RAILROAD COMMISSION UPDATE

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State Bar of Texas
10TH ANNUAL
OIL AND GAS DISPUTES
January 18-19, 2024
Houston

CHAPTER 8

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I. INTRODUCTION

Since this paper is presented at the Oil and Gas Disputes conference, we attempt to focus our Railroad Commission Update on disputed oil and gas regulatory matters, which means (for the most part) disputes adjudicated by and before the Railroad Commission of Texas. These disputes typically involve contested interpretation or application of Commission rules, and they are normally technical in nature. This is an update of the paper we first presented at the 2020 and 2021 Disputes Courses.

A few major and timely regulatory issues have the potential to impact all Texas oil and gas lawyers, particularly those who handle oil and gas disputes. First, the *Opiela* case, challenging the Commission's ability to issue allocation well and PSA well permits, continues to work its way through the Court system, seemingly headed towards the Supreme Court. Second, increased incidence of seismicity in West Texas is in the news and at the forefront of Commission policymaking. Finally, the Commission is in the process of overhauling its pollution and pit rules, which may be more of interest to Commission practitioners, but is something all oil and gas lawyers should be aware of.

The Railroad Commission, unlike pretty much every other agency in Texas, does not farm out its contested case hearings to the State Office of Administrative Hearings ("SOAH"); instead, contested case hearings are heard before an in-house Hearings Division, complete with a clerk's office (Docket Services), a judiciary (Administrative Law Judges), and staff experts (Technical Examiners). After a hearing, at which the parties present evidence as one would in a bench trial, the ALJ and Technical Examiner assigned to a case issue a written Proposal for Decision and Recommended Final Order ("PFD"), to which the parties may take exception, and which is then presented to the three elected Railroad Commissioners for ultimate decision at a duly noticed Open Meeting, which at the Railroad Commission is called Conference.

The Railroad Commission hears three basic types of disputes: (1) Oil and Gas Division disputes; (2) Gas Utility (pipeline) disputes; and (3) Surface Mining and Reclamation disputes. This paper will provide an update on the Oil and Gas disputes, in addition to the topical matters introduced above.

II. OUR STUDY AND SOME GENERAL OBSERVATIONS

For purposes of compiling this Update, we have conducted a study of all contested cases before the Railroad Commission that resulted in a decision by the Commissioners themselves, during 2022 and 2023 (through the November 15, 2023 Conference, which was the last Conference prior to this paper's due-date). Sifting through the data, a few general observations emerge:

Most of fields being actively developed today by horizontal drilling and fracture stimulation -- the Spraberry (Trend Area) Field in the Midland Basin, the various Bone Spring and Wolfcamp fields in the Delaware Basin, and the Eagle Ford Shale -- are UFT Fields.[1] These fields have rules that normally eliminate between-well spacing and allow operators great flexibility in locating wells. As a consequence, the types of contested hearings about well spacing which for many years were the bread and butter of the hearings division are no longer prevalent. During our study period, the Commissioners at Conference only adjudicated three Rule 37/Rule 38 cases.

That said, it must be emphasized (and is discussed below) that every single allocation well or PSA well drilling permit is a Rule 37 exception permit. Almost none of them require hearings, due to the Commission's long-standing rules governing who is, and who is not, entitled to notice and a hearing on Rule 37 cases.

The development of UFT Fields has resulted in the emergence of other types of cases. During 2022 and 2023, one of the most prevalent types of case adjudicated by the commission was the application for a permit to operate a salt water disposal well ("SWD"). These wells are necessary to handle the vast amounts of fracture stimulation flow-back water being generated from UFT development, as well as produced water from these prolific wells. At the same time as competition for SWD permits (and business) seems to be growing, the Commission's response to seismicity concerns has reduced the areas in which injection can take place, both geographically and geologically. As a consequence, SWD permitting cases continue to be hotly contested and frequent.

Not all Commission contested cases grapple with UFT Field issues. A significant portion of the caseload addresses the problems at the other end of the life cycle: what to do with old, marginal or abandoned wells. Many of the cases adjudicated by the Commissioners address the application of Statewide Rule 15 (the somewhat recent Inactive Well Rule), and the frequently related Good Faith Claim complaint/Single Signature P-

[1] Commission rules define a UFT Field as "A field designated by the Commission . . . for which horizontal well development and hydraulic fracture treatment must be used in order to recover resources from all or a part of the field." 16 Tex. Admin. Code §3.86(a)(13). The criteria for designation of a UFT field are set out in Statewide Rule 3.86(i).

4 processes. Many of those cases are default cases, meaning the operator of the marginal wells simply does not respond to Commission orders to make their case.

During the January 2022 through December 2023 study period, the Commissioners adjudicated 67 Oil and Gas Division cases. As noted above and discussed below, this list does not include flaring cases, most of the Inactive Well Rule cases, and most of the enforcement cases, as most of those cases, while requiring hearings, are not contested and are thus not discussed by the Commissioners. These 67 cases, broken down by type, are set out below:

Contested Good Faith Claim Cases	19 cases
Statewide Rule 9/46 (SWD Permit Applications)	18 cases
Contested Inactive Well Rule Cases	9 cases
Various Complaints	5 cases
Rule 8 Cases (solid waste treatment)	4 cases
Rule 37 Cases	3 cases
Contested Flaring Applications	2 cases
Various Complaints	2 cases
Contested MIPA Applications	2 cases
Disputed Enforcement Cases	1 case
Other	2 cases

Also during our January 1, 2022 through November 15, 2022 study period, the Commission adjudicated 518 Rule 32 (flaring exception) cases, 311 Good Faith Claim/Single Signature P-4 complaints, and 80 Mineral Interest Pooling Act applications on the Consent Agenda. All of these cases required the consideration of the Hearings Division, and many of them required actual hearings.

