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CORPORATION COMMISSION
OF OKLAHOMA

BEFORE THE CORPORATION COMMISSION
OF THE STATE OF OKLAHOMA

APPLICANT:	**BAYS EXPLORATION, INC.**	)
RELIEF SOUGHT:	**POOLING**	) **CAUSE CD NO. 201105614**
LEGAL DESCRIPTION:	**SE/4 SECTION 7, TOWNSHIP 6 NORTH, RANGE 4 WEST, MCCLAIN COUNTY, OKLAHOMA**	)

CORRECTED REPORT OF THE OIL AND GAS APPELLATE REFEREE

This cause came on for hearing before **Susan R. Osburn**, Administrative Law Judge ("ALJ") for the Oklahoma Corporation Commission, at 8:30 a.m. on the 8th day of February, 2012, 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 purpose of taking testimony and reporting to the Commission.

A Motion to Reopen this cause came on for hearing also before Susan R. Osburn, ALJ, at 9:00 a.m. on the 25th day of May, 2012 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.

APPEARANCES: **David E. Pepper**, attorney, appeared on behalf of applicant, Bays Exploration, Inc. ("Bays"); **Gregory L. Mahaffey**, attorney, appeared on behalf of Newfield Exploration Mid-Continent, Inc. ("Newfield"); and **Jim Hamilton**, Assistant General Counsel for the Conservation Division, filed notice of appearance.

The ALJ issued her Report of the ALJ on the 8th day of March, 2012 to which Exceptions were timely filed and proper notice given of the setting of the Exceptions.

The ALJ issued her Oral Ruling on the Motion to Reopen on the 25th day of May, 2012 to which Oral Exceptions were timely lodged and proper notice given of the setting of the Exceptions.

The Appellate argument concerning the Exceptions to the ALJ's Report were referred to **Patricia D. MacGuigan**, Oil and Gas Appellate Referee ("Referee"), on the 21st day of May, 2012.

The Appellate argument concerning the Motion to Reopen Oral Exceptions was referred to **Patricia D. MacGuigan**, Referee, on the 15th day of June, 2012.

The Appellate Referee issued her Report on the 24th day of July, 2012 however due to copying error the Report of the Referee is being remailed so all report pages are included.

After considering the arguments of counsel and the record contained within this Cause, the Referee finds as follows:

STATEMENT OF THE CASE

NEWFIELD takes exception to the ALJ's recommendation in her March 8, 2012 Report that fair market value be established as $150 an acre and a 3/16 royalty or no cash and 1/5 total royalty as fair market value. Newfield also appeals the recommendation that the pooling order should not distinguish between vertical development and later horizontal development.

CD 201105614 is the application of Bays seeking pooling authority for the SE/4 of Section 17, T6N, R4W, McClain County, Oklahoma for the Prue, Hart, Skinner, Red Fork, Mississippi Lime, Misener-Hunton, Viola, Bromide Dense, First Bromide, Second Bromide, McLish, Joins, Osborne and Arbuckle common sources of supply which were all spaced on a 160-acre order basis by Orders 175592 and 287585. The issue in this cause, as first stated, was the impact of this pooling application for a vertical well on parties who did not participate in the vertical well but would want to participate when later horizontal development occurred. Newfield questioned whether upon non-participation they would be entitled to participate in later horizontal wells or whether their interests would be pooled in the formation as vertically spaced. During the course of the hearing, it turned out that fair market value also became an issue, with the landman for Bays recommending a certain cash bonus amount and royalty based on his search of transactions in the area and a separate recommendation based on a statement by the attorney for Newfield. No witnesses were presented for Newfield and both sides stated their reasons for recommending fair market value in the cause. As to the issue about vertical development and later horizontal development and the impact of non-participation in the initial vertical well, both attorneys indicated there was no

case law regarding this issue, and Bays' attorney argued that such an issue was premature in this cause.

Bays appeals the ALJ's recommendation that Newfield's May 11, 2012 Motion to Reopen be granted. Newfield requested that the cause be reopened for the taking of additional evidence concerning fair market value. At the time of the hearing, Newfield expected the landman for Bays to have determined the actual prices paid for the Newfield leases in and around the subject quarter section. However, Bays' contract landman testified that "[he] cannot find out the cash bonus" for the Newfield leases. He did acknowledged that Newfield had taken a number of leases between June 11, 2010 and August 21, 2011 in units contiguous to the SE/4 of Section 7 and had also taken a lease from Fleischaker Royalty for a 1/5th royalty in the SE/4 of Section 7. Bays' landman admitted that he did not contact Newfield and that he had not contacted Hal Smith, Newfield's broker, to inquire about what they had paid for leases in the area. Newfield asserts that it would be in the interest of justice and protection of correlative rights for the Commission to take additional evidence as to the actual amounts paid for leases in and around the subject tract in determining fair market value options for respondents not wishing to participate.

