

**BEFORE THE CORPORATION COMMISSION
OF THE STATE OF OKLAHOMA**

✓
12/5
APPLICANT: MARATHON OIL COMPANY) CAUSE CD NO. 201601631
)
RELIEF SOUGHT: POOLING - MULTI-UNIT)
HORIZONTAL WELL)
)
LEGAL DESCRIPTION: ALL OF SECTION 17,)
TOWNSHIP 15 NORTH, RANGE 13 WEST,)
BLAINE COUNTY, OKLAHOMA)

FILED
OCT 04 2016

COURT CLERK'S OFFICE - OKC
CORPORATION COMMISSION
OF OKLAHOMA

REPORT OF THE ADMINISTRATIVE LAW JUDGE

On 24 August 2016, this cause came on for hearing before Patrick O. Colaw, Administrative Law Judge (ALJ) for the Corporation Commission (Commission) of the State of Oklahoma, in the Commission's Courtroom, Jim Thorpe Building, Oklahoma City, Oklahoma, pursuant to notice given as required by law and the rules of the Commission for the purpose of taking testimony and reporting to the Commission.

SUMMARY OF THE CASES:

Marathon Oil Company (Marathon) has the right to drill in Section 17 and seeks to pool the Mississippian, Hunton, and Woodford common sources of supply as part of a multiunit well in Sections 17 and 20, Township 15 North, Range 13 West. Mustang Fuel Corporation (Mustang) also owns an interest in Section 17 and protests the cause. According to the Pre-Hearing Conference Agreement, the disputed matters are fair market value, operations, elections, and well costs. However, before the cause was opened, Mustang narrowed its protest to elections and well costs--with the belief the issue of well costs would be resolved after some evidence was presented. It was resolved, leaving only the issue of alternate operatorship.

The only matter at issue is operatorship; specifically, Mustang seeks to be an alternate operator of Section 17. Marathon has commenced drilling operations in Section 20, immediately south of Section 17, on the Trace Tillman BIA 1-20-17XH Well which is part of a multiunit horizontal well running south to north.

RECOMMENDATIONS:

It is the recommendation of the ALJ that the Application of Marathon Oil Company in Cause No. 201601631 be granted and Applicant be named the unit operator in Section 17, Township 15 North, Range 13 West, Blaine County, Oklahoma.

APPEARANCES:

Robert A. Miller, attorney, appeared on behalf of Applicant, Marathon Oil Company (Marathon)

David E. Pepper, attorney, appeared on behalf of Protestant, Mustang Fuel Corporation (Mustang)

Richard K. Books, attorney, appeared on behalf of an interested party, Echo Energy, LLC.

FINDINGS AND SUMMARY OF EVIDENCE:

A. The following numbered exhibits were offered by the Applicant and accepted into evidence in Cause CD No. 201601631:

1. Amendment to Exhibit "A" (entitled *List for Force Pooling Hearing*), dated 15 August 16, and an Entry of Appearance and Waiver of Notice for Gallaspy Oil Properties (two pages).
2. Authorization for Expenditure (AFE), dated 22 August 16 (one page).

B. Applicant called **Brandon Jenkins** to give testimony. Mr. Jenkins testified he is a landman employed by the Applicant. Mr. Jenkins sponsored Exhibits 1 and 2. The entirety of his testimony is contained in the transcript of the proceedings.

1. Under direct examination, Mr. Jenkins testified Marathon filed an application for forced pooling in Section 17 on 24 April 2016. A proposal letter was sent on 4 April 2016. In Section 17, Marathon owns 160 acres and Mustang owns 404 acres. In Section 20, Marathon owns 400 acres and Mustang owns no acreage. In the multiunit (Sections 17 and 20 combined), Marathon owns 43.75% and Mustang owns approximately 33%.