III. CURRENT ISSUES

A. Allocation and PSA Wells and the *Opiela* case: a question of proper well location

1. The History of the Case and the Court of Appeals Opinion

On June 30, 2023, the Third Court of Appeals issued its opinion in the *Opiela* case, in which a 2-1 majority of the panel held that the drilling permit at issue was invalid, but in so doing rejected a number of the arguments pressed by the Opielas. A Petition for Review has been filed but has not been ruled upon at the time of this paper.[2] Given the importance of the issue, an expectation seems to exist that the Petition will be granted, so the legal framework described below may well change. The case involves the Commission's issuance of drilling permits for allocation wells and PSA wells; the case does not involve damages issues (i.e. how should the royalty owners get paid).

Allocation well permits and PSA well permits are means by which operators can remove the regulatory bar and obtain permits to drill horizontal wells that cross lease lines without pooling the tracts. From the Railroad Commission's perspective, an allocation well is "a horizontal wellbore crossing two or more tracts/leases and for which the operator allocates production among the leases/tracts covered. The operator has made a good-faith claim that it holds leases covering each tract included in the developmental unit."[3] A PSA well permit is available when 65% of the mineral and working interest ownership agrees to the PSA itself.

During the time period from January 1, 2022 through December 8, 2023 (this paper's due date), the Commission issued 9,521 drilling permits coded as for future allocation wells (although many of these would have been something different upon completion -- the allocation well is often used as a vehicle to get a drilling permit while final title is cleared). During the same time period, the Commission issued 1,183 PSA well drilling permits. Because both allocation wells and PSA wells cross lease lines and there is no pooling, every allocation well permit and PSA well permit is a Rule 37 exception case.

Previously, only a single Texas Court of Appeals had issued an opinion addressing allocation wells, but it did not use the term. In *Browning v. Luecke*, Browning Oil Company drilled two horizontal Austin Chalk wells in pooled units that included acreage they had leased from the Lueckes. *Browning Oil Co., Inc. v. Luecke*, 38 S.W.3d 625, 638 (Tex. App. -- Austin 2000, pet. denied). Because the putative pooled units violated the Lueckes' oil and gas leases, the pooling was not valid. *Id.*, 642. But, this did not mean that the drilling permits were automatically invalid or that the wells were trespassing wells; it simply meant that none of the traditional attributes of pooling applied to these wells:

> The proper remedy for a breach of the pooling provisions may not ignore or exceed the ownership interests conveyed under the leases. The Lueckes contracted for a share in royalties based on total production from their land. The pooling provisions provide an exception to this arrangement only if Lessees properly pool the Lueckes' tracts. Then by a cross-conveyance of interests in all pooled lands the Lueckes would be entitled to royalties on a pro rata share of production from the pooled tracts. The trial court's finding that Lessees breached the pooling provisions, which we affirm, rendered the pooled units invalid with respect to the Lueckes' land. Absent valid pooling, there is no

[2] Cause No. 23-0772, before the Supreme Court of Texas.

[3] RRC Form P-16 Instructions for Completion Report (Rev. 09/2019).

> crossconveyance, and the Lueckes are not entitled to royalties on oil and gas produced from lands they do not own.

Id., at 643. Put another way, this meant that the normal pooled unit royalty calculation metric -- royalty on a proportionate surface acreage basis -- did not apply.

Instead, the Court explained the basic premise behind horizontal wells. While technologically advanced, they are really not terribly complicated from a regulatory perspective. Horizontal wells should be treated as a series of vertical wells. "Each tract traversed by the horizontal wellbore is a drillsite tract, and each production point on the wellbore is a drillsite." *Id.*, at 634.

The Third Court of Appeals reversed the trial court's judgment in favor of the Lueckes and remanded the case for a new damages determination. *Browning*, 38 S.W.3d at 647. The general guiding principle was that since the wells were not pooled unit wells, surface acreage royalty apportionment could not be used, and so the question for the factfinder was to determine how much of the wells' production was the Lueckes', as opposed to their neighbors'. *Id.* "The better remedy is to allow the offended lessors to recover royalties as specified in the lease, compelling a determination of what production can be attributed[4] to their tracts with reasonable probability." *Id.* The fact that the wells were horizontal wells drilled across multiple tracts without valid pooling authority did not cause the sky to fall, or require the wells to be plugged, or entitle the Lueckes to royalty on production that was not from their land. Instead, the wells were simply treated as strings of vertical wells.

Browning was not a regulatory dispute, but its holding is instructive in the context of the present dispute that has Commission practitioners talking -- the *Opiela* case. Elsie and Adrian Opiela filed a complaint with the Commission related to the permitting of the Audioslave A Lease Well No. 102H, which was originally permitted by EnerVest but is now operated by Magnolia Oil & Gas Operating, LLC. The Audioslave well is a horizontal well that was originally permitted as an allocation well, but the permit was later amended to be a PSA well. The Opielas own an undivided interest in the minerals in and under one of the tracts traversed by the wellbore. Their lease does not provide pooling authority. The Opielas' complaint asserts that the Commission should not have issued the drilling permit, because Magnolia does not have a good faith claim to operate the well, since it crosses multiple tracts and their lease does not allow pooling. In other words, the Opielas challenge the Commission's longstanding practice of issuing allocation well and PSA well drilling permits.

On October 2, 2019, the Railroad Commission issued its Final Order in the *Opiela/Magnolia* complaint, denying the Opielas' Complaint that Magnolia did not have a good faith claim to operate its Audioslave A Well No. 102H. The Opielas filed a judicial appeal of this ruling in the Travis County District Courts under the APA, and on May 12, 2021, the Travis County District Court issued a Final Judgment ruling against Magnolia and the Commission. The Final Judgment held that the Commission's specific ruling as to the Audioslave A 102H was in error, but it went further, also holding that the Commission's practice of issuing allocation well and PSA well drilling permits was in error, as, according to the Court, it should have required a rulemaking.