Thus, Newfield requested the Commission to reopen the record in the cause for the taking of additional evidence regarding fair market value.

NEWFIELD'S POSITION CONCERNING THE MARCH 8, 2012 ALJ REPORT:

1) The Report of the ALJ is contrary to the evidence, it is contrary to the law and fails to protect correlative rights or prevent waste of hydrocarbons.

2) The ALJ erred in setting $150/acre and 3/16th royalty or no cash and 1/5th royalty as fair market value. The Bays contract landman, John Rice, testified that Newfield owned a 40 acre lease located in the subject SE/4 of Section 7 taken from Fleischaker Royalty during the second quarter of 2011 for a 1/5th royalty. Mr. Rice also testified that Newfield had taken a number of additional leases between June 11, 2010 and August 21, 2011, in units contiguous to the SE/4 of Section 7, for 3/16th royalty. Mr. Rice testified that he "cannot find out the cash bonus" for the Newfield leases. However, Mr. Rice admitted that he had not contacted Newfield and admitted that he had not contacted Hal Smith, Newfield's broker, to inquire what they had paid for leases in the area. The ALJ erred in not taking a recess and/or in not requiring that Mr. Rice contact Newfield and Hal Smith to "find out" what cash bonus was paid for Newfield's leases, many of which were taken later than Bays' June 24, 2011, lease in the SE/4. An applicant for a pooling, a quasi condemnation proceeding under the police powers of the State, cannot simply "put his head in

the sand" and testify that he could "not find out" what current bonuses are being paid in the relevant nine-section area. Although, Mr. Rice said he talked to Fleischaker, he did not contact any of the other mineral owners leased to Newfield regarding the bonus received. If Mr. Rice had contacted Newfield, Hal Smith, or the numerous mineral owners, he would have discovered that substantially more money was paid than $150/acre or a 3/16th royalty and that $600/acre was paid by Newfield for a 1/5th royalty.

3) The ALJ erred in sustaining Bays' objection to a question by Newfield's counsel to Joe Bays regarding retention by Newfield of its rights for horizontal development for the Mississippi and Hunton, even if Newfield did not participate in Bays' proposed vertical well. The ALJ stated that the issue presented by the above question was "not part of a typical pooling order." However, the undisputed evidence and position of Newfield was that it purchased its leasehold for the primary purpose of horizontal development in the Mississippi, Woodford (not named in this pooling) and the Hunton. 52 O.S. Section 87.1 (e) requires pooling orders to be on such terms as will protect the correlative rights of all owners and as will allow each owner to recover his share of production without undue expense. The question posed to Mr. Bays is relevant to what plan of development will allow Newfield to recover its fair share of oil and gas from the Mississippi and Hunton through contemplated horizontal drilling.

4) The ALJ erred in ruling that the pooling order should not distinguish between vertical development and later horizontal development. At the time of the Supreme Court ruling in *Amoco v. Corporation Commission* 752 P.2d 835 (OK CT APP 1987, cert denied 1988), there was not much, if any, horizontal drilling in Oklahoma. Our horizontal amendment to the Spacing Statute, 52 Okla. Stat. Section 87.1, and to the OCC Rules, contemplates that horizontal spacing can coexist with existing vertical spacing in producing vertical units and that it will supersede vertical spacing in undeveloped units. Certainly, "unit pooling" does not preclude this Commission from implementing a plan of development that will protect both the owners desiring vertical development and owners desiring horizontal development of the same common source of supply. The ALJ erred in not finding that Newfield could elect a non-participation option in the Mississippi and Hunton for Bays' vertical well, but Newfield would retain its right to horizontally develop those common sources of supply in contemplated horizontal wells to be drilled in a 640-acre horizontal unit to encompass all of Section 7.

5) The Report of the ALJ should be reversed and the case reopened to require Bays to testify about the prices paid for non-Bays leases in the nine-section unit area. The Report of the ALJ should also be reversed and a plan of development ordered that will allow Newfield to reserve its rights to participate in horizontal wells drilled in the SE/4 of Section 7 or lands spaced therewith as to the Mississippi and Hunton.

