

OIL & GAS DOCKET NO. 7B-0240010

COMMISSION CALLED HEARING ON THE APPLICATION OF ID, INC. TO CONSIDER A SUPERCEDING ORDER TO ELIMINATE THE FINANCIAL ASSURANCE REQUIREMENT ESTABLISHED IN THE FINAL ORDER ISSUED ON APRIL 10, 1989 IN OIL AND GAS DOCKET NOS. 105400 AND 7B-92985 WHICH GRANTED THE PERMIT TO DRILL WELL NO. 1 ON THE P. H. BARNES (25394) LEASE, BROWN COUNTY REGULAR FIELD, BROWN COUNTY, TEXAS

APPEARANCES:

FOR APPLICANT:

James Halek
Aaron Harris

APPLICANT:

ID, Inc.

FOR PROTESTANT:

Harry Witherspoon

PROTESTANT:

Harry Witherspoon

PROPOSAL FOR DECISION

PROCEDURAL HISTORY

DATE OF REQUEST FOR HEARING:

August 19, 2004

DATE CASE HEARD:

October 1, 2004

HEARD BY:

James M. Doherty, Hearings Examiner
Donna Chandler, Technical Examiner

DATE RECORD CLOSED:

October 1, 2004

PFD CIRCULATION DATE:

November 5, 2004

STATEMENT OF THE CASE

On August 19, 2004, ID, Inc., requested a hearing to consider superceding a 1989 Commission final order insofar as it imposed as a condition of the granting of a drilling permit for the P. H. Barnes (25394) Lease, Well No. 1 ("subject oil mine"), Brown County Regular Field, Brown County, Texas, the

filing of a surety bond or other form of financial security in the amount of \$15,000 to ensure that the Commission would not be required to plug the well with state funds.

The current operator of record for the P. H. Barnes (25394) Lease is Central Basin Oil Inv., Inc. However, on May 20, 2004, a Form P-4 (Certificate of Compliance and Transportation Authority) was filed with the Commission requesting that the operator of this lease be changed from Central Basin to ID, Inc. The examiners have officially noticed that the most recent Form P-5 Organization Report filed by Central Basin lists Jason Halek as President. The examiners have also officially noticed that the most recent Form P-5 Organization Report filed for ID, Inc., lists James Halek as President. The evidence shows that James Halek is the father of Jason Halek.

At the time of the Form P-4 filing proposing a change of operator, the subject lease was the subject of a pending enforcement action against Central Basin in Oil & Gas Docket No. 7B-0238809. As a result, the Form P-4 was subjected to good faith claim review in the Commission's Office of General Counsel. On August 19, 2004, a determination was made that ID, Inc., had established a good faith claim. However, this determination notified ID, Inc., of the \$15,000 financial security requirement of the Commission's final order granting the drilling permit for the subject oil mine and that ID, Inc., would be required to file this financial security before the oil mine was transferred. Being dissatisfied with this requirement, ID, Inc., requested this hearing.

A hearing was held on October 1, 2004. James Halek and Aaron Harris appeared to represent ID, Inc., and presented evidence. Harry Witherspoon, the owner of the tract on which the subject oil mine is located, appeared to protest the application, and also presented evidence. At the request of the examiners, Mark England, an engineer in the Field Operations section of the Commission's Oil & Gas Division provided testimony regarding the estimated cost to plug the oil mine.

BACKGROUND

The examiners have officially noticed the examiners' proposal for decision (dated March 16, 1989) and the Commission's Final Order (dated April 10, 1989) in Oil & Gas Docket Nos. 105,400 and 7B-92985; *Application of Coral Petrofenix, Inc., for Exceptions to Statewide Rules 37 and 38 for the Well No. 1, P. H. Barnes Lease, Brown County Regular Field, Brown County, Texas and Also for Oil Mining Authority and A Maximum Efficient Rate for the Above Mentioned Well.*

Findings of Fact adopted by the Commission in the Final Order dated April 10, 1989, stated that Coral Petrofenix proposed to conduct an oil mining operation by augering a 9 ½ foot diameter bore hole to a depth of approximately 130', with 15 radials (laterals), or drainholes, drilled out horizontally into the target oil zone. The 15 radials were proposed to be at three different levels in the reservoir, each level consisting of five radials extending out from the central shaft a distance of 400' to 1,000'.

