



# RAILROAD COMMISSION OF TEXAS

## OFFICE OF GENERAL COUNSEL

OIL & GAS DOCKET NO. 09-0252373

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**APPLICATION OF FINLEY RESOURCES, INC., FOR THE FORMATION OF A UNIT  
PURSUANT TO THE MINERAL INTEREST POOLING ACT FOR THE PROPOSED EAST  
SIDE UNIT, NEWARK, EAST (BARNETT SHALE) FIELD, TARRANT COUNTY, TEXAS**

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**APPEARANCES:**

**FOR APPLICANT:**

Mickey R. Olmstead  
Paul R. Tough  
Wade Chappell  
James Nance

**APPLICANT:**

Finley Resources, Inc.

**FOR INTERESTED PARTY:**

Bill Spencer

**INTERESTED PARTY:**

Chesapeake Operating, Inc.

**PROPOSAL FOR DECISION**

**PROCEDURAL HISTORY**

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| <b>DATE APPLICATION FILED:</b>         | May 14, 2007  |
| <b>DATE APPLICATION SUPPLEMENTED:</b>  | June 20, 2007   |
| <b>DATE OF NOTICE OF HEARING:</b>      | July 19, 2007   |
| <b>DATE OF HEARING:</b>                | August 24, 2007   |
| <b>EXAMINERS ASSIGNED:</b>             | James M. Doherty, Hearings Examiner<br>Marshall Enquist, Hearings Examiner<br>Andres J. Trevino, Technical Examiner |
| <b>DATE CLOSING STATEMENT FILED:</b>   | September 14, 2007  |
| <b>DATE AMICUS CURIAE BRIEF FILED:</b> | January 4, 2008   |
| <b>DATE PFD CIRCULATED:</b>            | May 12, 2008  |

**STATEMENT OF THE CASE**

This is an application filed pursuant to the Mineral Interest Pooling Act (“MIPA”), Texas Natural Resources Code, Chapter 102. This is a rare, if not unique, MIPA case wherein the applicant holding a leasehold interest in a tract or block of acreage large enough to drill a well under the applicable well density rule seeks to use MIPA to force into the applicant’s pooled unit adjacent small tracts of owners unwilling to lease or pool voluntarily, so that the applicant can avoid the need to seek Rule 37 spacing exceptions for its proposed well.<sup>1</sup>

Finley Resources, Inc. (“Finley”) has leased multiple town lots containing a total of 82.9786 acres in the Riverside, Page Company’s East Side, KAB Air, and Kendall Additions in Tarrant County, about one mile from downtown Fort Worth. In the same area, Chesapeake Exploration, LLC has also leased several town lots containing 5.9904 acres, Dale Resources, LLC has leased a lot containing 0.1530 acres, and Dale Property Services, LLC has leased several town lots containing 1.4940 acres. Depending on which of the unit plats presented by Finley is correct, there are about 26 or 28 town lots containing 5.704 acres in the area of interest to Finley which are unleased. Finley has not been able to obtain leases on these 28 lots either because the mineral owners are unwilling to lease or because the mineral owners could not be found. Finley requests that the Commission enter an order pursuant to the MIPA force pooling the leasehold interests of Finley, Chesapeake Exploration, LLC, Dale Resources, LLC, Dale Property Services, LLC, and the interests of the unleased mineral owners into a 96.32-acre force pooled unit. If the application is approved, Finley proposes to drill a horizontal well in the Newark, East (Barnett Shale) Field on the force pooled unit.

The application is unopposed, and Chesapeake Operating, Inc. (“Chesapeake”), supports the Finley application. A hearing was held on August 24, 2007, before examiners Marshall Enquist and Andres J. Trevino. Finley appeared at the hearing and presented evidence, and Chesapeake appeared as an interested party. Finley filed a written closing statement on September 14, 2007, and Chesapeake filed an amicus curiae brief on January 4, 2008, supporting Finley’s position. Examiner James M. Doherty was subsequently assigned to review the record and assist with preparation of this proposal for decision.

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<sup>1</sup> When an applicant for a drilling permit proposes to drill on a pooled unit, the applicant is required to so indicate on the Form W-1 (Application to Drill, Deepen, Plug Back, or Reenter), and file a Form P-12 (Certificate of Pooling Authority) and associated plat. The applicant must indicate on the Form P-12 any undivided unleased and/or non-pooled interest in any tract included in the pooled unit, and the plat must show any unleased and non-pooled “window” tract interior to the pooled unit. If the proposed well is closer to any tract having an unleased and/or non-pooled interest than allowed by the applicable well spacing rule, the applicant must apply for a Rule 37 spacing exception, just as in the case of a well drilled closer to a lease or pooled unit boundary than allowed by the applicable well spacing rule.