THE ALJ FOUND IN HER MARCH 8, 2012 REPORT OF THE ALJ:

1) After taking into consideration all the facts, circumstances, evidence and testimony presented in this cause it is the recommendation of the ALJ that the Commission issue an order pooling the Prue, Hart, Skinner, Red Fork, Mississippi Lime, Misener-Hunton, Viola, Bromide Dense, First Bromide, Second Bromide, McLish and Osborne common sources of supply in the SE/4 of Section 7-T6N-R4W, McClain County, Oklahoma. As to the undisputed issues including operator, timeframes, deeming, and well cost that the order include the terms as recommended by Bays. As to the disputed issue regarding fair market value the record includes Bays' landman's testimony under oath regarding his investigation for and recommendation of fair market value for this pooling. On the other hand Newfield presented no witness and the record contains only a statement by Newfield's attorney about fair market value as related to him from a landman at Newfield. It was Newfield's position that contacting Fleischaker, who leased to Newfield, was not sufficient investigation of fair market value and that the Commission should continue the hearing and send Bays' landman out to inquire of Newfield or of Newfield's broker about the transaction. The ALJ notes that more often the more sophisticated industry parties, including brokers, companies, operators or owners of extensive mineral interests, will not reveal transaction amounts. Newfield was one of the parties involved in the Fleischaker transaction in question and had received a Bays' proposal letter so if they wanted to dispute values they had notice and opportunity to appear. It was not even apparent that fair market value was an issue until Newfield's attorney began cross examination of Bays' landman. In reliance upon the testimony taken under oath from the Bays' witness it is the recommendation of the ALJ that fair market value be established as a $150 per acre and a 3/16th royalty or no cash and a 1/5th total royalty.

2) As to the issue of whether nonparticipation under a pooling order for a vertical development would deprive a party of future participation in horizontal development, both sides indicated this is an issue that has not been addressed by the Supreme Court. It is the opinion of the ALJ that until the Supreme Court revisits the unit pooling issue and makes a distinction between pooling for vertical development and pooling for horizontal development that the *Amoco v. Corporation Commission*, 751 P.2d 2003 (Okl.Civ.App. 1986) would apply. Therefore, it is the opinion of the ALJ that this order would be a unit pooling for all named formations without any distinction of vertical versus horizontal development.

THE ALJ FOUND CONCERNING NEWFIELD'S MAY 11, 2012 MOTION TO REOPEN:

1) **ALJ Osburn** stated she heard this case as a protested cause in February 2012. The only issue shown on the Prehearing Conference Agreement ("PCA") dealt with whether Newfield could participate in a subsequent horizontal well if they chose not to participate in a vertical well in the pooled area. The ALJ issued a report regarding this on March 8, 2012. During the protested hearing it became evident that Newfield did not agree with the fair market value recommendation by Bays. Newfield did not bring a witness for fair market value. Bays' witness testified there were "some transactions out there for 'something' and one-fifth." Bays' witness testified they did not contact Newfield or Newfield's brokers because as competitors they would not reveal their bonus value. The ALJ stated she has heard the argument that competitors will not reveal their respective bonus values to one another, and further the ALJ believes this practice of nondisclosure to competitors is reasonable.

2) Newfield then moved to continue the cause. The ALJ stated she denied the motion to continue because it was not an issue present on the PCA. Newfield did not bring in a witness and Bays proceeded with the witness they had available.

3) After an appeal was filed, Newfield filed a Motion to Reopen on May 11, 2012. Bays argued there was no reason to reopen because Newfield had the opportunity and should have had their own witness at the hearing. Newfield argued the Commission relies specifically on these witnesses for fair market value. Newfield also argued that when such witnesses fail to adequately do their job, the Commission is relying on unreliable information.

4) The ALJ then recommended granting the Motion to Reopen. The ALJ contends she did not feel either side was in the right. Newfield should have brought a witness as well as made the issue of fair market value part of their prehearing conference agreement. Bays' landman witness should have checked all potential sources for fair market value, regardless if these sources would have revealed such information. Because the Commission en banc relies upon the testimony of witnesses for fair market value, it is important to reopen the cause and hear what the witness has to say relative to fair market value.

POSITIONS OF THE PARTIES CONCERNING NEWFIELD'S APPEAL OF MARCH 8, 2012 ALJ REPORT

NEWFIELD

1) **Gregory L. Mahaffey**, attorney, appeared on behalf of Newfield and stated the legal description of the land in question is SE/4 Section 7, T6N, R4W, McClain County, Oklahoma. Newfield states they own 40 acres within this particular 160 acre spacing unit.

2) Newfield argues they have acquired a substantial interest in this unit for the purpose of horizontal development of the Woodford formation. Newfield contends that while the Woodford is not part of this dispute, the Mississippi and Hunton formations are. Newfield argues that in drilling multi-unit lateral horizontal Woodford wells, the associated common source of supply is generally the Mississippi and Hunton formations.

3) Newfield states they have no interest in participating in Bays' vertical well, but would like to retain their interest in the right to participate in the Woodford as well as the Mississippi and Hunton in the event that Newfield's horizontal well were to get out of the Woodford zone.