The Commission's Final Order approved the Coral Petrofenix application, subject to conditions. One such condition stated:

“Prior to the commencement of any operations on this well, the operator Coral Petrofenix, Inc., shall file a surety bond or other form of financial security in the amount of \$15,000, to ensure that the Commission will not have to plug the well with state funds.”

The examiners have also officially noticed the Form W-2 (Oil Well Potential Test, Completion or Recompletion Report and Log) filed by Coral Petrofenix for the subject oil mine on March 2, 1990. The subject oil mine was completed on September 1, 1989. Total depth of the main shaft was reported to be 125'. Surface casing 9 ½ feet in outside diameter was set from the surface to a depth of 62'. Intermediate casing 8 ½ feet in outside diameter was set from 60' to 125'. The completion report indicates that the entire length of the casing was “grouted with cement” and a 3' thick slab was placed in the bottom of the main shaft as a seal.

The examiners have officially noticed Commission Form P-4 records which establish that Coral Petrofenix was the designated operator of the subject lease and oil mine until May 1, 1997, when the operator was changed to Arben Oil, Inc. Effective December 1, 2000, Arben transferred the lease and oil mine to Central Basin Oil Inv., Inc.

The examiners have further officially noticed Commission Form P-5 records which establish that the Form P-5 Organization Report of Central Basin Oil Inv., Inc., has been delinquent since October 2002. Central Basin is the subject of a S.B. 639 flag due to an outstanding violation in Oil & Gas Docket No. 09-0233185, and cannot renew its Form P-5 until this violation is resolved.

The examiners have also officially noticed Commission Form P-4 records establishing that the subject lease was severed on August 3, 2003, based on Central Basin's Form P-5 delinquency. The lease was also severed on February 3, 2004, based on a violation of Statewide Rule 13. These severances have not been resolved.

The examiners have further officially noticed Commission production records establishing that from 1993 to 1997, no production was reported to the Commission for the subject lease and oil mine. The following average monthly production was reported for 1998 to 2004: 1998 - 8.3 BO; 1999 - 3.9 BO; 2000 - 5.2 BO; 2001 - 6.4 BO; 2002 - 5.7 BO; 2003 - 2.0 BO; and 2004 - 0.5 BO. No production has been reported since March 2004. Production was reported for seven months (September 2003 through March 2004) after the subject lease was severed. No disposition of oil from the subject lease has been reported since September 2002.

The examiners have also officially noticed that there is a pending enforcement action against Central Basin in Oil & Gas Docket No. 7B-0238809, wherein violations of Statewide Rules 13 and 16 on the subject lease are alleged. This docket was called for hearing on October 1, 2004, and Central Basin did not appear. At this hearing, the Enforcement Section of the Office of General Counsel announced that the case appeared to have been settled.

DISCUSSION OF THE EVIDENCE

Applicant's Evidence

James Halek testified that ID, Inc., acquired an ownership interest in the production of the subject oil mine from Central Basin and now wishes to become the operator of the mine. ID, Inc., regards the oil mine as a research project that has potential for tertiary recovery. ID, Inc., charges oil molecules in the reservoir with ultrasonic waves, and this process is designed to cause oil to flow into the oil mine.

James Halek asserted that he had no connection with Central Basin other than as an investor. When ID, Inc., decided to attempt to become the designated operator of the subject lease, and of the P. H. Barnes (08680) Lease, it made inquiry as to the amount of financial security that it would be required to file to become operator. Commission staff advised that financial security in the amount of \$2,782 would be required, based on the total depth of the wells which ID, Inc., proposed to acquire, multiplied by two dollars per foot.¹

ID, Inc., objects to being required to file the \$15,000 of financial security for the subject oil mine required by the Commission's 1989 Final Order in Oil & Gas Docket Nos. 105400 and 7B-92985. Notwithstanding the requirements of this Final Order, ID, Inc., does not believe that any of the previous operators of the oil mine actually filed the required \$15,000 of financial security. Even though the annual premium for a \$15,000 bond would be relatively minimal, ID, Inc., does not have cash readily available for this purpose. James Halek testified that his lack of experience in the oil and gas business creates a problem in obtaining a bond, and ID, Inc., is incapable of filing a cash deposit of \$15,000.