The basic thrust of the case, per the Opielas, is based on the language of their oil and gas lease, which says: "Nothing contained herein shall authorize Lessee in any manner whatever to pool said land or any part of same for oil."[5] Per the Opielas: "Because of this prohibition, Magnolia cannot show a good-faith claim to include the Opielas' property in a multi-tract drilling unit."[6] In this manner, the Opielas invoke the Commission's "good faith claim" jurisprudence, which is discussed in more detail below, as it is more commonly invoked. By way of shorthand, in 1943, the Texas Supreme Court confirmed that the Railroad Commission lacked jurisdiction to adjudicate questions of title, but in so doing reserved to the Commission the right (even the obligation) to consider whether an applicant has at least a good faith claim of right to do that for which the applicant seeks a permit. *Magnolia Petroleum Co. v. Railroad Commission*, 170 S.W.2d 189, 191 (Tex. 1943) ("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.").

The good faith claim portion of the *Opiela* case is somewhat simple. The Opielas say that allocation wells are really just pooling by another name, and pooling "in any manner whatever" is forbidden, so Magnolia should not have been given drilling permits. Magnolia, in response, argues that unlike Browning Oil, it never claimed to pool. It just drilled a well on the Opielas' lease, and then also drilled it on the neighbors' (the Paweleks), both things it had the right to do under each applicable lease. The Commission ruled in favor of Magnolia, in keeping with its prior jurisprudence in the area.[7]

The Travis County District Court disagreed. As part of its May 12, 2021 Judgment, the Court made

[4] Or, perhaps, allocated.

[5] *See* Opiela's Brief on the Merits before the Third Court of Appeals, at p. 1.

[6] *Id.*

[7] The *Klotzmann* and *Monroe Properties* cases, both of which settled prior to a reported opinion.

findings on the good faith claim part of the case, finding that "The Commission erred in concluding that it has no authority to review whether an applicant seeking a well permit has authority under a lease or other relevant title documents to drill the well,"[8] and that "The Commission erred in failing to consider the pooling clause of the lease covered by the Audioslave Well in deciding that Magnolia has a good faith claim to operate the well."[9]

These findings, apparently drafted by counsel for the Opielas, are inconsistent with the actual record from the Commission proceeding in *Opiela* and unfairly mischaracterize the work of the Commission and its Hearings Division in the underlying case. Both were appropriately rejected by the Third Court of Appeals. *Railroad Commission of Texas v. Opiela*, ___ S.W.3d ___, 2023 WL 4284984, *7-9 (Tex. App. -- Austin 2023, pet. filed).

In so holding, the Third Court of Appeals also rejected the Opielas over-arching argument that production via a PSA or allocation well permit is simply pooling with a different name. *Opiela*, *8 ("We conclude that production through a PSA is not the same as pooling under Texas law."). In reaching this holding, the Court relied heavily on its analysis from *Browning v. Luecke* (summarized above), including the notion that a horizontal wellbore can be analyzed as simply a series of drillsites.

The Court of Appeals did not reach the District Court's more sweeping other finding, that the Commission "erred in adopting rules for allocation and Production Sharing Agreement ("PSA") well permits without complying with the requirements of the Administrative Procedure Act, Tex. Gov't Code § 2001.001 et seq."[10] The Opielas argued that by issuing allocation well permits and PSA well permits without having conducted a formal APA rulemaking, the Commission has exceeded its jurisdiction. In response, Magnolia and the Commission argued that the Commission's issuance of allocation and PSA well permits is in keeping with its existing regulatory framework, and also is performed, appropriately, pursuant to its adjudicatory powers, as opposed to its rulemaking authority. For now, the question is academic. The Third Court of Appeals declined to reach it, on the basis of its ultimate holding that the drilling permit was invalid regardless of whether a rulemaking should have been applied. *Opiela*, *9-10. This holding was something of a curveball.

As noted above, the permit on which the well in *Opiela* was drilled was a PSA well permit, not an allocation well permit. The Commission issues PSA well permits when the operator certifies that at least 65% of the interest owners in each tract has signed a production sharing agreement, that is, an agreement as to how proceeds from the well shall be shared.[11] Operators routinely include in this calculation lessors who have agreed to pooling, as a pooling clause in a lease is an agreement as to how proceeds from a well crossing other tracts will be shared; this is also what Magnolia did. The Third Court of Appeals rejected this approach. The 2-1 majority opinion held that Magnolia could not include in its 65% calculation the 49.437% of owners who had agreed to pool, and thus there was no substantial evidence to support the Commission's finding that the drilling permit was valid. *Opiela*, *12. Given this resolution, the Court did not reach the question of whether the 65% requirement, or allocation well permits, ought to have required a rulemaking.

Justice Chari Kelly dissented. Prior to her election to the court, she was a prosecutor and criminal defense lawyer, and it is not clear that she has any background in oil and gas law or experience practicing before the Railroad Commission. Nonetheless, her short dissenting opinion gets right to the point, at least from the author's perspective. Even though she agrees that pooled unit wells and PSA wells are fundamentally different, she would not have overruled the Commission's "unchallenged findings" that more than 65% of the interest owners had agreed to a method of dividing proceeds from the well at issue. *Opiela*, *13 (J. Kelly, dissenting). She would then have addressed the rulemaking issue.

A Petition for Review has been filed before the Texas Supreme Court, so it seems likely we will hear more on this issue.

2. One possible analytical approach

From a purely regulatory perspective, this need not be complicated. At issue in the *Opiela* case is an application for a drilling permit for a horizontal well. Allocation and PSA well permitting is simply a question of permitting a well at a location that is necessary to prevent waste or protect correlative rights, which are the core statutory obligations of the Commission. Here the permitting requires an application for exception to the Commission's rules because the wellbore crosses a lease line.

When horizontal wells are drilled in pooled units, the pooling eliminates lease lines, for Rule 37 purposes, because the pooling effects a cross conveyance of the

[8] Final Judgment in *Opiela*, at ¶2.

[9] Final Judgment in *Opiela*, at ¶3. The author does not believe that these findings are a fair reflection of the record from the actual RRC hearing in *Opiela*, and the clearly incorrect finding that the Commission failed to consider the pooling clause was expressly rejected by the Third Court of Appeals. The Commission considered it; it simply chose to not give it determinative legal effect.