### APPLICABLE LAW

The MIPA is a limited compulsory pooling statute unique to Texas which has been characterized by scholars as an “act to encourage voluntary pooling” or a “compulsory voluntary pooling act.” Smith and Weaver, *Texas Law of Oil and Gas*, Chapter 12, §12.3(B)(1)(a) at page 12-24 (Matthew Bender 2007). Pursuant to §102.013 of the MIPA, the Commission must dismiss an application for force pooling if it finds that a fair and reasonable offer to pool voluntarily has not been made by the applicant to the owners of other interests in the proposed unit.

Subject to limitations found elsewhere in the act, §102.011 of the MIPA provides that when two or more separately owned tracts of land are embraced in a common reservoir of oil or gas for which the Commission has established the size and shape of proration units, whether by temporary or permanent field rules, and where there are separately owned interests in oil and gas within an existing or proposed proration unit in the common reservoir and the owners have not agreed to pool their interests, and where at least one of the owners of the right to drill has drilled or has proposed to drill a well on the existing or proposed proration unit to the common reservoir, the Commission, on the application of an owner specified in Section 102.012 of the act and for the purpose of avoiding the drilling of unnecessary wells, protecting correlative rights, or preventing waste, shall establish a unit and pool all of the interests in the unit within an area containing the approximate acreage of the proration unit, which unit shall in no event exceed 160 acres for an oil well or 640 acres for a gas well plus 10 percent tolerance.

### DISCUSSION OF THE EVIDENCE

The Newark, East (Barnett Shale) Field was discovered on October 15, 1981. This field has special field rules providing for 330' lease line spacing, and there is no between well spacing requirement. As to horizontal wells, where the horizontal portion of the well is cased and cemented back above the top of the Barnett Shale formation, the distance to any property line, lease line, or subdivision line is calculated based on the distance to the nearest perforation in the well, and not based on the penetration point or terminus. Where an external casing packer is placed in a horizontal well and cement is pumped above the external casing packer to a depth above the top of the Barnett Shale formation, the distance to any property line, lease line, or subdivision line is calculated based on the top of the external casing packer or the closest open hole section in the Barnett Shale.

The standard drilling and proration unit for the Newark, East (Barnett Shale) Field is 320 acres. An operator is permitted to form optional drilling units of 20 acres. Operators must file a Form P-15 (Statement of Productivity of Acreage Assigned to Proration Units) listing the number of acres that are being assigned to each well on the lease or unit for proration purposes. No double assignment of acreage is permitted. While the allocation formula for the field is suspended, operators are not required to file plats of proration units with Form P-15.

Finley is requesting the Commission to approve a force pooled unit, referred to as the East Side Unit, consisting of 96.32 acres out of the B. E. Waller Survey, A-1659, and the R. Cross Survey, A-304, in Tarrant County. The area of the proposed unit is about one mile from downtown Fort Worth and contains 300 to 350 lots. According to Finley, this is a working class, and largely Hispanic, neighborhood.

Finley commenced attempts to obtain oil and gas leases on the lots in the area of interest in 2005. Since that time, Finley has sent letters to lot owners explaining Finley's proposal, held neighborhood meetings at an area hotel and church, and gone door to door to solicit oil and gas leases. As a result of this activity, Finley has obtained oil and gas leases covering 82.9786 acres within the area of the proposed 96.32 acre force pooled unit. Chesapeake Exploration, LLC has also leased several lots containing 5.9904 acres, Dale Resources, LLC has leased a lot containing 0.1530 acres, and Dale Property Services, LLC has leased several lots containing 1.4940 acres. Depending on which of Finley's plats is correct, there are about 26 or 28 lots containing 5.704 acres in the area of interest to Finley which are unleased. Finley has not been able to obtain leases on these lots either because the mineral owners are unwilling to lease or because the mineral owners could not be found. Appendix 1 to this proposal for decision is a copy of Finley Exhibit No. 14, which is a plat of the lots within the proposed East Side Unit color coded to show the particular lots leased by Finley, Chesapeake, and the Dale companies<sup>2</sup>, as well as those lots that are unleased. A Chesapeake Energy landman provided Finley with a letter dated August 23, 2007, stating that Chesapeake desired to participate with its full interest in wells drilled by Finley on the proposed unit and intended to execute a mutually agreeable joint operating agreement covering the proposed unit.