James Halek stated that he was unaware of the reasons for imposition of the \$15,000 financial security requirement in the Commission's 1989 Final Order. He asserted also that he did not know what it would cost to plug the subject oil mine. Although he professed not to know whether the subject oil mine penetrates a usable quality water zone, the "energy well" drilled by Central Basin about 75'-80' away was the subject of a Texas Commission on Environmental Quality ("TCEQ") surface casing recommendation

¹ It is not clear that at the time ID, Inc., was given this advice, Commission staff were aware that the subject oil mine was anything other than a conventional oil well. Apparently, Commission staff with whom ID, Inc., had discussions about the amount of required financial security were unaware of the \$15,000 financial security requirement for the subject oil mine provided by the Commission's 1989 Final Order in Oil & Gas Docket Nos. 105400 and 7B-92985. ID, Inc., filed \$2,782 as financial security to cover the subject oil mine and ten conventional shallow wells on the P. H. Barnes (08680) Lease, that ID, Inc. proposed to acquire from Central Basin.

requiring that surface casing be set to a depth of 97' for water protection.

Protestant's Evidence

Harry Witherspoon purchased the tract on which the subject oil mine is located in 2000. He is the owner of the surface and 25% of the minerals. Mr. Witherspoon testified that he had experienced constant problems with the manner in which Central Basin has operated the property, some related to failure to adhere to lease terms and some related to violations of Commission rules. His complaints to Jason Halek and James Halek have not resolved the problems.

Mr. Witherspoon sees no real distinction between Central Basin and ID, Inc. He believes that these companies, or an affiliated entity, have been operating the subject lease without a valid Organization Report for about two years. He objects to modification of the \$15,000 financial security requirement for the subject oil mine based on what he believes is a lack of credibility of the principals of Central Basin and ID, Inc. Mr. Witherspoon stated his understanding that the original operator of the subject oil mine, Coral Petrofenix, filed the required \$15,000 of financial security. Mr. Witherspoon has a nearby water well that encounters usable quality water at a depth of 65'. The base of this usable quality water zone is believed to be at about 93'.

Mark England Evidence

In response to questions from the examiners, Mark England, an engineer in the Field Operations section of the Commission's Oil & Gas Division, testified that in 1993, the Commission was required to use state funds to plug a well in Comanche County that was similar to the subject oil mine. This well was 14' in diameter and 90' deep, but did not penetrate the base of usable quality water. Only a surface plug was required, and total cost to plug the well was \$9,200.

Mr. England also testified that because the subject oil mine is 125' deep and a TCEQ surface casing recommendation for another nearby well says that the base of usable quality water is around 90', it appears that the subject oil mine penetrates the base of usable quality water. Plugging of the well will therefore require a plug at the base of usable quality water as well as a surface plug. If approved API oil well cement is used, plugging the subject oil mine according to the standards of Statewide Rule 14 will cost about \$42,000. Use of alternative materials, if approved by the Commission, could reduce the cost to about \$25,000.

EXAMINERS' OPINION

ID, Inc., is the proponent of an order superceding the Commission's 1989 Final Order in Oil & Gas Docket Nos. 105400 and 7B-92985, insofar as it imposes the \$15,000 financial security requirement for the subject oil mine. As such, ID, Inc., has the burden of proof, and the examiners conclude that ID, Inc., did not sustain this burden.

The only justification argued by ID, Inc., in support of the relief which it seeks is the assertion that previous operators of the subject oil mine did not file the required \$15,000 of financial security. The examiners are unable to confirm this one way or the other, and it is not clear how ID, Inc., would know whether any previous operator, other than Central Basin, filed the required financial security. In any event, the fact that one or more previous operators may have violated the requirement is no justification for eliminating the requirement altogether.

The financial security requirement of the Commission's 1989 Final Order granting the drilling permit for the subject oil mine is a requirement related to prevention of pollution of surface and subsurface water. Usable quality groundwater is at risk of being contaminated by migration or discharge of saltwater or other oil and gas wastes from inactive and unplugged wellbores, which constitute a cognizable threat to the public health and safety. The Commission has the sole responsibility for the control and disposition of waste and the abatement and prevention of pollution of surface and subsurface water resulting from activities associated with the exploration, development, and production of oil or gas pursuant to §26.131 of the Texas Water Code.