4) Newfield argues the ALJ erred in finding that the pooling order should not distinguish between vertical and horizontal development. Newfield acknowledges that the *Amoco Production Co. v. Corp. Com'n of State of Okla.*, 751 P.2d 203 (Okl. 1986), is the seminal case regarding unit pooling. Newfield argues, however, that *Amoco* was decided prior to the rise in horizontal drilling and prior to the horizontal amendment to the spacing statute at 52 O.S. Section 87.1. Newfield contends these recent developments contemplate that horizontal spacing can coexist with vertical spacing.

5) Newfield asserts that unit pooling does not preclude the Commission from implementing a plan of development that will protect the owners desiring to drill a horizontal well as well as those desiring to drill a vertical well. Newfield claims the ALJ erred in finding that if Newfield elected to not participate in the Mississippi and Hunton formations in the Bays' vertical well, they would not retain the rights to horizontally develop these formations.

6) Newfield argues the ALJ erred in sustaining Bays' objection to a question asked of Mr. Joe Bays, owner of Bays. Newfield states the question presented asked if Bays would have endured any hardship or suffered a violation of correlative rights if Newfield chose not to participate in this vertical well but retained their rights in the Mississippi and Hunton for later horizontal development. Newfield states Bays objected and the ALJ sustained on the basis that Newfield was calling for a legal conclusion. Newfield argues the ALJ erred in sustaining this objection.

7) Newfield states that the Mississippi and Hunton formations were not the primary objective of the vertical well in question, but rather that Bays is drilling into a deeper formation. Newfield argues that such information went to the plan of development for this particular area, and as such, the ALJ erred in sustaining Bays objection to the question regarding the potential adverse impact future horizontal development would have on Bays vertical well. Newfield states testimony related to what adverse impact horizontal development will have on Bays vertical well is relevant and should be allowed to be placed into the record.

8) Newfield asserts the ALJ erred in its determination of fair market value.

9) Newfield states they are one of the most active operators in the state, claiming to have most likely drilled more Woodford wells than anyone in the state.

10) Newfield argues that Bays' contract landman, Mr. John Rice, "stuck his head in the sand" by failing to talk to Newfield about what they paid for their leases in the area. Newfield states, citing the Report of the ALJ on page 4, Mr. Rice admitted to not contacting anyone at Newfield regarding the leases in the area, despite acknowledging he had no reason to believe they would or would not provide him with information on the leases. Newfield adds that Mr. Rice never attempted to contact Hal Smith, Newfield's broker, to seek information on the amounts paid for leases in the area.

11) Newfield states Bays' contract landman agreed that Newfield had taken numerous leases in the area, including a number of leases in the offset quarter section. Newfield points to the Fleischaker lease, stating that Bays' landman did contact the lessee who refused to disclose the bonus paid on the lease. Newfield reasserts that Mr. Rice did not contact Newfield on that particular lease to ascertain the bonus received.

12) Newfield states they did not bring a landman to the initial hearing, because they believed Bays would have someone available to testify to the relevant leases in question. Newfield reasserts that even though they are one of the more active operators in the area, Bays did not investigate what Newfield was paying for these leases. Newfield claims many of their leases were taken after Bays' June 24, 2011 lease in the SE/4. Newfield contends that Bays failed to conduct their due diligence by failing to investigate the lease information in the nearby Newfield leases.

13) Newfield argues that had Bays acted with due diligence, they would have discovered that Newfield leased in the area at prices in the amount of $600 an acre with a 1/5th royalty interest as opposed to only $150 an acre with a 3/16th royalty interest. Newfield asserts their higher negotiated prices on their leases were single unit arm's length transactions.

14) Newfield reasserts that the ALJ erred in its determination of fair market value, and asks that additional evidence be taken including requiring Bays landman to conduct an investigation into the terms of the nearby Newfield leases. Newfield states they have filed a Motion to Reopen with the intent to introduce into evidence the Newfield leasing information in the surrounding area.

15) Newfield argues that the testimony Bays and their landman put forward with regards to fair market value was "not the way that this Commission generally works." Newfield contends the landman had a duty to try to determine all the recent transactions in the area. Newfield reasserts Bays failed to do so.

BAYS

1) **David E. Pepper**, attorney, appeared on behalf of Bays and stated that Newfield failed to bring their own witness. Bays argues because Newfield failed to bring a witness, the statements made by Newfield's counsel are not to be considered as factual evidence. Bays contends accordingly they, as well as the court, are unaware of Newfield's desire to use all of their acreage for horizontal development. Bays further contends this failure has left Bays and the court unaware of Newfield's desire to not participate.

2) Bays contends the ALJ who heard the case is one of the most experienced at the Commission. Bays contends this ALJ weighed the credibility of the two witnesses Bays presented.

3) Bays states they agree that Newfield is one of the biggest players in the Woodford formation. Bays contends the Woodford formation is not spaced in this unit.