Finley claims that nine of the unleased tract owners within the proposed unit could not be found to discuss whether these owners were willing to lease to Finley. Finley's comments on a tabulation of these "not found" owners indicate either that the lot was "vacant," or there was "no answer" when Finley went door to door, or that a "mean dog" was enough encouragement for Finley's representative to leave his card on the front gate.<sup>3</sup> Finley's tabulation of those tract owners who refused to lease to Finley has Finley's comments that the owners were "not interested," did not answer or could not be found, or decided not to lease. Finley explained that the owners who refused to lease to Finley responded by telling Finley's representative to "get off my property," or stated that they didn't want to sign an oil and gas lease or that they "didn't want to have anything to do with your company, or any company." Finley speculated that the unleased owners likely "were concerned about having to see the rig, having to smell the rig, and having to hear it."

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<sup>2</sup> Finley understands that Dale Resources, LLC has an agreement with Chesapeake pursuant to which Chesapeake purchases leases taken by Dale.

<sup>3</sup> Finley presented copies of 26 receipts for certified mail sent to the unleased owners. These included evidence of receipt of Finley's correspondence by 18 of the unleased owners. Certified mail to 8 of the unleased owners was returned as undeliverable.

In January 2007, Finley mailed a "final offer" to the owners of the lots within the proposed unit that were still unleased, using mailing addresses that Finley had been able to find by internet research of records of the Tarrant County Appraisal District, looking for telephone numbers, door to door canvassing, and neighborhood meetings. The same offer was made to each unleased owner "on a yardstick basis." This offer provided notice that Finley was proposing to form a pooled unit described in an attached Exhibit "A" and drill a horizontal well from a "preexisting drillsite location" off the unit to test the Barnett Shale or to a depth of 7,500', whichever was the lesser depth at an estimated cost of \$3,084,477 as set forth in an attached detailed and itemized statement labeled Exhibit "B".<sup>4</sup> The "final offer" made to the unleased owners by Finley stated the net acreage and "estimated percentage" of the proposed unit attributable to each owner. Finley offered the unleased owners three options: (1) lease their minerals to Finley ("Option 1"); (2) participate in the drilling and completion of the well to be drilled on the unit ("Option 2"); or (3) farmout the owners' minerals to Finley ("Option 3").

Regarding Option 1 (lease), Finley offered a \$2,100 per net acre bonus as an incentive to sign an attached oil and gas lease.<sup>5</sup> The proposed oil and gas lease, in Paragraph 1, provided that the lease was a "no surface use" lease, and the lessee could not conduct any operations on the surface of the leased premises without the express written consent of the lessor. Paragraph 12 of the proposed oil and gas lease provided, however, that "In exploring, developing, producing and marketing oil, gas and other substances covered hereby on the leased premises, in primary or enhanced recovery, Lessor hereby grants and conveys to Lessee the right of ingress and egress along with the right to conduct such operations on the leased premises as may be reasonably necessary for such purposes, including but not limited to geophysical operations, the drilling of wells, and the construction and use of roads, canals, pipelines, tanks, water wells, disposal wells, injection wells, pits, electric and telephone lines, power stations, and other facilities deemed necessary by Lessee to discover, produce, store, treat and transport production."

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<sup>4</sup> Finley Exhibit Nos. 6 and 7 are copies of the "final offer" sent to certain unleased owners. Exhibits "A" and "B" are not attached to these copies of the offer.

<sup>5</sup> It appears from Finley Exhibit No. 9 that the unleased lots range in size from 0.1210 acres to 1.0320 acres. The bonus offered by Finley for a 0.1210 acre lot was thus \$254.10 and the offered bonus for a 1.0320 acre lot was \$2,167.20. The average unleased lot calculated from Exhibit No. 9 is 0.237 acres, for which the offered bonus would have been \$497.70. About 80% of the unleased lots listed on Exhibit No. 9 have 0.1720 acres or less, and the offered bonus for these lots was \$361.20 or less.

The oil and gas lease the unleased owners were asked to sign further provided that the lease would cover accretions and any small strips or parcels of land owned by the lessor contiguous or adjacent to the leased premises and stated the area to be used for the purposes of determining the amount of any rentals or shut-in royalties "whether it actually comprises more or less".<sup>6</sup> The proposed oil and gas lease had a three year primary term, granted Finley the option to extend the primary term for two years for \$100 per acre, and provided that the lease would continue in effect after the primary term as long as production or operations continued on the leased premises or on lands pooled therewith. The proposed lease provided for a 20% royalty, and granted the lessee the right to pool. The lease provided that the leased premises could be pooled for horizontal completions into units of up to 1,000 acres, or in the case of horizontal completions with dual opposing laterals, 2,000 acres.