[10] Final Judgment in *Opiela*, at ¶1.

[11] This process is described in the instructions to RRC Form P-16; it is not set out in Commission rules.

interests; all that is required is that the wellbore be of adequate distance from the pooled unit boundary, and the internal lease or tract lines need not be considered. If an operator chooses to drill a horizontal well across multiple tracts without pooling, the operator cannot take advantage of this attribute of pooling. But that does not mean the well cannot be drilled.

In today's world, where laterals are ever longer and thus drilling units larger, it is quite common for operators to create even pooled units that contain unleased interior tracts. If an unleased interior tract (or "window tract") exists within a unit, its boundaries must be honored for Rule 37 spacing purposes. This often means a No Perf Zone ("NPZ") may be needed, or a Rule 37 exception.[12] Allocation and PSA wells are no different. If an operator cannot drill a well under pooling authority, then it must honor the boundary between tracts as a lease line for Rule 37 purposes; it is for this reason that every allocation and PSA well is a Rule 37 exception well.

Normally, this requirement is not an impediment to drilling. In the classic allocation well case, the same operator operates both un-pooled tracts under separate leases, so it can waive the right to protest the request for a Rule 37 exception on its own behalf.[13] The existence of this structure undermines the Opielas' arguments that a formal rulemaking should be required. Rule 37, the Railroad Commission's spacing rule, is perhaps the oldest Commission Rule. A robust body of caselaw exists interpreting it. Rule 37 itself sets out procedures for challenging the issuance of drilling permits, including a delineation of who is, and is not, entitled to notice of applications for exceptions to the rule.

More importantly, almost every field with special field rules (which would include all fields in which allocation and PSA wells are commonly permitted) has its own spacing rules, promulgated after a contested case hearing at which data specific to the field is presented and evaluated by the Hearings Division. As expressly confirmed by the Texas Supreme Court, the Commission has the general discretion to decide to determine field rules by adjudicative proceedings (i.e. contested case hearings) rather than rulemaking under the APA. *Railroad Commission of Texas v. WBD Oi l& Gas Co.*, 104 S.W.3d 69, 74 (Tex. 2003), citing *Lone Star Gas Company v. Railroad Commission of Texas*, 844 S.W.2d 679, 689 (Tex. 1992).

Of necessity, an APA rulemaking procedure to adopt a statewide rule is general, as are the data in support of a particular rule, because it is intended to be a basic template. As explained in the *WBD* case, while the ability to participate in a rulemaking may be broader than a contested case hearing, rulemakings afford vastly less due process to affected parties than do adjudicative contested case hearings. *WBD*, 104 S.W.3d at 76-78. In rulemakings, the rules of evidence do not apply, there is no cross examination of witnesses, there is no sworn testimony at all, there is no opportunity for discovery, and indeed no hearing is even required.

Special field rules adopted via contested case hearings, on the other hand, apply to a subset of operators developing a particular geologic target. Because they focus on a particular area, the regulatory framework devised by the Commission and approved by the Texas Courts provides for notice and hearing to those parties most likely to be affected by local field rules. Evidence specific to that development can be brought to the Commission, and the parties affected can, through the evidentiary process, provide the Commission with comprehensive information.

When an operator concludes that it must drill a well at a location that is an exception to the Statewide rules, or to the special field rules, the Commission regulatory process treats that application as unique, because each application is unique. No two wells in the state are identical. Every well, even in the same target zone, is specific to itself. For this reason, the Commission requires that individual well applications for exceptions to its rules for location, or allowable, or flaring be contested cases in which the applicant bears the burden of proof to show the exception is necessary. The grant, or not, of the exception is an adjudication of the interests of specific owners in a unique place and time. Such a granular analysis requires a very specific type of due process that gives potentially affected parties the opportunity to have a hearing, where testimony and evidence can be presented and challenged.

Ultimately, this means that whether or not a particular allocation well or PSA well should be granted a Rule 37 exception, and thus a drilling permit, must be considered in light of the facts specific to whether that well is entitled to an exception to prevent waste or protect correlative rights. This cannot be done fairly under the APA rulemaking process, which as explained by *WBD* allows broader participation but much more limited due process. Choosing to determine these issues using contested case procedures rather than rulemaking procedures is an appropriate exercise of the Commission's discretion. *WBD*, 104 S.W.3d at 74.

In the context of that framework, the following rules and procedures applied in the Opielas' case. First, royalty owners like the Opielas are not entitled to notice of applications for exceptions to spacing rules. In 2000, the Third Court of Appeals explained, as many decisions before had, that a royalty owner is not an "affected person" for Rule 37 purposes and is therefore not entitled to notice of applications for spacing exceptions nor given the right to protest them. *H.G. Sledge, Inc. v.*

[12] Increasingly, the Mineral Interest Pooling Act is also used to address window tracts; more on this later.

[13] 16 TEX. ADMIN. CODE §3.37(h)(2)(B).

PITCO, 36 S.W.3d 597, 604 (Tex. App. -- Austin 2000, pet. denied). The *Sledge* opinion, handed down on the same day as *Browning v. Luecke*, goes through the history of Rule 37 and its amendments and explains the well-developed processes at play. It notes that "the question of proper well location is 'one vested peculiarly in the Commission as an administrative body, and one which cannot be exercised by the courts.'" *Id.*, quoting *Stewart v. Humble Oil & Ref. Co.*, 377 S.W.2d 830, 833 (Tex. 1964). *Sledge* also cites a much earlier case, *Shell v. Railroad Commission*, that cleanly articulates the very different roles to be played by lessors, lessees, regulators, and courts:

> Our examination of the many rule 37 opinions delivered by this and other courts fails to disclose that it has ever been suggested that royalty owners are necessary or even proper parties to an appeal from a Commission order granting or refusing a drilling permit. The only interest of the royalty owners is to receive when produced their share of the oil or its proceeds. The lessee is invested with the exclusive right of possession and development. In the drilling and spacing of wells the lessee represents the royalty owners in so far as they may have any interest therein. They were so represented in the making of the applications for the permits and in all proceedings thereunder before the Commission; to which proceedings they were not made parties and in which they did not participate other than by such representation.