Under Section 91.101 of the Texas Natural Resources Code, to prevent pollution of surface water or subsurface water in the state, the Commission is authorized to issue orders and permits relating to: (1) the drilling of oil and gas wells or any purpose in connection with them; and (2) the operation, abandonment, and proper plugging of wells subject to the Commission's jurisdiction. Having the jurisdiction to issue a drilling permit for the subject well, the Commission also had the jurisdiction to condition its issuance on the posting of financial security sufficient to ensure that use of State funds to plug the well would not be necessary, particularly where it appeared that the well was so unique that standard Form P-5 financial security was insufficient. It is clear from the face of the Commission's 1989 Final Order in Oil & Gas Docket Nos. 105400 and 7B-92985 that the \$15,000 financial security requirement was imposed on the subject oil mine "to ensure that the Commission will not have to plug the well with state funds." ID, Inc., made no showing that the purpose for which this requirement was imposed is any less valid today than it was in 1989.

It is doubtful that the financial security requirements of §§91.103-91.1042 of the Texas Natural Resources Code applicable to conventional oil, gas and injection wells contemplated the plugging liability associated with a 9 ½ foot diameter oil mine shaft with multiple laterals. While §91.1041 authorizes the filing of financial security in an amount derived by multiplying the total depth of a well by two dollars per foot, in this particular case the total depth of the oil mine shaft (125') bears no rational relationship to the estimated plugging cost for the oil mine. For this oil mine, ID, Inc., has filed financial security in the amount of \$250, as compared to estimated plugging cost of up to \$42,000. This demonstrates the need to enforce the \$15,000 financial security requirement of the Commission's 1989 Final Order, not a need to supercede it.

ID, Inc., is not compelled to become the operator of the subject oil mine. However, if it elects to pursue the Form P-4 requesting a change of operator from Central Basin to ID, Inc., the Commission has the jurisdiction to condition approval of the Form P-4 change of operator on ID, Inc.'s compliance with

all conditions of the Commission's order granting a permit for the oil mine, including the \$15,000 financial security requirement.

Based on the record in this case, the examiners recommend that the Commission adopt the following Findings of Fact and Conclusions of Law.

FINDINGS OF FACT

1. At least ten (10) days notice of the hearing in this docket was sent to all parties entitled to notice.
2. ID, Inc., has filed with the Commission a Form P-4 (Certificate of Compliance and Transportation Authority) requesting that the operator of the P. H. Barnes (25394) Lease, Well No. 1 ("subject oil mine") be changed from Central Basin Oil Inv., Inc., to ID, Inc.
3. By Final Order signed April 10, 1989, in Oil & Gas Docket Nos. 105400 and 7B-92985, the Commission granted a Rule 37/38 exception permit to drill the subject oil mine, subject to a condition that the operator file financial security for the oil mine in the amount of \$15,000 to ensure that the Commission would not be required to plug the well with state funds.
4. The financial security requirement in the Commission's Final Order signed April 10, 1989, in Oil & Gas Docket Nos. 105400 and 7B-92985 is a requirement related to prevention of pollution of surface and subsurface water. Inactive and unplugged wellbores present a cognizable threat to the health and safety of the public in that they present a risk of pollution of surface and subsurface water through migration or discharge of saltwater or other oil and gas wastes.
5. By this application, ID, Inc., requests that the Commission issue an order superceding the Final Order signed April 10, 1989, in Oil & Gas Docket Nos. 105400 and 7B-92985, insofar as it imposes a \$15,000 financial security requirement for the subject oil mine.
6. The subject oil mine was drilled by augering a 8 ½ to 9 ½ foot mine shaft to a depth of 125' and by drilling 15 laterals off the mine shaft at three different depth levels between 110' and 125'. Some laterals were originally proposed to be 400' in length and others 1,000' in length. Surface casing 9 ½ feet in outside diameter was set from the surface to a depth of 62'. Intermediate casing 8 ½ feet in diameter was set from 60' to 125'. A 3 foot slab was placed in the bottom of the main shaft as a seal. Ultrasonic waves are applied to oil molecules in the reservoir, with the expectation that this will cause oil to flow from the laterals into the mine shaft where it can be pumped to the surface.
7. The subject oil mine was drilled by a previous operator and was completed on September 1, 1989.
8. The subject oil mine has produced a minimal amount of oil since 1993. No production was reported to the Commission from 1993 to 1997. The following average monthly production was reported for 1998 to 2004: 1998 - 8.3 BO; 1999 - 3.9 BO; 2000 - 5.2 BO; 2001 - 6.4 BO;

2002 - 5.7 BO; and 2004 - 0.5 BO. No production has been reported since March 2004. No disposition of oil from the subject lease has been reported since September 2002.