Option 2 (participation) in Finley's "final offer" to the unleased owners required the owners to pay their proportionate share of all well costs and provide Finley with a notarized statement agreeing to pay these costs on or before the spud date of the proposed well. The offer set forth an estimated amount of costs attributable to each owner (for example, \$9,434.84 for an owner of a 0.3059 acre lot) but cautioned that this cost "could change considerably due to numerous factors faced while drilling, stimulating and completing a well."

Option 3 (farmout) in Finley's "final offer" required that the unleased owner convey to Finley an 80% net revenue interest attributable to the owner's mineral interest and retain an overriding royalty interest of 20%, proportionately reduced to the extent the owner's mineral interest bore to all of the mineral interests in the proposed unit, until payout of all well costs, with the option, at payout, to convert the retained override to a 25% working interest, proportionately reduced.

The Finley offer notified the unleased owners that if the owner selected Option 2 (participation), the owner would be required to pay the proportionate share of drilling costs attributable to the owner within 15 days prior to commencement of actual drilling operations as set forth in a proposed AAPL Form Joint Operating Agreement, otherwise the owner would be subject to non-consent penalties provided in the JOA.

The unleased owners to whom Finley's "final offer" was made were required to make an election of one of the three options within 14 days of the offer and the offer provided that if such an election had not been made within that time by returning a signed copy of the offer to Finley, it would be deemed that the owner did not choose any option, in which case Finley intended to seek compulsory pooling of the owner's interest pursuant to a forced pooling order to be issued by the Railroad Commission pursuant to the MIPA.

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<sup>6</sup> There are streets and alleys within the area of Finley's proposed unit, and Finley believes that under the doctrine of strips and gores, the individual lot owners own the minerals to the middle of these streets and alleys. Assuming this to be true, it is not clear from Finley's offer that the unleased owners were offered anything attributable to their ownership of these "strips and gores".

According to Finley, its "final offer" to the unleased owners was as good, if not better, than the offer made to other owners in the proposed unit who agreed to lease. In 2005, Finley began its leasing activity by offering a \$250 per lot bonus and a 18.75% royalty. In 2006, after it experienced competition for leases, it began to offer a \$300 per lot or \$1,750 per net acre bonus and a 20% royalty. Ultimately, it increased the bonus it was offering to \$2,100 per net acre.

Notice of this hearing was mailed to Chesapeake, Dale, and all of the owners of unleased tracts within the area of Finley's proposed unit at their last known mailing addresses.<sup>7</sup> In addition, notice of the hearing was published in the Fort Worth Star Telegram on July 24, July 31, August 7, and August 14, 2007.

Finley Exhibit No. 16 is a plat of Finley's proposed unit showing the tracts leased by Finley, Chesapeake and Dale, the tracts that remain unleased, and "proposed wellbore paths for developing the pooled unit," showing proposed penetration points and "three possible surface locations." A copy of Exhibit No. 16 is attached to this proposal for decision as Appendix 2. All three "possible" surface locations are off the proposed unit. Chesapeake controls "possible" Location A to the west of the proposed unit and has several wells it wants to drill from a pad at that location. There is no agreement to enable Finley to drill from Location A. Finley controls Location B to the south of the proposed unit, and this is the most likely surface location from which a well on the unit would be drilled. Location C to the east of the proposed unit is, in Finley's opinion, logistically better than Location B, but Finley does not control this location. Finley has been in negotiations with Frost Brothers to obtain a "surface easement" that would permit it to drill from Location C, and if this easement can be obtained, the penetration point and bottom hole orientations shown on Exhibit No. 16 would be reversed, with the lateral sections "approximately the same." According to Finley, operators typically perforate near the end of a lateral and then space out perforations every 200' to 300' all the way across the lateral.

Finley decided on the proposed laterals shown on Exhibit No. 16 based on geology and engineering to maximize access to the natural fractures that exist in the Barnett Shale, which generally trend to the southwest. The proposed laterals shown on Exhibit No. 16 appear to approach near to or actually traverse some of the unleased tracts within the area of Finley's proposed unit.