Shell Petroleum Corp. v. Railroad Commission, 137 S.W.2d 797, 798 (Tex. Civ. App. -- Austin 1940, no writ).

Nonetheless, when they filed their complaint related to the issuance of the drilling permit, the Opielas were given an opportunity to assert they were affected and to have a hearing on whether the permit to drill should have been granted. They offered evidence that the permittee did not have a good faith claim to ask for the exception and permit. The Commission conducted a full contested case hearing, applied the exact same rules it has applied in all good faith claim cases, and ultimately did not agree with them. The Commission's process worked exactly as it was designed to (as informed by the *Magnolia* case), and all parties, including the Opielas, received due process.

Horizontal wells, while technological marvels, still fit into the Commission's regulatory schemes. If they are not drilled within pooled units, and if they cross multiple tracts, their permitting is addressed by Rule 37. The Commission has never required notice of an application for a Rule 37 exception to be given to royalty owners, for the reasons stated. This robust and venerable framework would clearly have allowed Magnolia to drill two vertical wells, each a foot away from the Opiela-Pawelek boundary, on either side. That being the case, there can be no reason to disallow allocation wells and the manner in which they have been permitted, at least from a purely regulatory perspective.[14] From the author's perspective, the application for drilling permits for allocation wells at the Railroad Commission should be considered a question of proper well location, nothing more, and that is a question the Commission is well equipped to handle.

3. Why this matters

Since the District Court's Final Judgment in *Opiela*, the Commission has issued 12,044 allocation well drilling permits.

B. Concerns about induced seismicity

For some time, concern has existed that salt water injection might be linked to apparently increased instance of seismic events.[15] Commission rules that govern SWD permits were amended somewhat recently to provide specific authority for regulation of the potential for SWD-induced seismicity. In recent months, the Commission has created three Seismic Response Areas ("SRAs") surrounding specific seismic events, all in West Texas.[16] SWD well operators within these SRAs were asked to voluntarily curtail or shut-in injection, and Commission Staff has initiated show-cause proceedings to seek orders from the Hearings Division when the operators have been unwilling to do so voluntarily.

Most of these cases have settled, but one did not.[17] In that case, the operator operated two deep injection wells within the Gardendale SRA, both of which

[14] And the purely regulatory perspective is all that this paper, and the current *Opiela* case, must grapple with. How to pay the royalty owners in an allocation well must be determined by the courts, not the Commission, and indeed, the Opielas have filed that lawsuit as well.

[15] The increase in observed seismic events at least partially coincides with the increase of the number of seismic monitoring stations.

[16] For the specific information, see: https://www.rrc.texas.gov/oil-and-gas/applications-and-permits/injection-storage-permits/oil-and-gas-waste-disposal/injection-disposal-permit-procedures/seismicity-review/seismicity-response/

[17] Oil & Gas Docket No. OG-21-00008558, Commission Called Hearing Requested by Crownquest Operating, LLC To Show Cause Why the Injection/Disposal Permit Should Not be Suspended for the Nail Ranch '36' Lease, Well No. 1D, Spraberry (Trend Area) Field, Martin County, Texas

injected into the Ellenburger foundation. When the Gardendale SRA was created, the Commission asked all deep injection well operators to voluntarily curtail injection to 10,000 barrels per day, and the operator declined. Later, in December, 2021, four seismic events with magnitudes between 3 and 4 occurred within the Gardendale SRA, and the Commission suspended injection authority for all deep disposal wells. The operator requested a hearing, and a full hearing was held, at which the operator put forth technical evidence arguing that its two SWD wells were too far from the reported seismic events to have been contributing, and the Commission put on technical evidence to the contrary (including testimony of the Commission's staff seismologist).

On November 10, 2022, the Hearings Division issued a Proposal for Decision, recommending that the Commission rule that staff was within its authority to curtail injection from these deep wells; "The evidence shows that more likely than not the injection of fluids into the Subject Wells contributed to pressure on the Midland North Fault in the Gardendal SRA prior to the fault slipping."[18] Subsequent to the PFD, in the face of additional seismic events within the Gardendale SRA, the operator agreed to no longer challenge the permit suspension.

This remains an issue that must be watched.

C. Proposed Changes to Rule 8[19]

On October 2, 2023, the Commission issued a Notice to Operators with draft amendments to its water protection and environmental protection regulations. Basically, this is draft language that revamps Rule 8 and the portions of new Chapter 4 that focus on recycling of produced water. Both areas have been the subject of informal study among the staff and stakeholders for some time. The staff has wanted to modernize Rule 8 for a number of years, in particular tightening up on any use of pits, and also has been tasked with crafting new rule language to push forward the Legislative mandate to encourage recycling of produced water rather than disposal. The draft rules can be found on the Commission's website.[20]

Division 1 of Subchapter 4(A) contains the broad 'thou shalt not pollute' provision that has long been the base for Rule 8 (Originally Rule 20) pursuant to the Commission's original governing statutory directives. The proposed amendments contain a much more detailed definitions section, including a proposed definition of groundwater, that should be reviewed by any in-house technical team. The generator of oil and gas waste is expressly identified as the party responsible for characterizing the waste. This responsibility will add a step to drilling operations that will have to be built in to an operator's company process. Other portions of this general section include specific reference to penalties similar to those in Rule 107 and acknowledgment of the TCEQ authority over surface waters.

The operative language of Rule 8 will now be set out in Subchapter A of Chapter 4. The draft proposed language lays out more stringent requirements for pit permitting and uses, including the requirement that all pits be authorized, by rule, permit or order. This will include application of the proposed regulations to temporary pits, which has already caused significant comment among operators, particularly smaller independent operators. The Commission summary identified registration of pits and evaluation of groundwater conditions at pit locations as key proposed modifications. Subchapter B contains proposed language for the recycling related provisions applicable to commercial facilities and new provisions relating to drill cuttings.