2. Mr. Jenkins testified the common sources of supply Marathon seeks to pool are the Mississippian, Woodford, and the Hunton. The fair market value (FMV) of the common sources of supply in Section 17 is \$2,000 per acre and a 3/16 royalty, \$1,500 per acre and a 1/5 royalty, or \$750 per acre and a 1/4 royalty. These values represented the highest and best values in the 8 surrounding sections. On 27 April 2016, another entity took a three year lease in Section 9 for \$3,500 per acre and 1/5 royalty for all formations. Mr. Jenkins testified this lease was not indicative fair market value as it included all formations ("surface to basement") and had a term of 3 years. Mr. Jenkins added the values offered for Section 17, the "toe" or bottom hole of the horizontal well, are the same as the values offered for Section 20, the surface location for the multiunit.

3. Mr. Jenkins testified he used due diligence to locate each party. He testified the well has commenced drilling and Marathon requests a time frame of 20 days to make elections, 25 days to pay costs, and 35 days to pay bonus for the initial well.

4. Furthermore, he testified only parties participating in the initial well will be eligible to propose and/or participate in any subsequent well.

5. On cross examination, Mr. Jenkins confirmed a portion of the costs in the AFE included the drilling of a pilot hole in Section 20 and agreed Mustang would have access to the corresponding well information if they participated in the well. Additionally, Mr. Jenkins confirmed the target of the well is the Meramec interval of the Mississippian common source of supply and the Hunton is a possible candidate for future development. He did not know the plans for the Woodford. Mr. Jenkins confirmed Mustang owned in Sections 17 and 8 but not Section 20 and Marathon did not own in Section 8.

6. On further cross examination, Mr. Jenkins stated Marathon objected to an alternate operator for a subsequent well in Sections 17 and 8 because Marathon is taking all the risk in Section 17 by drilling the initial well. He substantiated his opinion based upon the fact there is not much development in the area and the well was somewhat of a "step-out" well, similar to a wildcat as there was not much horizontal development in the area. He agreed with Mustang's counsel that no reason exists which would prohibit Mustang from proposing a subsequent multiunit well in Section 17 to Section 8.

7. On continued cross examination, Mr. Jenkins testified since the well has commenced, the order should provide that Marathon will continue to operate the well in a normal, prudent manner.

8. In response to the ALJ's questions, Mr. Jenkins testified the proposal letters to the respondents included an AFE for approximately \$12 million instead of the approximate \$10 million AFE offered during the hearing. He was unsure if the \$10 million AFE was provided to the respondents. He confirmed that Mustang has not filed an application for a multiunit well, location exception or any other filing in Sections 8 or 17 as of 23 August 2016.

9. On redirect examination, he clarified his opinion stated above, that no reason exists which would prohibit Mustang from proposing a subsequent multiunit well in Section 17 to Section 8, was from the perspective of a landman.

10. On re-cross examination, Mr. Jenkins agreed Marathon does not own in Section 8, the section north of Section 17, and Mustang has the right to propose a well from Section 17 into Section 8. He was asked, hypothetically, about operatorship if Mustang filed an application for a multiunit and location exception for Sections 17 and 8, with Marathon owning nothing in Section 8, and he stated Mustang would be the logical operator.

11. During the testimony of Mr. Jenkins, the parties stipulated Mustang and Marathon would enter into a joint interest billing arrangement for the Tillman Well.

C. Applicant called **Matt McGuire** to give testimony. Mr. McGuire testified he is a geophysicist. Mr. McGuire has testified before the courts of the Commission on more than one occasion and has had his qualifications as an expert in the field of geophysics accepted. The entirety of his testimony is contained in the transcript of the proceedings.

1. Mr. McGuire testified a pilot hole was drilled in Section 20 to the Hunton then back up to evaluate the Meramec interval of the Mississippian and the Woodford common sources of supply. The pilot hole was necessary to find the best "landing zone" or placement for the wellbore and to evaluate the formations because no vertical offset controls exist to evaluate the reservoir quality of the Meramec and Woodford.

2. He testified about the potential for development in the "up hole" formations (Springer, Marrow, Cherokee (Red Fork), Hoxbar, Penn Sands, Tonkawa, and Cottage Grove); however, he testified it was hard to quantify the value of the "up hole" formations.

3. Mr. McGuire testified the nearest Mississippian, Woodford, or Hunton wells are over 6 miles away. According to his examination, no Mississippian horizontal wells exist in Blaine County. He described the current well as a "step out" well, similar to a wildcat well with much risk involved.