A number of Barnett Shale wells have been drilled in the area of the proposed unit, with the more heavily developed trend in the Trinity River bottom. All nearby Barnett Shale wells are productive, although not all are currently producing due to lack of pipeline access. The lower Barnett Shale member is the target zone for most wells in the area. A stratigraphic cross section anchored on top of the Barnett Shale shows that the formation is consistent across several miles in the area of Finley's proposed unit. Initial production rates for Barnett Shale wells in this area show productivity along the trend area over several miles. An isopach map prepared from the few logs

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<sup>7</sup> The Commission's hearing file contains nine returned envelopes for notices of hearing marked "Return to Sender/Not Deliverable As Addressed/Unable to Forward."

available, scout tickets, or other available data shows a few thick areas of the lower member of the Barnett Shale, 400' to 500' thick, in the area of Finley's proposed unit, and a thickness of 325' to 350' across the whole area within 2.5 miles of the unit. Barnett Shale wells to the south of the proposed unit have produced to date about 1 BCF each. A structure map of the top of the lower member of the Barnett Shale shows a fairly subtle change in subsea depth over the several miles covered by the map. Finley sees no reason to believe that there are any missing sections of the lower member of the Barnett Shale in the area of its proposed unit and believes that all the acreage in the proposed unit is productive in the Barnett Shale. The Newark, East (Barnett Shale) Field is said to be a common reservoir beneath all of this acreage. Finley projects recovery of about 8 BCF of gas for each of its proposed laterals on the proposed unit.

If the Finley application is approved and production on the proposed unit is obtained, proceeds of production attributable to the owners of unleased tracts will be escrowed and paid when such owners are found. If an unleased owner is never found, proceeds of production attributable to his interest will be "ceded" to the State. Finley requests that in the event the Commission approves the Finley application, the Commission's order provide for payment by the unleased owners within the force pooled unit of a 100% risk penalty. Finley says the risks are mostly mechanical, involving possible problems with the hole while drilling. Finley also proposes that it be designated the operator of the force pooled unit.

According to Finley, it is not likely that it will drill the proposed wells if this application is not approved because of the need to obtain a Rule 37 exception for the location of the proposed laterals near unleased tracts. There are some pathways through the unit area permitting the proposed laterals to be drilled without traversing any unleased tract, but Finley believes that drilling around some of the unleased tracts would be "circuitous."

### **EXAMINERS' OPINION**

The MIPA is a unique act forged by the legislature largely to protect small tract owners and operators in the wake of the *Normanna* decision<sup>8</sup> which invalidated prorationing formulas with large per well allowable factors allowing substantial uncompensated drainage by wells on small tracts. The courts have consistently construed the MIPA as limited in function to protect small tract lessees or owners rather than as a broad act designed to protect correlative rights generally, or as an act allowing large tract lessees or owners more flexibility in development. Thus, the MIPA has been construed to favor small tract owners who are being pooled against their will or who are seeking to muscle-in to a larger unit, and the legislative history of the act virtually mandates this construction. Smith and Weaver, *Texas Law of Oil and Gas*, Vol. 3, Chapter 12, §12.1(B) at page 12-5, §12.3(B) at page 12-38 (Matthew Bender 2007).

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<sup>8</sup> *Atlantic Refining Co. v. Railroad Commission*, 346 S.W.2d 801 (Tex. 1961).

Finley's MIPA application has a different purpose. Finley is the lessee of multiple lots in the neighborhoods known as the Riverside, Page Company's East Side, KAB Air, and Kendall Additions near downtown Fort Worth, containing a total of 82.9786 acres. The Finley oil and gas leases covering these lots permit Finley to pool the separate lots into a pooled unit. Special field rules for the Newark, East (Barnett Shale) Field provide for optional 20 acre drilling units, so that by voluntary pooling, Finley has enough acreage under lease to drill a well or multiple wells. Finley is thus in the class of a "large tract" owner having sufficient acreage to drill, seeking to use the MIPA against small tract owners who are unwilling to lease to Finley, or not interested in or opposed to oil and gas development in the neighborhood, or who assertedly cannot be found, by force pooling their interests into a Finley operated unit so that the need to seek a Rule 37 exception for a proposed horizontal well can be avoided.

The Commission's authority to order compulsory pooling is not unlimited. Pursuant to §102.011 of the MIPA, the Commission is authorized to order compulsory pooling only for the purposes of avoiding the drilling of unnecessary wells, protecting correlative rights, or preventing waste. The examiners recommend denial of the Finley application because Finley did not prove that force pooling into the proposed unit of the interests of the unleased owners of lots in the area of the unit is necessary for any of these purposes.

There is no suggestion in any of Finley's evidence that failure to order compulsory pooling as requested by Finley will necessitate the drilling of unnecessary wells on any of the unleased lots in the area of the proposed unit. Neither did Finley prove that compulsory pooling of the interests of the unleased owners is necessary to protect correlative rights or prevent waste. By virtue of its leases covering lots containing 82.9786 acres, Finley has enough acreage to drill a well or wells, including a horizontal well. There has been no proof by Finley that such a well would not enable Finley to recover its fair share of hydrocarbons from the common reservoir or any proof that failure to force pool the interests of the unleased owners would result in the ultimate loss of hydrocarbons.