The Commission has held two (2) public hearings on the proposed rules, and action is expected to be taken in the Spring of 2024.

IV. RECENT DECISIONS IN CONTESTED CASES

A. SWD Permit Applications

1. Basic Framework and Procedure

Salt Water Disposal Wells are wells that inject produced water into formations of sufficient porosity and permeability to take the water. This injection requires a permit independent of the permit to drill the well, the issuance of which is governed by Chapter 27 of the Texas Water Code. The Water Code, in turn, requires the Commission to promulgate SWD permitting rules. TEX. WATER CODE §27.034.

The Railroad Commission has adopted two rules governing SWD permitting: injection into non-productive formations is governed by Statewide Rule 9 (16 TEX. ADMIN. CODE §3.9), and injection into

[18] Oil & Gas Docket No. OG-21-00008558, Commission Called Hearing Requested by Crownquest Operating, LLC To Show Cause Why the Injection/Disposal Permit Should Not be Suspended for the Nail Ranch '36' Lease, Well No. 1D, Spraberry (Trend Area) Field, Martin County, Texas, Proposal for Decision, p. 44.

[19] Ana Maria Marsland provided the content for this discussion, as well as valuable input on the paper as a whole. Any mistakes, though, are the author's.

[20] https://www.rrc.texas.gov/media/nmtd3dlg/prop-new-ch4-subcha-informal-comment-draft-posted-100223.pdf (Subchapter A) and https://www.rrc.texas.gov/media/fsdbao2k/prop-amend-ch4-subchb-informal-comment-draft-posted-100223.pdf. (Subchapter B).

productive formations is governed by Statewide Rule 46 (16 TEX. ADMIN. CODE §3.46). The basic permitting requirements are governed by Chapter 27 of the Water Code and are generally the same under whichever Commission Rule applies. They are summarized in Section 27.051(b) of the Water Code:

> (b) The railroad commission may grant an application for a permit under Subchapter C in whole or part and may issue the permit if it finds:
>
> (1) that the use or installation of the injection well is in the public interest;
> (2) that the use or installation of the injection well will not endanger or injure any oil, gas, or other mineral formation;
> (3) that, with proper safeguards, both ground and surface fresh water can be adequately protected from pollution; and
> (4) that the applicant has made a satisfactory showing of financial responsibility if required by Section 27.073.

TEX. WATER CODE §27.051.

Commission rules elaborate on the process for an SWD permit application. The applicant is required to obtain a letter from the Commission's Groundwater Advisory Unit setting out the fresh water bearing formations that must be protected from possible migration of the injected water. 16 TEX. ADMIN. CODE §3.9(2).[21] The applicant is also now required to provide a screenshot of the USGS seismic event website showing a 100 square mile circular radius around the location of the requested disposal well. 16 TEX. ADMIN. CODE §3.9(3)(B). If the well will be located in an area of historical seismicity, additional requirements may be imposed by the Commission, typically additional geological study. 16 TEX. ADMIN. CODE §3.9(3)(C).

Commission rules require that notice of the application be provided to "affected persons," who, for notice purposes, are: "the owner of record of the surface tract on which the well is located; each commission-designated operator of any well located within one-half mile of the proposed disposal well; the county clerk of the county in which the well is located; and the city clerk or other appropriate city official of any city where the well is located within the municipal boundaries of the city." 16 TEX. ADMIN. CODE §3.9(5)(A). If the application is for a commercial disposal well, notice is also required to be provided to the record surface owners of adjoining tracts. 16 TEX. ADMIN. CODE §3.9(5)(B). Notice is also required to be published. 16 TEX. ADMIN. CODE §3.9(5)(D).

Notice of the application affords those receiving it the opportunity to protest the application. If no protest is timely received, the Commission will grant the permit without a hearing, assuming that the entire application meets Commission requirements. If a protest of an SWD permit application is made to the Commission within 15 days of the protestant's receipt of the application, the application must be heard by the Hearings Division. 16 TEX. ADMIN. CODE §3.9(5)(E)(i). The hearings process begins once the application is approved by Commission staff, and at the hearing, the applicant must prove all elements required by the Water Code.[22]

Since SWD permit applications are published, it has become common for SWD permit applications to be protested by those to whom notice of the application is not required. The Commission has been willing to consider whether these protestants ought to be allowed to invoke the (expensive and time consuming) hearings process and participate in any hearing. To have standing to protest an SWD permit application, a protestant must be an "affected person," which in this context means "a person who has suffered or will suffer actual injury or economic damage other than as a member of the general public or as a competitor, and includes surface owners of property on which the well is located and commission-designated operators of wells located within one-half mile of the proposed disposal well." 16 TEX. ADMIN. CODE §3.9(5)(E)(ii) (emphasis added). Of significant note: an adjacent surface owner, though entitled to notice of applications for commercial disposal authority, is not among those identified as affected by rule. If such a protestant's standing is challenged by a motion to dismiss, they are obligated to appear at a prehearing conference and put forth evidence in support of their status as an affected person, even though notice to them was required.

If an SWD Permit application is protested by someone with standing, a hearing will take place, the

[21] Because the practical requirements of Rules 9 and 46 are largely identical, this paper will cite only to Rule 9. Correlative provisions to these citations are also found in Rule 46.

[22] As a cautionary tale, *see* Oil & Gas Docket No. OG-21-00006770; Application of Drillogix Exploration LLC ("In presenting evidence, Drillogix was apparently not aware that the draft permit for the proposed well, standing alone, is not sufficient to show that the Application meets the statutory requirements. The Examiners cannot provide legal advice and generally refrain from aiding a party in the presentation of their case if doing so would be unduly prejudicial to another party. Without an evidentiary record supporting facts that the Application is compliant with the Commission's rules and applicable State of Texas statutes, the Examiners are compelled to find that there is no factual or legal basis for recommending approval of the Application.").