4. On cross examination, he testified that there are currently no horizontal Mississippian multiunit wells in Blaine County. However, there were eight or nine applications by Marathon granted for Meramec horizontal multiunit wells. He confirmed the concept of alternate operator in the same section has been approved in the past but not within the same formation (common source of supply).

5. On redirect examination, he testified Marathon does not oppose Mustang pursuing a multiunit well in Sections 8 and 5, both north of Section 17.

6. Responding to the ALJ's questions, Mr. McGuire reiterated his testimony of the value of the multiunit development is the most economic way to develop the section but single unit development is still economic.

7. On redirect, Mr. McGuire agreed a single section well for Mustang in Section 8 is still economic.

8. On re-cross, Mr. McGuire agreed a single section well for Marathon in Section 20 is still economic.

D. Applicant called **Rick Gaddis** to give testimony. Mr. Gaddis testified he is a petroleum engineer working as a completion engineer. The entirety of his testimony is contained in the transcript of the proceedings.

1. Mr. Gaddis testified he opposed another operator drilling a multiunit well from Section 8 to 17. This scenario could interrupt the timing of drilling and completing the wells. One concern is the possibility of a collision if the wells are drilled "toe to toe".

2. On cross examination, Mr. Gaddis agreed he remembered a circumstance in which two operators were named in the same section. He distinguished that circumstance because the operators were designated for different formations. He stated Marathon has not drilled a Hunton

well. Mr. Gaddis was asked if he would "feel better" about an alternate operator scenario in Section 17 if the parties were ordered to consult before operations. He responded in the negative.

3. On redirect, Mr. Gaddis underscored the point that the two operator scenario in the same section was in two separate formations.

4. In response to the ALJ's questions, Mr. Gaddis testified the Tillman Well is located in the west half of the unit with the surface location situated in the southwest quarter of Section 20. Additionally, he provided the plan was for Marathon to develop the unit from west to east and he anticipated a fifty percent allocation to each section.

E. Following Mr. Gaddis' testimony, the Applicant rested its case.

F. Protestant called **Steven Mark Kane** to give testimony. Mr. Kane testified he is a petroleum engineer and the Director of Engineering at Mustang. Mr. Kane has testified before the courts of the Commission on more than one occasion and has had his qualifications as an expert in the field of engineering accepted. His qualifications were accepted without objection. The entirety of his testimony is contained in the transcript of the proceedings.

1. On direct examination, Mr. Kane testified Mustang seeks to drill a multiunit well in Section 17 and 8 because they have positions in both sections and they have supporting parties in Section 8. Additionally, he testified Mustang has participated in approximately 30 horizontal wells if you include the Woodford. He testified Mustang is capable of drilling a multiunit horizontal well from Section 17 to 8 and have drilled 12 horizontal wells to date but none are in Kingfisher, Blaine, or Canadian Counties.

2. He stated Mustang should be named an alternate operator and would cooperate with others in the unit to avoid collisions in the unit. Mustang has an approximately 33% interest in the Tillman Well which is approximately a \$3 million dollar stake in the well. He stated this large interest re-emphasizes Mustang's motivation to "pay attention" and not jeopardize the production of the well in which they own such a large percentage.

3. On cross examination, Mr. Kane confirmed Mustang has owned and operated vertical wells in Section 17 for over 30 years yet just completed the plans for a multiunit well in Sections 8 and 17 on the Friday before the hearing [19 August 2016]. Also, he confirmed Mustang has never drilled a Meramec well. Mustang has drilled a Woodford well in Major County and three of four horizontal wells in the four county area.

4. Mr. Kane could not specify if Mustang's plan to develop the section would occur in the next several months or several years. When asked if Mustang had considered a single unit lateral, Mr. Kane responded Mustang had considered both single and multiunit wells.

5. When asked about including a provision in the order to cooperate with other operators in the section, he agreed with the premise that it could be a difficult provision to enforce.

6. On redirect examination, he testified a multiunit horizontal well is more economical because Mustang would be able to maximize its ownership in the section and capture the biggest acreage.