Finley did not claim, or prove, that drilling of a horizontal well on the 82.9786 acres that it now has under lease, or on the combined leased acreage of Finley, Chesapeake, and Dale which these operators appear willing to pool voluntarily, would not be possible. The fact that Finley might be required to drill around unleased tracts in the unit area and a Rule 37 exception might be necessary<sup>9</sup>

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<sup>9</sup> In the Newark, East (Barnett Shale) Field, in the case of horizontal wells where the horizontal portion of the well is cased and cemented back above the top of the Barnett Shale formation, the distance to any property line, lease line, or subdivision line is calculated based on the distance to the nearest perforation in the well, not the distance to any portion of the horizontal drainhole from the penetration point to the terminus.

is not a reason to order compulsory pooling of the unleased tracts against the will of the unleased owners.<sup>10</sup> If Finley has the concern that a Rule 37 exception cannot be justified as necessary to protect correlative rights or prevent waste, then for the same reasons, compulsory pooling cannot be ordered under §102.011 of the MIPA, there being no proof that compulsory pooling is required to avoid the drilling of unnecessary wells.

The examiners have found no legislative history to suggest that compulsory pooling was intended to be used, at least in the circumstances presented here, as a substitute for successful leasing activity in residential areas or as a tool to facilitate the pooling of interests of owners who have not been found by reference to internet records of the central appraisal district and area telephone number listings or by door to door canvassing.<sup>11</sup> Neither do we think it appropriate that the MIPA be used by owners having the right and ability to drill on large tracts or large blocks of acreage as a sword to force unwilling small tract owners to lease for the purpose of allowing more flexibility in development, particularly in the absence of evidence that any conservation or correlative rights interest is being served.

Based on the record in this case, the examiners recommend adoption of the following findings of fact and conclusions of law.

#### **FINDINGS OF FACT**

1. Notice of this hearing was mailed to all interested parties at mailing addresses provided by the applicant Finley Resources, Inc. ("Finley"), at least 30 days prior to the hearing date. Envelopes containing the notice of hearing mailed to nine of the owners of unleased tracts within the area of the proposed unit were returned to the Commission marked "Return to Sender/Not Deliverable As Addressed/Unable to Forward."
2. Notice of this hearing was published in the Fort Worth Star Telegram on July 24, July 31, August 7, and August 14, 2007, the first date of such publication being 30 days prior to the hearing date for this application.

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<sup>10</sup> Well location is not typically an issue in MIPA cases. In such cases, the issue is whether compulsory pooling is necessary for the purposes of avoiding the drilling of unnecessary wells, preventing waste, or protecting correlative rights. The MIPA is not a vehicle to guarantee a MIPA applicant already having sufficient acreage to drill more flexibility in development or an optimal location to drill, particularly where it is not shown that compulsory pooling would serve any conservation or correlative rights interest.

<sup>11</sup> Although the examiners do not doubt that Finley mailed its offer to pool voluntarily to all the unleased owners in the area of the proposed East Side Unit at the best addresses that could be found from internet records of the central appraisal district, the receipts for certified mail provided by Finley indicate that 32.1% of the unleased owners may never have received the offer, and returned notices of hearing in the Commission's hearing file indicate that 32.1% may have never received notice of the hearing in this docket other than by publication in the Fort Worth Star Telegram.

