



RAILROAD COMMISSION OF TEXAS

OFFICE OF GENERAL COUNSEL

May 27, 2005

OIL AND GAS DOCKET No. 08-0242308

COMMISSION CALLED HEARING TO SUPERCEDE THE FINAL ORDER ISSUED AUGUST 24, 2001 IN OIL & GAS DOCKET No. 08-0226159 REQUIRING PLUGGING OF WELL No. 1 ON THE COWDEN "Q" LEASE, VEM (GRAYBURG) FIELD, ECTOR COUNTY, AND TO ENABLE O & O OPERATORS, LLC TO BECOME THE OPERATOR OF RECORD AND TO USE THE ABOVE-REFERENCED WELL FOR DISPOSAL PURPOSES.

APPEARANCES:

FOR APPLICANT.

Oscar Juarez II, President
Ismael Valenzuela, Foreman

APPLICANT

O & O Operators, LLC
"

PROPOSAL FOR DECISION

PROCEDURAL HISTORY

DATE OF REQUEST FOR ACTION.	March 22, 2005
NOTICE OF HEARING:	March 24, 2005
DATE CASE HEARD:	April 20, 2005
HEARD BY.	Marshall Enquist, Hearings Examiner
PFD CIRCULATION DATE.	May 27, 2005

STATEMENT OF THE CASE

This Hearing was set to consider the request of O & O Operators, LLC (hereinafter "O & O") to supercede the Final Order issued August 24, 2001 in Docket No 08-0226159 requiring plugging of Well No 1 on the Cowden "Q" (32351) Lease, VEM (Grayburg) Field (hereinafter "subject lease"), and to recognize O & O as the operator of record O & O asserts that it can restore the well to its former disposal capacity, preventing waste in surrounding producing wells, and therefore the well should not be plugged

SUMMARY OF EVIDENCE

The examiner took official notice of the Final Order in Oil & Gas Docket No 08-0226159, Commission records related to O & O's most recent Commission Form P-5 (Organization Report) filing, and Commission records identifying the wells for which O & O is currently recognized as the operator. O & O filed its most recent Organization Report with the Commission on January 4, 2005, and has posted financial assurance with the Commission in the form of a \$50,000 Letter of Credit which expires on April 6, 2006. O & O currently operates 60 wells.

O & O's president, Oscar Juarez II, appeared at the hearing and presented evidence in support of the application. O & O provided a copy of its Saltwater Disposal Agreement and Bill Of Sale from the prior operator, Steve Becker, former president of Prairie Crude, Inc.

The current Commission recognized operator of the subject lease, Prairie Crude, Inc (hereinafter "Prairie Crude"), submitted Commission Form P-4s (Producer's Transportation Authority and Certificate of Compliance), for the Cowden "Q" Lease effective September 1, 1991.

The call of the hearing misstates the date of the Final Order issued against Prairie Crude in Oil & Gas Docket No 08-0226159. In that docket, a Master Default order against Prairie Crude was issued on August 24, 2001 as stated in the call of the hearing. However, Prairie Crude filed a Motion for Rehearing which was granted by the Commission on October 23, 2001. The grant of the Motion for Rehearing effectively vacated the August 24, 2001 Final Order. On January 10, 2002, the case was heard again, resulting in a Final Order against Prairie Crude on May 10, 2002. This is the operative order directing plugging of Well No 1 on the Cowden "Q" Lease and is the order that O & O seeks to supercede.

In the Final Order of May 10, 2002, for Oil & Gas Docket No 08-0226159, Prairie Crude was ordered to plug the Cowden "Q" Lease Well No 1 and pay an administrative penalty of \$4,000 for violations of Statewide Rules 14(b)(2) and 8(d)(1). O & O has submitted a two-signature Form P-4 to designate itself as the operator of the subject lease and has stated that it has no officers in common with Prairie Crude or any connection to Prairie Crude. Prairie Crude received notice of this hearing at its P-5 Organization Report address, but did not appear in protest. The superceding order sought by O & O would be effective only as to transferring the ownership of the subject well and removing the plug-only requirement. The Final Order in Oil & Gas Docket No 08-0226159 would remain in effect as to the requirement that Prairie Crude pay an administrative penalty of \$4,000.