Hearings Division will issue a PFD, and the Commission will decide the case at Conference. During our 2022-2023 study period, this happened with 18 cases. In the majority of contested cases, even with technical opposition, the Commission votes to approve the application. This is not surprising; once an application reaches the hearing stage, Commission staff has already found that it meets technical and regulatory requirements.

2. Standing Issues

Disputes about standing to protest SWD permit applications have become commonplace at the Commission. *See, for example, NGL Water Solutions Eagle Ford, LLC v. Railroad Commission of Texas*, 2019 WL 6336178 (Tex. App. -- Austin 2019, no pet.) (mem. op.). The Commission's general practice now is to hold a prehearing conference in each contested SWD permit application docket, where motions to dismiss protests are taken up and the parties are set (or not) prior to the hearing on the merits.

Several years ago, Apache Corporation protested SWD permit applications in the vicinity of its Alpine High Field, even when these disposal wells, if permitted, would be further away than the one-half mile provided in the Rules.[23] In the first of these cases to be decided, the PFD recommended granting Apache standing and denying the applications. The Commissioners did not agree, and they granted the Motion to Dismiss Apache's protests, on the basis that Apache was too far away (3 miles) to be considered affected and thus have standing.[24] Apache filed a judicial appeal of this decision, and the Travis County District Court ruled in its favor, finding that the Commission erred in granting the Motion to Dismiss Apache's protests.[25] The Commission appealed, and the appeal was transferred to the 7th Court of Appeals, which reversed the Travis County District Court and affirmed the Commission's ruling that Apache did not have standing. *Railroad Commission of Texas v. Apache Corp.*, 2023 WL 2138962 (Tex. App. -- Amarillo 2023, pet. filed) (mem. op.).[26]

3. Delaware Basin Issues

Not surprisingly, many of the contested SWD permits are in the Delaware Basin, which is perhaps the most active drilling and production area in the state. A couple issues arise here, including: (1) concerns that injection will impact historical vertical production, and (2) concerns that injection will pressurize formations that must be drilled through to reach the target productive horizons.

In the Delaware Basin, the most common zone into which to inject is the Delaware Mountain Group ("DMG"), which is a group of three formations including, from top to bottom, the Bell Canyon, the Cherry Canyon, and the Brushy Canyon. The DMG sits above the Bone Spring and Wolfcamp formations, which are the primary current producing formations in the area. Historically, the DMG has been sporadically productive. It is not nearly as prolific as the deeper formations now able to be produced with hydraulic fracturing and horizontal wellbores.

Some SWD permit applications under Statewide Rule 46 have been protested on the basis that an SWD operator, if seeking authority to inject into a potentially productive zone, ought to be required to have authority from the mineral owner, and not just the surface owner. The Commission has recently rejected this argument.[27] The Commission has also rejected complaints from Wolfcamp operators worried that shallower injection will cause drilling challenges or delays, due to pressurization of the DMG.[28]

Due to the potential presence of historical DMG production, SWD permit applicants in the Delaware Basin (as anywhere) must pay careful heed to all plugged wellbores within a reasonable radius of their application, typically 1/2 mile. At hearing, applicants should be prepared to discuss each such wellbore, and explain why it will not be a conduit for flow, through wellbore schematics (based on plugging and cementing records) and potentially through pressure front calculations.

A number of complaints have also been filed by DMG producers, arguing that DMG injection has watered out their wells. None has come before the Commissioners, yet, but this is an issue to watch. As a policy matter, if the Commission were to deny SWD applications, or suspend existing permits, on this basis, it would profoundly curtail the more prolific deeper production, which requires significant injection capacity to be viable.

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[23] Apache argued that injected fluids will be able to migrate up into the fresh water zones, that they will contaminate those zones, and that Apache will be blamed, as its Alpine High field has prompted local interest in a part of Reeves County not otherwise experiencing active oil and gas development.

[24] Oil and Gas Docket 08-0317254.

[25] *Apache Corporation v. Railroad Commission of Texas*, Cause No. D-1-GN-20-001422, Before the 200th Judicial District Court, Travis County, Texas.

[26] Apache has filed a Petition for Review (Cause No. 23-0264) before the Supreme Court of Texas. The Supreme Court has requested briefing on the merits but had not ruled on the Petition at the time of submission of this paper.

[27] Oil and Gas Dockets 08-0320752 and 08-0320772.

[28] *See, for example*, Oil and Gas Dockets 08-0321458 and 08-0322180.

B. MIPA Cases

The Mineral Interest Pooling Act ("MIPA") has been utilized to great affect in recent years. The Commission has been willing to grant applications for forced pooling filed by operators to capture wholly unleased "window tracts" within the boundaries of voluntary pooled units. These applications are particularly helpful in the urban or quasi-urban environment, where the challenge of locating town lot owners can be daunting. This creative use of the MIPA started in the Fort Worth area with the *Finley* case some years ago, but it has recently taken off, both in the Barnett Shale area but also in West Texas. Operator-driven MIPA applications have allowed otherwise-impossible development in the cities and communities of Midland, Rankin, Pecos, Big Spring, and Barstow, in addition to Fort Worth. The Commission has issued 80 of these MIPA orders on the consent agenda during the time period from January 1, 2022 through November 15, 2023.

Almost all of these cases are uncontested, typically because the force pool-ees are not locatable. Nonetheless, the Commission carefully applies the requirements of the MIPA, which include a number of challenges to modern development, given the age of the statute. The MIPA does not allow an oil unit larger than 160 acres (plus 10% tolerance).[29] This makes MIPA units for modern wells quite skinny. The MIPA does not apply to any reservoir discovered and produced before March 8, 1961.[30] This initially made applying the MIPA in the Midland Basin tricky, but not impossible, though prior uncertainty on this point has seemingly been resolved.[31] Some of the Commission ALJs do not believe the MIPA allows for multi-well units, but others have ordered MIPA units which contemplate subsequent development.