4) Bays argues while their landman had not talked to Newfield, even if they had and hypothetically Newfield had testified to a fair market value of $600 an acre and a 1/5th royalty interest, Bays landman would not have considered this relevant evidence of fair market value. Bays states there had been a number of leases in the same range for $150 acre and a 3/16th royalty interest. Bays argues the analysis of fair market value was accurate and as such the ALJ accepted it. Bays contends that the ALJ did not feel the need to do any further investigating at the hearing; therefore the ALJ should be affirmed.

5) Bays cites *Amoco Production Co. v. Corp. Com'n of State of Okla.*, 751 P.2d 203 (Okl.Civ.App. 1986), and *SKZ, Inc. v. Petty*, 782 P.2d 939 (Okl. 1989) for the proposition that Oklahoma has unit pooling. Bays asserts that there is

currently no case law that states a party can opt out of one well in a unit and participate in another.

6) Bays argues Newfield is attempting to persuade the Commission to create new law by allowing a party to opt out of a vertical spacing order but retain the right in potential horizontal development or the future filing of a horizontal spacing. Bays contends this "fly(s) in the face of all current existing case law." Bays claims Newfield's position would allow Newfield to be a non-original risk taker in the first well with the right to come back for further horizontal development.

7) Bays contends their in-house landman has just recently been hired and has never testified in a protest. Bays asserts their contract landman is a qualified and capable expert.

8) Bays reasserts that the Woodford formation has not been spaced. Bays argues Newfield can file for a 640 acre spacing regarding the Woodford that is not affected by this case.

9) Bays reasserts the ALJ's report should be affirmed.

RESPONSE OF NEWFIELD

1) Newfield reasserts the issue they take with Bays' landman is not that he is a contract landman, but rather because he inadequately performed his job by failing to call Newfield and other mineral owners in the area for determining fair market value.

2) Newfield argues that Bays is essentially forcing them to participate in the vertical well or forfeit their rights in the Mississippi and Hunton formations. Newfield reasserts they believe the Commission does have the authority as part of the plan of development to make a declaration as to what the effect of not participating in the Bays' vertical well will have on their rights in horizontal spacing.

3) Newfield states *Amoco Production Co. v. Corp. Com'n of State of Okla.*, 751 P.2d 203 (Okl.Civ.App. 1986), *SKZ, Inc. v. Petty*, 782 P.2d 939 (Okl. 1989), *Inexco v. Corp. Com'n of State of Okla.*, 767 P.2d 404 (Okl. 1988), are all frequently cited cases regarding spacing, but distinguishes them because they were decided before horizontal spacing.

4) Newfield states Bays did not dispute that the leases that Continental took covered all formation rights including the Woodford. Newfield states all the leases they took themselves included all formation rights. Newfield argues

that while the Woodford is not spaced or pooled, there has been no discussion or attempt to say that there should be some allocation of either bonus or cost.

5) Newfield reasserts that Bays had the burden of proof to bring all the relevant transactions to the Commission. Newfield reasserts there were transactions after the date in which Bays took this lease in both the unit in question and contiguous units. Newfield states Bays' landman did not look at these leases. Newfield argues Bays' landman had a duty to bring forth the relevant lease information and evidence for the purpose of facilitating the ALJ's determination of fair market value.

POSITION OF THE PARTIES CONCERNING BAYS' ORAL APPEAL OF NEWFIELD'S MAY 11, 2012 MOTION TO REOPEN

BAYS

1) **David E. Pepper**, attorney, appeared on behalf of Bays and stated he agrees with the ALJ's recitation of the facts. Bays states the primary issue in this case was a pooling fight which dealt with "vertical versus horizontal type separation."

2) Bays argues Newfield, "as a sideline matter", was opposed to the due diligence that was done by the Bays' landman.

3) Bays argues Newfield did not bring a witness or any exhibits to discuss fair market value. Bays contends Newfield did not bring a witness or any exhibits because Newfield believed Bays' witness would discuss what Newfield wanted covered. Bays argues this is not a basis to reopen the record.

4) Bays contends "it is well settled law in our country that once an appeal is perfected...the trial court loses jurisdiction of those matters which are appealed." Bays argues the trial court retains jurisdiction over collateral issues. Bays cites *Herbert v. Wagg*, 117 P. 209 (Okl. 1910) for authority on this position. Bays contends the Commission has essentially adopted this position through their rules. Bays states a report has been issued although a final order has not. Bays states the appeal has been perfected.

5) Bays states Newfield cites OCC-OAC 165: 5-13-3(p) for authority on their motion. Bays argues this rule is clear and is to be used to reopen causes for the purpose of taking evidence which was not or could not have been available at the time of the hearing. Bays contends none of these requirements are

available for Newfield. Bays believes the evidence and witnesses were available and could have been introduced by Newfield at the time of the hearing. Bays contends Newfield has no standard to determine whether the due diligence efforts by Bays' landman were sufficient. Bays restates Newfield failed to introduce their own witness and as such Newfield relies only on their attorney's own argument that Bays' landman failed in his due diligence.