Prior to the hearing, O & O performed an MIT test on the well which indicated the wellbore is sound. Not surprisingly, the Form H-5 pressure test for the subject well is delinquent. O & O is prepared to present UIC with a completed Form H-5 and the pressure recording chart to bring the well into compliance for disposal/injection purposes. O & O has already ordered storage tanks and a gunbarrel, to enable it to separate hydrocarbons from produced water trucked into the facility, and offered into evidence a letter from the Sales Manager of Permian Tank confirming that the order would be ready for delivery in the last week of April, 2005.

According to O & O, surrounding operators are presently forced to truck their saltwater 10 to 15 miles away for disposal, with a disposal facility cost of 30 to 45 cents per barrel. O & O will compete by disposing at a rate of 30 to 35 cents per barrel. In addition, their disposal well will be closer to surrounding producing wells, reducing travel distance, time and expense (vehicle wear and fuel costs) for the operators of those wells. Access to a less remote and less expensive disposal facility will allow surrounding producers to extend the production life of their wells, thereby preventing waste.

The subject well is permitted as a commercial disposal well under UIC Permit No. 70953 and was last used for injection in 1995. The operator, Prairie Crude, Inc., had financial difficulties and lost several leases, as well as falling behind on what it termed "Commission paperwork". The well was sealed by the Commission in 1996.

The well is permitted for injection over a wide interval, from 3970' to 5360', at an injection rate of 4,000 barrels per day with a maximum surface injection pressure of 1950 psi. The well is somewhat over-engineered, with 16" surface casing cemented to 261 feet and 10 3/4" production casing cemented to 4301 feet. This protects usable quality groundwater, which is found in two zones: the first at 250 feet and the second from 1050 to 1350 feet. Commercial disposal permits are transferrable and O&O has already conducted the Mechanical Integrity Test necessary to bring the well into compliance with Commission rules. If the Commission does approve the superceding order, any Commission-imposed restrictions currently on the well will pass to O&O. The only restriction currently in place is the need for an annual Mechanical Integrity Test as opposed to the usual requirement of a test every 5 years.

AUTHORITY

Texas Natural Resources Code §85.049(a) provides:

On a verified complaint of any person interested in the subject matter that waste of oil or gas is taking place in this state or is reasonably imminent, or on its own initiative, the commission after proper notice, may hold a hearing to determine whether or not waste is taking place or is reasonably imminent and if any rule or order should be adopted or if any other action should be taken to correct, prevent or lessen the waste.

Texas Natural Resources Code §89.041 establishes the affirmative statutory responsibility of the Commission concerning abandoned wells:

If it comes to the attention of the commission that a well has been abandoned or is not being operated is causing or is likely to cause pollution of fresh water above or below the ground or if gas or oil is escaping from the well, the commission may determine at a hearing, after due notice, whether or not the well was properly plugged as provided in Section 89.011 or Section 89.012 of this code.

Texas Natural Resources Code §89 042(a) provides

If the commission finds that the well was not properly plugged, it shall order the operator to plug the well according to the rules of the commission in effect at the time the order is issued

Texas Natural Resources Code §91 107 requires that an operator have, on file with the Commission, financial assurance in the form of a bond, letter of credit or cash deposit in the amount necessary for both existing wells operated and any wells being transferred, prior to Commission approval of the transfer

Under Statewide Rule 14, the Commission may require a person seeking to be recognized as the operator of a well to provide evidence of a good faith claim of a continuing right to operate

EXAMINER'S OPINION

O & O asserts that it can meet the requirements to be recognized as the operator of the subject lease and restore the well to its best use as a commercial disposal facility. However, this claim is complicated by the Final Order requiring that Prairie Crude plug the well. An order superceding a Commission Final Order may be warranted if the operator shows 1) that it has a good faith claim of a continuing right to operate the well or lease, 2) that it has met the financial assurance requirements of Texas Natural Resources Code §91 107, and 3) that a superceding order is necessary to prevent waste. O & O has satisfied all of these requirements.