The Commission has been more reluctant to approve "muscle-in" applications, where the applicant seeks to force pool their own tract into an existing unit.[32] All of these cases are, of course, contested, unlike the window tract cases, which is a significant factor. The recent trend began with the last couple *Ammonite* cases, in which the Commission ruled that a muscle-in applicant was required to prove, via technical testimony, that its tract was being drained by the existing well or wells. The Fourth Court of Appeals[33] affirmed a Commission order dismissing an Ammonite application, on the basis that Ammonite's offer to voluntarily pool was unreasonable due to an inadequate proposed charge for risk. *Ammonite Oil and Gas Corporation v. Railroad Commission*, 04-20-004650CV (Tex. App. -- San Antonio 2021, pet. granted) (mem. op.). Ammonite filed a Petition for Review, which the Supreme Court granted; the Court held oral argument in the case on September 13, 2023.[34] No opinion has been issued as of the time of submission of this paper, but based on oral argument, (a) the Court did not seem inclined to take the same approach followed by the San Antonio Court of Appeals, even if it ultimately affirms, and (b) the Court did seem troubled by the possibility of riverbed stranding.

The Commission has recently denied another muscle-in application, for the same reasons as articulated in the *Ammonite* cases, plus some others.[35]

Nonetheless, for an operator with a challenging window tract holdout, or perhaps simply some un-findable mineral owners, the MIPA remains a viable option, and one with which the current Commission ALJs are familiar. The sense of uncertain and dread which used to accompany discussions of embarking on a MIPA application may no longer be apt.

C. End-of-Life Issues: Inactive Wells and Good Faith Claims

In 2009, the Legislature required the Railroad Commission to enact an inactive well rule, to address issues related to long-inactive marginal wells. The Rule has been codified as Statewide Rule 15, and it basically sets out a number of requirements that an operator must meet, depending on how long a well has been inactive, in order to maintain an exception to the requirement that the well be plugged. The Rule also requires each operator to plug or return to active status 10% of its inactive wells each year, as a condition to renewing its P-5.

A corollary to Rule 15 is the Good Faith Claim complaint. Even when otherwise compliant with Rule 15, an operator is not eligible for a plugging extension unless it has "a good faith claim to a continuing right to operate the well." 16 TEX. ADMIN. CODE §3.15(e)(3).

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[29] TEX. NAT. RES. CODE §102.011.

[30] TEX. NAT. RES. CODE §102.003.

[31] The Spraberry (Trend Area) Field was created as a consolidation of earlier fields in 1952, but the Wolfcamp reservoir was not added to it until the 1990s. The MIPA has been successfully used to create units in this field, but at least one case rejected MIPA applications on the basis of proximate pre-1961 production. The Commissioners have since indicated a willingness to allow MIPA to be used in the STA Field. *Applications of Sinclair Oil & Gas Company*, OG-22-00009049.

[32] See Ronnie Blackwell, *The Mineral Interest Pooling Act: A Case Study of the Last Five Years*, Section Report of the Oil, Gas & Energy Resources Law Section of the State Bar of Texas, Vol. 43, No. 4 (December 2019). Blackwell's paper is discussed in some length in Smith & Weaver's Texas Law of Oil and Gas.

[33] Appeals of MIPA orders go to the County where the well is located, not to Austin.

[34] Cause No. 21-1035 before the Supreme Court of Texas.

[35] Oil & Gas Docket No. OG-21-00006266; *Application of Caliber Oil & Gas, LLC*

That, in turn, is defined as "A factually supported claim based on a recognized legal theory to a continuing possessory right in a mineral estate, such as evidence of a currently valid oil and gas lease or a recorded deed conveying a fee interest in the mineral estate." 16 TEX. ADMIN. CODE §3.15(a)(5). And so, any interested party (normally a landowner or top-lessee) can file a Good Faith Claim complaint with the Commission, which will then require the operator to produce some evidence of its good faith claim. While the Commission cannot, and will not, adjudicate title, it absolutely will require an operator to put forth its evidence of a valid leasehold, through this process.

Frequently, operators, for whatever reason, simply do not respond to these orders from the Commission requiring them to submit their evidence of a good faith claim. In 2022-2023, the Commission adjudicated 311 of these cases on the consent agenda, meaning that the operator did not respond to the complaints. In these cases, the Commission normally issues an order finding that the operator does not have a good faith claim to operate the wells, and requiring that the wells be plugged. The consequences of ignoring Commission mail are significant.

During 2022-2023, the Commissioners adjudicated 19 disputed Good Faith Claim cases. In actually disputed Good Faith Claim cases, it is not terribly difficult for an operator to meet its burden, but the operator must try. It is not the Commission's mandate to adjudicate title, only to see if an operator is willing and able to explain why it thinks it still has a lease. Similarly, the Commission normally cannot adjudicate between competing good faith claims; if the parties are fighting about what a lease or contract means, but both agree it applies, the Commission normally finds that a good faith claim exists. In defense against a Good Faith Claim complaint, an operator normally presents its claimed oil and gas lease, plus an explanation of any gaps in production. Generally, Commission decisions on contested Good Faith Claim complaints are fact-specific and roughly split between the operator and the complainant.

The Commission also adjudicates contested Single-Signature P-4 cases. A Railroad Commission form P-4 is the form that indicates which operator is responsible for each well in Texas. When a well transfers from one operator to the next, a new P-4 is filed, which normally contains the signatures of both the previous operator and the new operator. When a dispute arises as to who has the right to operate a well, such as in the top-lease situation, the new operator claiming the right submits a Single-Signature P-4 -- that is a P-4 without the prior operator's consent -- and the Hearings Division hears the claim.

A Single-Signature P-4 case resembles a Good Faith Claim complaint in that the issue is whether the current operator still has good faith claim of right to operate the well. The claiming new operator should also be prepared to prove its own good faith claim. As with the Good Faith Claim complaints, many of these are adjudicated on a default basis, and the decisions on the contested Single Signature P-4 cases are roughly split.