3. Finley is requesting the Commission to approve, pursuant to the Mineral Interest Pooling Act, a force pooled unit in the Newark, East (Barnett Shale) Field, referred to as the East Side Unit, consisting of 96.32 acres out of the B. E. Waller Survey, A-1659, and the R. Cross Survey, A-304, in Tarrant County. The area of the proposed unit is about one mile from downtown Fort Worth and contains 300 to 350 lots. The Finley application is not protested, and Chesapeake Operating, Inc., supports the application.
4. Finley has obtained oil and gas leases covering lots containing 82.9786 acres within the area of the proposed 96.32 acre pooled unit. Chesapeake Exploration, LLC has also leased several lots containing 5.9904 acres, Dale Resources, LLC has leased a lot containing 0.1530 acres, and Dale Property Services, LLC has leased several lots containing 1.4940 acres. There are about 26 or 28 lots containing 5.704 acres in the proposed unit which are unleased. Appendix 1 to the proposal for decision, which is incorporated into this finding by reference, is a plat of the proposed unit color coded to show the lots leased to Finley, Chesapeake, and the Dale companies and the lots that are unleased.
5. Finley is advised that Dale Resources, LLC has an agreement with Chesapeake pursuant to which Chesapeake purchases leases taken by Dale. Chesapeake has advised Finley that it desires to participate with its full interest in wells drilled by Finley on the proposed unit and intends to execute a mutually agreeable joint operating agreement covering the proposed unit.
6. Oil and gas leases taken by Finley from the owners of lots containing 82.9786 acres within the proposed unit contain pooling clauses granting to Finley the right to pool these lots into a pooled unit. Finley has the right to form a voluntary pooled unit consisting of 82.9786 acres for the drilling of a well or wells in the Newark, East (Barnett Shale) Field, and Chesapeake appears to be willing to participate in such a unit by contributing at least an additional 5.9904 acres.
7. The Newark, East (Barnett Shale) Field was discovered on October 15, 1981. This field has special field rules providing for 330' lease line spacing, and there is no between well spacing requirement. As to horizontal wells, where the horizontal portion of the well is cased and cemented back above the top of the Barnett Shale formation, the distance to any property line, lease line, or subdivision line is calculated based on the distance to the nearest perforation in the well, and not based on the penetration point or terminus. Where an external casing packer is placed in a horizontal well and cement is pumped above the external casing packer to a depth above the top of the Barnett Shale formation, the distance to any property line, lease line, or subdivision line is calculated based on the top of the external casing packer or the closest open hole section in the Barnett Shale.
8. The standard drilling and proration unit for the Newark, East (Barnett Shale) Field is 320 acres. An operator is permitted to form optional drilling units of 20 acres. Operators must file a Form P-15 (Statement of Productivity of Acreage Assigned to Proration Units) listing

the number of acres that are being assigned to each well on the lease or unit for proration purposes. No double assignment of acreage is permitted. While the allocation formula for the field is suspended, operators are not required to file plats of proration units with Form P-15.

9. The Newark, East (Barnett Shale) Field is a common reservoir underlying all of the tracts within the proposed unit, and all of the acreage in the proposed unit is productive in the Newark, East (Barnett Shale) Field.
10. About nine of the unleased tract owners within the proposed unit could not be found by Finley to discuss whether these owners were willing to lease to Finley. The remaining owners of the unleased tracts within the proposed unit were unwilling to lease to Finley.
11. The unleased tracts within the proposed unit range in size from 0.1210 acres to 1.0320 acres.
12. Finley proposes to drill a horizontal well in the Newark, East (Barnett Shale) Field with two laterals extending from penetration point to terminus west to east across the proposed unit. A plat of the proposed unit showing the proposed location of this well is attached to the proposal for decision as Appendix 2 and is incorporated into this finding by reference.
  - a. There are three "possible" surface locations off the proposed unit.
  - b. Chesapeake controls "possible" Location A to the west of the proposed unit and has several wells it wants to drill from a pad at that location. There is no agreement to enable Finley to drill from Location A.
  - c. Finley controls Location B to the south of the proposed unit, and this is the most likely surface location from which a well on the unit would be drilled.
  - d. Location C to the east of the proposed unit is, in Finley's opinion, logistically better than Location B, but Finley does not control this location. Finley has been in negotiations with Frost Brothers to obtain a "surface easement" that would permit it to drill from Location C, and if this easement can be obtained, the penetration point and bottom hole orientations shown on Appendix 2 would be reversed, with approximately the same lateral sections.
  - e. Finley did not present evidence as to where the proposed laterals would be perforated. Operators typically perforate near the end of a lateral and then space out perforations every 200' to 300' all the way across the lateral.