The first two factors apply to all transfers of inactive wells, not just cases where a well is ordered to be plugged. Any operator seeking to acquire an existing well which has been inactive for more than 12 months must show that it has a good faith claim of a continuing right to operate the well upon demand by the Commission. This requirement is found in Statewide Rule 14(b)(2). Additionally, the operator must show that it has met the requirements of Texas Natural Resources Code §91 107 which preclude the Commission from approving the requested transfer of an existing well to a new operator unless the new operator has filed financial assurance with the Commission in the form of a bond, letter of credit or cash deposit.

In this case, a good faith claim of a right to operate the subject leases is established by virtue of the Salt Water Disposal Agreement and Bill of Sale. O & O has a \$50,000 Letter of Credit in place which satisfies the financial assurance requirement under Texas Natural Resource Code §91 107.

Superceding a Final Order to Prevent Waste

Final Orders in Commission Enforcement Proceedings generally require an operator to plug a well for a violation of Statewide Rule 14(b)(2) if there is no reported production from the well (or

injection for injection and disposal wells) in the past 48 months. These "plug-only" orders reflect the Commission policy, that in cases where a well is in violation of Commission rules and has not reported any production or injection activity for a lengthy period of time, that the Commission will require that the well be plugged.

To support these "plug-only" orders, a Finding of Fact identifies when the well or lease last reported any production or injection activity. An additional finding of fact addresses the statutory requirement in Texas Natural Resources Code §89 041, by finding that the unplugged well is causing or is likely to cause pollution of fresh water above or below the ground.

A "plug-only" order falls under the Commission's authority in Texas Natural Resources Code §89 042. Further, the courts recognize that a Commission order to plug a well "is entitled to the same weight and finality as an order granting or refusing a permit to drill a well." *Wrather Petroleum Corporation v Railroad Commission*, 230 S W 2d 388, 390 (Tex App - Austin 1950, *reh'g denied*) citing *Railroad Commission of Texas v Gulf Production Co*, 132 S W 2d 254, 256, (Tex 1939). Finally, the findings of fact are not "technical prerequisites" but satisfy a "substantial statutory purpose." *Morgan Drive Away, Inc v Railroad Commission*, 498 S W 2d 147, 150 (Tex 1973), *Railroad Commission of Texas v R J Palmer*, 586 S W 2d 934 (Tex App - Austin 1979, *no writ*).

In this case, the Final Order entered against Prairie Crude was a "plug-only" order. As noted above, O & O must show that a superceding order is necessary to prevent waste.

Application of Waste Standard

In this docket, the question is whether O & O presented sufficient evidence that an order superceding a "plug-only" order is necessary to prevent waste. It is the examiner's conclusion that O & O presented sufficient evidence to support the entry of a superceding order to prevent waste.

O & O proposes to restore the well to its previous use as a disposal well. O & O has conducted an MIT test to assure the mechanical integrity of the well and will be installing new equipment, including storage tanks and a gunbarrel. It is likely that O & O's efforts will result in the recovery of at least some hydrocarbons that would not otherwise be recovered by surrounding producing wells, by extending the life of the economic limit of those wells. Accordingly the examiner concludes that an order superceding the plug only provisions in the Final Order will prevent waste.

Based on the record in this docket, the examiner recommends adoption of the following Findings of Fact and Conclusions of Law.