6) Bays argues if the Referee finds the due diligence efforts were not sufficient, Newfield has asked the Referee to remand it. Bays argues in the alternative, if the Referee finds the due diligence efforts were sufficient that the ALJ should be affirmed. Bays argues Newfield should not now be allowed to reopen the case to put on additional evidence.

7) Bays contends the ALJ stated she wants to hear from Bays' witness at hearing again, while Newfield has stated in their motion they seek to put on new evidence. Bays argues against both outcomes.

8) Bays argues the ALJ cannot open the case to hear more on the issue of due diligence because that issue is closed and is before the Referee on appeal.

9) Bays further argues the ALJ can likewise not reopen the case simply because Newfield wishes to submit new exhibits and testimony because that would violate OCC-OAC 165: 5-13-3(p). Bays contends once a case is closed, unless something new which was previously unavailable comes up, it moves to the appeal process. Bays contends the Commission has these rules to minimize cost, time, and the delay in furthering these things.

10) Bays reasserts Newfield failed to bring one witness to the hearing. Bays argues while Newfield did not like the ruling, their only remedy is the appeal before the Referee.

11) Bays reasserts the possible confusion with regards to the ALJ seeking to reopen the case and hear from Bays' landman who previously testified, compared to Newfield who seeks to reopen to put on additional evidence from their own witnesses or exhibits. Bays argues the Motion to Reopen should be reversed and that this case should proceed with the Referee ruling on what has already been argued.

NEWFIELD

1) **Gregory L. Mahaffey**, attorney, appeared on behalf of Newfield and stated the Commission has the discretion to accept or reject the Referee's recommendations and issue its own order. Newfield states that because there

has been no order in this case, new evidence can be introduced in a motion to reopen.

2) Newfield argues that the evidence for fair market value was not available because Bays' landman did not adequately perform his job. Newfield states if Bays' landman had performed his job adequately, the parties would not be at this hearing.

3) Newfield argues the standard of review for the Referee for this matter is whether there was an abuse of discretion by the ALJ in granting the motion. Newfield contends it is within the sound discretion whether the ALJ wishes to reopen a case or not. Newfield argues only in the event the ALJ is abusing that discretion should the Commission reverse the ALJ's decision.

4) Newfield contends the ALJ admits Newfield should have brought their own witness, but that she also acknowledges the process for calculating fair market value is more important than any one applicant. Newfield argues the ALJ correctly realized "if we bless what Bays did, we are inviting landmen to abuse the process and not follow the standard that they need to follow when you are taking somebody's interest." Newfield argues the Commission is charged with determining fair market value. Newfield states a pooling is quasi-condemnation. Newfield asserts the Commission should not be taking someone's interest under "our original Constitutional premise"' without providing just compensation.

5) Newfield states the ALJ did not put any limitation on reopening, whether it is additional cross-examination of Bays' landman or new witnesses or exhibits. Newfield argues the ALJ found that Bays had not complied with the process for determining fair market value. Newfield contends Bays' landman knew of relevant transactions within the relevant time period but did not investigate as to determine the bonus value of these transactions.

6) Newfield reasserts Bays' landman admitted even though he had no reason to believe Hal Smith at Energy Lease Brokerage or anyone at Newfield would not tell him about the relevant lease transaction terms, that he simply did not attempt to talk to them. Newfield argues they believe this is what caused the ALJ's decision, because Bays had the burden of proof to show, even in an uncontested case, fair market value.

7) Newfield contends the "ostrich theory" of ignoring transactions a party may not like, is not practiced before the Commission. Newfield asserts it is the duty of the landman to investigate the relevant leases and bring them before the Commission. Newfield argues they were "shocked" that Bays' landman did not call or attempt to discover the bonus values given for the relevant leases. Newfield reasserts the ALJ was correct in her position that the fair market

value determination at the Commission is bigger than any one party or one case.

8) Newfield contends to ensure the integrity of the fair market value process at the Commission, a message to the landmen must be sent that the "ostrich theory" of not contacting the relevant parties is unacceptable.

9) Newfield argues Bays should not be afraid to reopen the case, because if the newly introduced evidence is not relevant to fair market value, the ALJ will make the same ruling as she did in her first report.

10) Newfield reasserts the ALJ's granting of the Motion to Reopen should be affirmed.

RESPONSE OF BAYS

1) Bays reasserts the evidence for fair market value was available. Bays contends Newfield could have brought their own witnesses to testify that they were never contacted and offer evidence to as what they paid for their leases. Bays asserts for Newfield to state the evidence was not available is a "clear misstatement of facts."

2) Bays notes the ALJ acknowledges the evidence for fair market value could have been available at the hearing. Bays argues the ALJ has stated Newfield should have brought their own witness as well as put the issue of fair market value in the PCA.