9. The Form P-5 Organization Report for the current designated operator of the subject lease, Central Basin Oil Inv., Inc., has been delinquent since October 2002.
10. The certificate of compliance for the subject lease has been canceled since August 3, 2003, and has not been reissued.
11. The subject lease and oil mine are not currently in compliance with the Commission's rules.
12. ID, Inc., has filed financial security with the Commission in the amount of \$2,782, based on the total depth of the subject oil mine and ten shallow conventional oil wells which ID, Inc., proposes to acquire from Central Basin Oil Inv., Inc., multiplied by two dollars per foot .
13. Calculated at two dollars per foot of total depth, the amount of financial security filed by ID, Inc., attributable to the subject oil mine is \$250.
14. The subject oil mine penetrates the base of a usable quality water zone. When plugged, the subject oil mine will require a plug at the base of the usable quality water zone as well as a surface plug.
15. If approved API oil well cement is used, the estimated cost to plug the subject oil mine is \$42,000. If use of less expensive alternative materials were approved by the Commission, the estimated cost to plug the subject oil mine would be at least \$25,000.
16. ID, Inc., did not submit any evidence establishing that superceding the financial security requirement of the Commission's Final Order signed April 10, 1989, in Oil & Gas Docket Nos. 105400 and 7B-92985 is necessary to prevent waste or protect correlative rights.
17. ID, Inc., did not submit any evidence establishing that conditions have changed materially since issuance of the Commission's Final Order signed April 10, 1989, in Oil & Gas Docket Nos. 105400 and 7B-92985 or that the financial security requirement in the Final Order is no longer necessary to ensure that the subject oil mine will be plugged without the use of state funds.

CONCLUSIONS OF LAW

1. Proper notice of hearing was timely issued by the Railroad Commission to appropriate persons legally entitled to notice.
2. All things necessary to the Commission attaining jurisdiction over the subject matter and the parties to this hearing have been performed or have occurred.
3. Pursuant to §26.131 of the Texas Water Code, the Commission is solely responsible for the control and disposition of waste and the abatement and prevention of pollution of surface and

subsurface water resulting from activities associated with the exploration, development, and production of oil or gas.

4. Pursuant to §91.101 of the Texas Natural Resources Code, to prevent pollution of surface water or subsurface water in the state, the Commission is authorized to adopt and enforce orders and permits relating to: (a) the drilling of oil and gas wells or any purpose in connection with them; and (b) the operation, abandonment, and proper plugging of wells subject to the Commission's jurisdiction.
5. ID, Inc., failed to prove that the justification for the financial security requirement in the Commission's Final Order signed April 10, 1989, in Oil & Gas Docket Nos. 105400 and 7B-92985, which granted the Rule 37/38 exception permit for the P. H. Barnes (25394) Lease, Well No. 1, no longer exists or that conditions have otherwise changed since issuance of the Final Order.
6. ID, Inc., failed to prove that superceding the Commission's Final Order signed April 10, 1989, in Oil & Gas Docket Nos. 105400 and 7B-92985, insofar as it required that the operator of the P. H. Barnes (25394) Lease, Well No. 1, file financial security for the well in the amount of \$15,000, is necessary to prevent waste or protect correlative rights.
7. In the event ID, Inc., becomes the designated operator of the P. H. Barnes (25394) Lease, Well No. 1, it will be subject to the financial security requirement for the said well contained in the Commission's Final Order signed April 10, 1989, in Oil & Gas Docket No. 105400 and 7B-92985.

RECOMMENDATION

The examiners recommend that the application of ID, Inc., in this docket be denied and that the attached final order be entered.

Respectfully submitted,

James M. Doherty
Hearings Examiner

Donna Chandler
Technical Examiner