13. There are pathways through the acreage leased to Finley, Chesapeake, and Dale along which a horizontal well might be drilled without traversing any unleased tract. Finley proposes that the unleased tracts within the proposed unit be force pooled into the unit so that Finley will not be required to request a Rule 37 exception to drill a horizontal well and to avoid circuitry involved in drilling around the unleased tracts.
14. In January 2007, Finley mailed a final offer to the owners of the lots within the proposed unit that were still unleased, using the mailing addresses that Finley had been able to find by internet research of records of the Tarrant County Appraisal District, looking for telephone numbers, door to door canvassing, and neighborhood meetings. This offer provided notice that Finley was proposing to form a pooled unit and drill a horizontal well from a preexisting drillsite location off the unit to test the Barnett Shale or to a depth of 7,500', whichever was the lesser depth. Finley offered the unleased owners three options: (1) lease their minerals to Finley ("Option 1"); (2) participate in the drilling and completion of the well to be drilled on the unit ("Option 2"); or (3) farmout the owners' minerals to Finley ("Option 3").
  - a. Regarding Option 1 (lease), Finley offered a \$2,100 per net acre bonus as an incentive to sign an attached oil and gas lease. The proposed oil and gas lease had a three year primary term, granted Finley the option to extend the primary term for two years for \$100 per acre, and provided that the lease would continue in effect after the primary term as long as production or operations continued on the leased premises or on lands pooled therewith. The proposed lease provided for a 20% royalty, and granted the lessee the right to pool.
  - b. Option 2 (participation) in Finley's final offer to the unleased owners required the owners to pay their proportionate share of all wells costs and provide Finley with a notarized statement agreeing to pay these costs on or before the spud date of the proposed well. The offer set forth an estimated amount of costs attributable to each owner (for example, \$9,434.84 for an owner of a 0.3059 acre lot) but cautioned that this cost could change considerably due to numerous factors faced while drilling, stimulating and completing a well.
  - c. Option 3 (farmout) in Finley's final offer required that the unleased owner convey to Finley an 80% net revenue interest attributable to the owner's mineral interest and retain an overriding royalty interest of 20%, proportionately reduced to the extent the owner's mineral interest bore to all of the mineral interests in the proposed unit, until payout of all well costs, with the option, at payout, to convert the retained override to a 25% working interest, proportionately reduced.
  - d. The Finley offer notified the unleased owners that if the owner selected Option 2 (participation), the owner would be required to pay the proportionate share of drilling costs attributable to the owner within 15 days prior to commencement of actual

drilling operations as set forth in a proposed AAPL Form Joint Operating Agreement, otherwise the owner would be subject to non-consent penalties provided in the JOA.

- e. The unleased owners to whom Finley's final offer was made were required to make an election of the three options within 14 days of the offer and the offer provided that if such an election had not been made within that time by returning a signed copy of the offer to Finley, it would be deemed that the owner did not choose any option, in which case Finley intended to seek compulsory pooling of the owner's interest pursuant to a forced pooling order to be issued by the Railroad Commission pursuant to the MIPA.
  - f. Finley presented copies of receipts for certified mail sent to the unleased owners. Certified mail to at least 8 of the unleased owners was returned as undeliverable.
15. The owners of unleased tracts within the proposed unit have not agreed to lease to Finley or to pool their unleased interests into the proposed unit.
  16. Finley did not present evidence to establish that compulsory pooling of the interests of the owners of unleased tracts into the proposed unit will avoid the drilling of unnecessary wells.
  17. Finley did not present evidence to establish that compulsory pooling of the interests of the owners of unleased tracts into the proposed unit will prevent the ultimate loss of hydrocarbons.
  18. Finley did not present evidence to establish that compulsory pooling of the interests of the owners of unleased tracts into the proposed unit is necessary to enable Finley and its lessors to recover their fair share of hydrocarbons from the subject reservoir.

#### CONCLUSIONS OF LAW

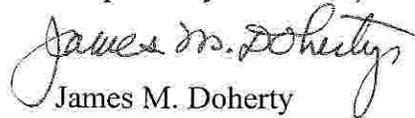
1. Pursuant to Texas Natural Resources Code §102.016, notice of the filing of this application and of this hearing was given to interested parties by mailing to their last known mailing addresses and by notice by publication in the case of interested parties whose whereabouts were unknown at least 30 days before the hearing.
2. The Commission has jurisdiction to decide this matter, at least with respect to owners of unleased interests that received Finley's offer to lease and/or pool voluntarily.
3. The Mineral Interest Pooling Act, Texas Natural Resources Code, Chapter 102, is limited in function to protect small tract lessees or owners rather than as a broad act designed to protect correlative rights generally or as an act allowing large tract lessees or owners more flexibility in development.

4. Finley Resources, Inc., did not sustain its burden to prove that compulsory pooling as proposed by Finley will serve the purposes of avoiding the drilling of unnecessary wells, preventing waste, or protecting correlative rights.
5. Pursuant to Texas Natural Resources Code §102.011, the Commission has no authority to order compulsory pooling where it is not established that such compulsory pooling will serve the purposes of avoiding the drilling of unnecessary wells, preventing waste, or protecting correlative rights.

**RECOMMENDATION**

The examiners recommend that the application of Finley Resources, Inc., pursuant to the Mineral Interest Pooling Act be denied.

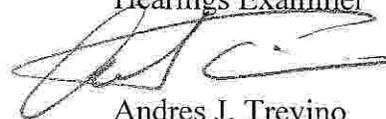
Respectfully submitted,



James M. Doherty  
Hearings Examiner



Marshall Enquist  
Hearings Examiner



Andres J. Trevino  
Technical Examiner