3) Bays reasserts they read nothing in the ALJ's ruling that Newfield can now bring in their own witness or exhibit. Bays states the ALJ stated, "I want to hear from that witness," referring to Bays' landman.

4) Bays argues there is no "ominous provision" which provides that certain cases are bigger than others and as such exceptions to the Commission Rules are made. Bays contends they are entitled to rely on the Commission Rules.

5) Bays request the Referee overturn the ALJ's decision to reopen the case.

CONCLUSIONS

I.

THE REFEREE FINDS THE REPORT OF THE ADMINISTRATIVE LAW JUDGE FILED ON MARCH 8, 2012, SHOULD BE AFFIRMED BUT MODIFIED AS TO THE ISSUE OF FAIR MARKET VALUE.

1) The issues concerning operator, time frames, deeming, and well costs were undisputed and therefore the order to issue in this matter should include the terms as recommended by Bays.

2) As to the disputed issue regarding fair market value, the Referee affirms the recommendation of the ALJ to grant the Motion to Reopen this cause to take additional evidence in order to determine fair market value. The Referee will subsequently discuss her basis for affirming the ALJ's recommendation to grant the Motion to Reopen to take further evidence concerning fair market value.

3) With regard to the issue of whether nonparticipation under a pooling order for vertical development would deprive a party of future participation in horizontal development, the Referee would affirm the recommendation of the ALJ that the order to issue in this case would be a unit pooling for all named formations without any distinction of vertical versus horizontal development.

4) Newfield is arguing that Bays is essentially forcing them to participate in Bays' vertical well or forfeit their rights in the Mississippi and Hunton formations Newfield wants to horizontally develop the Woodford which could affect the Mississippi and Hunton formations. Newfield wants the Commission to make the declaration that Newfield would not have to participate in Bays' vertical well in order to retain a right in potential horizontal development or the future filing of horizontal spacing. Newfield's position would allow Newfield to be a non-original risk taker in the first well with the right to come back for further horizontal development. Currently the case law provides for unit pooling for all named formations without any distinction of vertical versus horizontal development. See *Amoco Production Company v. Corporation Commission of State of Oklahoma*, 751 P.2d 203 (Ok.Civ.App. 1986), *SKZ, Inc. v. Petty*, 782 P.2d 939 (Okl. 1989), *Inexco Oil Co. v. Oklahoma Corp. Com'n*, 767 P.2d 404 (Okl. 1988). *Amoco Production Company v. Corporation Commission of State of Oklahoma*, 751 P.2d at 203 provides:

First, the statute mandates developing the spacing unit as a unit. Operator Amoco is developing the spacing unit as a unit. A 640 acre drilling and spacing order was issued on all 13 common sources of supply. After the spacing order was entered, the unit could be force pooled. *Gulfstream Petroleum Corporation v. Layden*, 632 P.2d 376 (Okl. 1981). *Helmerich v. Corporation Commission*, 532 P.2d 419 (Okl. 1975). This pooling was for unit development. A force pooling order unitizes the working interest in the entire unit as to the named formations.

* * *

Second, the statute authorizes pooling when the terms and conditions are just and reasonable. An election not to participate transfers by operation of law the right to drill the spacing unit. The measure of compensation for forcibly pooled minerals is there "fair market value." *Miller v. Corporation Commission*, 635 P.2d 1006 (Okl. 1981). ...Our Supreme Court has said, once the spacing unit is pooled and the time for elections has passed, the interest becomes vested and beyond the Corporation Commission's reach to modify. The rights are no longer vulnerable to extinguishment. *Crest Resources v. Corporation Commission*, 617 P.2d 215 (Okl. 1980).

Third, the statute requires that owners will receive a just and fair share of the oil and gas. The original election is based upon certain information, or lack of information. Good faith elections were made prior to the first well. It is not fair or just to alter the positions of the interest owners after the initial well is drilled. Once an operator relies on the unit that the Corporation Commission creates, new elections deprive the original risk capital investors of rights earned by taking the risk of the initial well. The order of the Commission granting a second election is a deprivation of a property right of the initial risk capital investors. They do not recover their just and fair share of production.

5) The Supreme Court in the *Inexco Oil Company v. Oklahoma Corporation Commission* case, 767 P.2d at 405 states:

> Order No. 260474 required Ward and Vierson, Nova's predecessor in interest, to participate in the costs of drilling and completing Wolfe #1-23 or accept a bonus in lieu of participation. Ward and Vierson elected to accept a bonus. Once the election period passed, the property interests of the affected parties vested. *Ranola Oil Company v. Corporation Commission*, 752 P.2d 1116, 1119 (Okl. 1988). Once vested, the property rights of the parties were beyond the reach of the Commission's power to modify. Id.; *Crest Resources v. Corporation Commission*, 617 P.2d 215, 218 (Okl. 1980). By accepting the bonus, Ward assigned its exploratory rights to Inexco, the operator, and can assert no right to participate in the subsequent increased density wells. Similarly, Nova, as Vierson's successor in interest, can assert no right to participate in the subsequent increased density wells. *Ranola*, 752 P.2d at 1119. Once the bonus was paid, Inexco's property rights vested. Id.