FINDINGS OF FACT

- 1 O & O Operators, LLC (hereinafter "O & O") and Prairie Crude, Inc (hereinafter "Prairie Crude") were given at least 10 days notice of this proceeding O & O appeared at the scheduled time and place for the hearing through its president Oscar Juarez II and presented evidence Prairie Crude did not appear
- 2 O & O filed its first Commission Form P-5 (Organization Report) with the Commission on January 16, 2003 O & O has posted financial assurance with the Commission in the form of a \$50,000 Letter of Credit
- 3 Prairie Crude was recognized as the operator of the Cowden "Q" Lease (hereinafter "subject lease") after filing Commission Form P-4s (Producer's Transportation Authority and Certificate of Compliance), effective September 1, 1991
- 4 In Oil & Gas Docket No 08-0226159, Prairie Crude was ordered to plug the Cowden "Q" Lease Well No 1 and pay an administrative penalty of \$4,000 pursuant to a Final Order entered on May 10, 2002 for violation of Statewide Rules 14(b)(2) and 8(d)(1)
- 5 O & O has a Salt Water Disposal Agreement and Bill of Sale from the former operator and present trustee of the lease, giving O & O the right to operate the well
- 6 Superceding the requirement in the Final Order entered in Oil & Gas Docket No 08-0226159 that the Cowden "Q" Lease Well No 1 be plugged is necessary to prevent waste
 - (a) Due to removal of associated equipment, the Cowden "Q" Lease Well No 1 is currently not equipped for disposal operations
 - (b) By re-equipping and repairing the associated equipment of the Cowden "Q" Lease Well No 1, and setting up storage tanks and a gunbarrel, the well can be restored to its former status as a disposal facility
 - (c) Nearby producing wells are currently trucking their produced saltwater 10 to 15 miles for disposal, and being charged 30 to 45 cents per barrel at the disposal facilities
 - (d) O & O plans to undercut to competition by disposing of produced water at a rate of 30 to 35 cents per barrel
 - (e) Operation of the Cowden "Q" Lease Well No 1 as a commercial disposal facility will allow surrounding producers to cut their disposal costs by reducing the distance necessary to truck their saltwater for disposal, saving on vehicle expense and fuel expense

- (f) Lowered disposal costs will allow surrounding producers to extend the economic life of their wells, thus preventing waste.
- 7. The requirement in the Final Order in Oil & Gas Docket 08-0226159 that Prairie Crude pay an administrative penalty of \$4,000 will remain in effect.

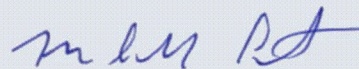
CONCLUSIONS OF LAW

- 1. Proper notice of hearing was timely issued to the appropriate persons entitled to notice.
- 2. All things necessary to the Commission attaining jurisdiction have occurred.
- 3. O & O has a good faith claim of a right to operate the subject lease.
- 4. O & O has filed financial assurance in the type and amount required under Texas Natural Resources Code §91.107 to be approved as the operator of the subject lease.
- 5. A Final Order superceding the Final Order entered in Oil & Gas Docket No. 08-0226159 on May 10, 2002, requiring plugging of Well No. 1 on the Cowden "Q" Lease, VEM (Grayburg) Field, Ector County, is necessary to prevent waste.
- 6. The Final Order in this Docket superceding the Final Order in Oil & Gas Docket 08-0226159 is effective only as to the disposition of Well No. 1 on the Cowden "Q" Lease, VEM (Grayburg) Field, Ector County, and does not relieve Prairie Crude of its obligation to pay an administrative penalty of \$4,000 to the Railroad Commission.

RECOMMENDATION

The examiner recommends that the Commission grant O & O's request to supercede the provisions in the Final Order entered in Oil & Gas Docket No. 08-0226159 requiring plugging of Well No. 1 on the Cowden "Q" (32351) Lease. The examiner further recommends that all other provisions of the Final Order in Oil & Gas Docket 08-0226159 remain in full force and effect.

Respectfully submitted,



Marshall Enquist
Hearings Examiner