7. In response to questions from the ALJ, Mr. Kane testified he was unaware if Mustang received notice of Marathon's application for a multiunit well. Also, when asked about Mustang's record with regard to operational compliance issues, he stated was unaware as he had only been employed by Mustang for less than one year.

G. Following Mr. Kane's testimony, the Protestant rested its case.

H. Having heard the testimony of the witnesses and after reviewing the evidence submitted, the ALJ took the cause under advisement and closed the record.

RECOMMENDATIONS AND CONCLUSIONS:

In the present case, Marathon seeks to pool the mineral interests of owners in the Mississippian, Woodford, and Hunton common sources of supply and to be named the operator of the unit well in Section 17 as part of a multiunit well in Sections 20 and 17. Marathon's intended target is the Meramec interval of the Mississippian common source of supply. Mustang seeks to be named an alternate operator in the same drilling and spacing unit and the same formations in Section 17.

After taking into consideration all of the testimony, facts, circumstances, and evidence presented in these causes, it is the recommendation of the ALJ that the application of Marathon be granted.

In accordance with OAC 165:5-7-7, an applicant seeking to pool the interest of mineral owners shall: (1) present evidence they exercised due diligence to locate each respondent and that a bona fide effort was made to reach an agreement with each such respondent as to how the unit would be developed; (2) give proper notice of the hearing for a pooling order no less than fifteen (15) days prior to the date of the hearing upon each respondent; (3) publish notice of the hearing pursuant to 165:5-7-1(n)(2); and (4) offer into evidence a AFE which was prepared or revised within forty-five (45) days of the date of the hearing.

In the present pooling application, the Applicant presented substantial evidence satisfying each element of OAC 165:5-7-7. Undisputed testimony was presented that the Applicant has ownership and right to drill in Section 17. The Applicant exercised due diligence in attempting to locate each respondent and made a bona fide effort to reach an agreement with each respondent as to how the unit would be developed¹. Further, notice was proper on the respondents as well as with the publications in Blaine and Oklahoma counties. Finally, Applicant presented an AFE (reviewed within 45 days of the hearing) into evidence.

¹ The record reflects Marathon sent an initial well proposal to the respondents which included an AFE for \$12 million. The AFE offered at the hearing is for \$10 million.

Marathon has presented substantial evidence supporting its pooling application. The only issue left to consider is operatorship.

Often, when determining the operator of a drilling and spacing unit under a pooling application, the party with the largest interest is designated as the operator. However, that trend is not the law. Instead, the legislature leaves designating an operator to the discretion of the Commission. The Commission is granted wide latitude in determining the operator.

To aid the Commissioners, the ALJ serves as the initial finder of fact. It is the duty of the ALJ, as the fact finder, to observe the demeanor of the witnesses, assess their credibility, and assign appropriate weight to their opinions. *Grison Oil Corporation v Corporation Commission*, 99 P.2d 134 (Okla. 1940). The Supreme Court in *Texas Oil and Gas Corporation v Rein*, 535 P.2d 1277 (Okla. 1974) provides that it is in the wide discretion of the Commission to name an operator.

To aid in making a recommendation to the Commissioners, the nonexclusive and purely persuasive factors discussed in Charles Nesbitt's insightful article, *A Primer on Forced Pooling of Oil and Gas Interests in Oklahoma*,² are considered and discussed below.

Unit Interest - In Section 17, Marathon owns 160 acres while Mustang owns 404 acres. In the northern adjacent section, Section 8, Marathon owns 0 acres while Mustang owns 20 acres. In the southern adjacent section, Section 20, Marathon owns 400 acres while Mustang owns 0 acres. Clearly the majority of the acreage in Section 17 is owned by Mustang.

Experience - It was undisputed during the hearing that Marathon has more experience with horizontal wells and multiunit horizontal wells than Mustang. Evidence was presented that Mustang has participated in numerous horizontal wells and has drilled some horizontal wells. However, it was clear from the testimony that Marathon has more experience with horizontal wells.