See also *SKZ, Inc. v. Petty*, supra, 782 P.2d at 941.

6) Thus, the Referee agrees with Bays' position that there is currently no case law that allows a party to opt out of one well in a unit and participate in another. For the Commission to create new law by allowing a party to opt out of a vertical spacing order but retain the right in potential horizontal development or the future filing of a horizontal spacing "fly(s) in the face of all current existing case law." Newfield's position would allow Newfield to be a non-original risk taker in the first well with the right to come back for further horizontal development. Thus, the ALJ in the Referee's opinion was correct when she stated "that this order would be a unit pooling for all named formations without any distinction of vertical versus horizontal development."

II.

THE REFEREE FINDS THE ORAL REPORT OF THE ALJ's GRANTING OF NEWFIELD'S MAY 11, 2012 MOTION TO REOPEN SHOULD BE AFFIRMED.

1) Bays argues there is no valid reason to reopen because Newfield had the opportunity and should have had their own witness at the hearing to discuss fair market value. Newfield argues that the Commission relies specifically on these witnesses in uncontested hearings and contested pooling hearings for the ascertainment of fair market value and when such witnesses fail to adequately do their job, the Commission is relying on unreliable information which affects correlative rights.

2) The Referee notes that OCC-OAC 165:5-13-3(p) allows the Commission *discretion* to reopen a cause for the taking of additional evidence. The Referee sees no abuse of discretion on the part of the ALJ in allowing additional evidence to be presented concerning fair market value. The ALJ heard the hearing on the merits and was the best one to determine if the record was in need of supplementation.

3) OCC-OAC Rule 165:5-13-3(p) states in relevant part:

> (p) **Reopening the Record**. Any person may file and serve, by regular mail, on all parties of record a motion to reopen the record for further hearing or to offer additional evidence. The Commission, at any time prior to final order in the cause, **may**, upon such motion or upon the motion of the Commission, order the record to be reopened for the purpose of taking testimony and receiving evidence which was not or could not have been available at the time of the hearing on the merits or for the purpose of examining its jurisdiction. (emphasis added)

One can see by the use of the word "may" that a motion to reopen is "permissive" only and not "mandatory". It does not require the Commission to reopen the hearing but it allows the Commission discretion to allow the presentation of additional fair market value evidence.

4) The Referee agrees with the ALJ's contention that she did not feel either side was in the correct position. Newfield should have brought a witness as well as made the issue of fair market value part of their Prehearing Conference Agreement. Bays' landman witness should have checked all

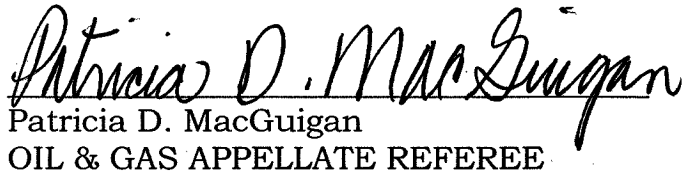
potential sources for fair market value which it clearly did not do. The ALJ contended that the Commission en banc relies upon the testimony of witnesses for fair market value and therefore it was important to reopen the cause and hear what the witnesses had to say relative to fair market value. The Commission is charged with determining fair market value because a pooling is a quasi condemnation, as it takes someone's interest, and therefore just compensation should be given for said interest. See A Premier on Forced Pooling of Oil and Gas Interests in Oklahoma, by Charles Nesbitt, 50 Okl.B.J. 648 (1979).

5) The Referee finds that the Commission's mandate is to prevent waste and protect correlative rights under the Conservation laws. 52 O.S. Section 87.1. As stated in *Winter v. Corporation Commission of Oklahoma,* 660 P.2d 145 (Okl. 1983):

> ...Having been given a choice of remedies, it is incumbent upon the Commission to use the remedy which will best prevent waste and protect correlative rights...

Allowing the record to be reopened for additional testimony concerning fair market value will allow the Commission to protect correlative rights and will follow and adhere to the above stated mandate.

RESPECTFULLY SUBMITTED THIS 25th day of July, 2012.



Patricia D. MacGuigan
OIL & GAS APPELLATE REFEREE

PM:ac

xc: Commissioner Murphy
Commissioner Anthony
Commissioner Douglas
Jim Hamilton
ALJ Susan R. Osburn
David E. Pepper
Gregory L. Mahaffey
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