was notified of the Complaint.
3. Pennant, Finley Resources Inc. and Diamondback E&P, LLC requested a hearing on the merits ("Respondent Operators").
4. A Notice of Hearing was issued December 12, 2018.
5. The Hearing on the Merits was held on January 7, 2019.
6. Respondent Operators presented documentary evidence and testimony to show that: (1) oil production began during the primary term and continued thereafter; (2) the pooled unit was properly formed by designation filed with the County Clerk in Reeves County; (3) that there has been continuous production since the completion of the original oil well in 1960 and has continued through the formation of such unit for deep gas production; (4) that the relevant Lease identified by Williams was included and properly described; and (5) that such Lease has been extended to the present and remains in effect as a result of continuous production.²⁴
7. As defined in 16 Tex. Admin. Code § 3.15(5), a "good faith claim" is "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."²⁵
8. Williams did not present evidence sufficient to establish a factually supported claim.
9. Respondent Operators presented evidence to show Pennant holds a good faith claim right to the Lease.
10. Respondent Operators presented evidence sufficient to establish a factually supported claim based on a recognized legal theory to a continuing possessory right in the mineral estate in and under the subject tracts of land included within the Lease.

Conclusions of Law

1. Proper notice of hearing was timely issued to persons entitled to notice. *See, e.g.*, Tex. Gov't Code §§ 2001.051, 052; 16 Tex. Admin. Code §§ 1.42, 1.45.

²⁴ *Id.*

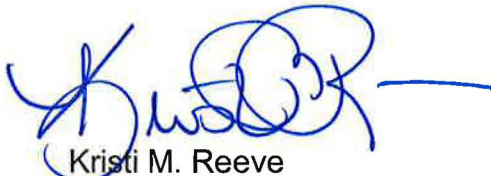
²⁵ 16 Tex. Admin. Code § 3.15(5).

2. The Commission has jurisdiction in this case. See, e.g., Tex. Nat. Res. Code § 81.051.
3. Respondent Operators provided a reasonably satisfactory showing that Pennant has a good faith claim to operate the Kearney, Martin (20440) Lease, Well Nos. 2 and 116, Worsham (Delaware Sand) Field, Reeves County, Texas.
4. Williams' request for relief should be denied.

Recommendation

The Administrative Law Judge and Technical Examiner recommend the Commission dismiss the Complaint brought by Complainant against Respondent.

Respectfully Submitted,



Kristi M. Reeve
Administrative Law Judge



Robert Musick, P.G.
Technical Examiner