Plan of Development - Marathon has a plan of development for the multiunit and has commenced its first well in the multiunit. Mustang presented no plan of development; it only referenced an AFE for a multiunit well in Sections 17 and 8 which was very recently created. Furthermore, Mustang could not state if the development would occur in the next several months or several years.

Rig Contract - At the time of the hearing, Marathon had a rig drilling the Tillman Well. No evidence was presented by Mustang about the status of a rig contract.

AFE - Marathon offered an AFE for the Tillman Well with a completed for production expense of \$10,471,102. Mustang did not offer an AFE³.

² 50 Okl. B.J. 648 (1979)

³ The reason for Mustang's failure to offer an AFE may have been due to the nascency of the AFE and missing the document exchange deadline for the protested cause.

In addition to the Nesbitt factors above, I also considered two other factors which I call the *Virgil*⁴ factor and the *Laches*⁵ factor.

Virgil - Marathon is taking great risk in a "step out" well. It has proposed and commenced the \$10 million dollar well as the first well in a full section development plan in an otherwise unproven horizontal prospect. Great credit toward operatorship should be given the venturing party.

Laches - Mustang has owned in Section 17 for over thirty (30) years and has developed the section vertically but has not created a horizontal development plan for Section 17. Mustang only prepared an AFE for a multiunit well in Sections 17 and 8 days before the hearing and has not filed any applications with the Commission pertaining to a multiunit well or location exception in this section.

Evaluating the factors above, the scales dip in favor of Marathon.

The concept of an "alternate operator" is mentioned in OAC 165:5-7-11(b) Designation of Operator Under a Forced Pooling Order: "Each order forced pooling the rights and equities in a drilling and spacing unit shall designate at least one operator to operate the well or unit. In addition, the Commission may designate one or more alternate operators in the order." (emphasis added).

No further mention of the phrase is found in the Commission rules nor does the case law provide any insight.⁶ Each time the witnesses were confronted with the phrase by Mustang, each witness explained they have never seen an alternate operator be named in the same target formation in the same drilling unit. Because the discretion to designate "one or more alternate operators" is not necessary in this circumstance, I do not recommend an alternate operator be designated.

The overarching mandate for the Oklahoma Corporation Commission is the prevention of waste and protection of the correlative rights of interested parties.⁷ In the present cause, the substantial evidence portrays an intrepid operator seeking to explore a prospect in an otherwise unproven horizontal spacing unit. By seeking to develop this section horizontally, Marathon is protecting the correlative rights of mineral owners and preventing actual and economic waste.

Marathon is protecting the correlative rights of not only Mustang and Marathon but also all other minority interest owners in the section by developing unexplored hydrocarbons. Furthermore, by developing the multiunit horizontally, a greater portion of the target interval will be able to be developed and produced which prevents hydrocarbons from remaining in place, or actual waste. Economic waste is mitigated by drillings a multiunit horizontal well in which only

⁴ Referencing the Roman poet, Vergil, who famously wrote "fortune favors those who dare."

⁵ While not applying the equitable theory of law to the present facts, I analogize to the legal theory which stands for the principle that equity aids the vigilant, not those who slumber on their rights.

⁶ The phrase is used in *Inexco Oil Company v Commission*, 767 P.2d 404, 1988 OK 78; however the functional concept is not discussed.

⁷ Paraphrased from 52 O.S. 87.1(a)

one vertical well bore, one surface road, one surface location, and one pipeline is necessary for nearly two miles of horizontal production.

After taking into consideration all of the facts, circumstances, evidence and testimony presented in this cause, it is the recommendation of the ALJ the recommends Cause No. 201601631 Pooling Application of Marathon be granted and they named the unit operator in Section 17, Township 15 North, Range 13 West, Blaine County, Oklahoma.

It is my determination that it is in the best interest of parties being pooled and is the best option to effect the prevention of waste and protection of correlative rights.

RESPECTFULLY submitted this 5th day of October, 2016.



Patrick O. Colaw
Administrative Law Judge

cc: Robert A. Miller
David Pepper
Richard K. Books
Michael L. Decker, OAP Director
Oil Law Records
Court Clerk
Commission Files