

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

APPLICANT: SILVER CREEK OIL & GAS, LLC)
)
RELIEF SOUGHT: POOLING)
)
LEGAL DESCRIPTION: ALL OF SECTION 21,)
TOWNSHIP 8 NORTH, RANGE 5)
EAST, POTTAWATOMIE AND)
SEMINOLE COUNTIES,)
OKLAHOMA)

) CAUSE CD NO.
) 201308764
)

FILED
DEC 08 2014

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CORPORATION COMMISSION
OF OKLAHOMA

APPLICANT: LANDMARK ENERGY, LLC)
)
RELIEF SOUGHT: POOLING)
)
LEGAL DESCRIPTION: SECTION 21, TOWNSHIP 8)
NORTH, RANGE 5 EAST,)
POTTAWATOMIE AND)
SEMINOLE COUNTIES,)
OKLAHOMA)

) CAUSE CD NO.
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)

REPORT OF THE OIL AND GAS APPELLATE REFEREE

These Causes came on for hearing before **Michael Norris**, Administrative Law Judge for the Corporation Commission of the State of Oklahoma, on the 7th and 21st days of May, 2014, at 8:30 a.m. 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: **Richard J. Gore**, attorney, appeared on behalf of applicant, Landmark Energy, LLC ("Landmark"); **John C. Moricoli, Jr.**, attorney, appeared on behalf of applicant, Silver Creek Oil and Gas, LLC

("Silver Creek"); **James L. Myles**, Deputy General Counsel for Deliberations, filed notice of appearance.

The Administrative Law Judge ("ALJ") filed his Report of the Administrative Law Judge on the 19th day of August, 2014, to which Exceptions were timely filed and proper notice given of the setting of the Exceptions.

The Appellate argument concerning the Oral Exceptions was referred to **Patricia D. MacGuigan**, Oil and Gas Appellate Referee ("Referee"), on the 31st day of October, 2014. After considering the arguments of counsel and the record contained within these Causes, the Referee finds as follows:

STATEMENT OF THE CASE

LANDMARK APPEALS the ALJ's recommendation that the application of Silver Creek in CD 201308764 be approved and that Silver Creek should be designated as the unit operator.

This is a case of competing interests for designation of an operator in the captioned pooling applications of Silver Creek and Landmark. Silver Creek and Landmark request that the Commission pool the interests and adjudicate the rights and equities of oil and gas owners in the Mississippian, Woodford, Hunton and Sylvan common sources of supply underlying the 640-acre horizontal drilling and spacing unit comprised of Section 21, T8N, R5E, Pottawatomie County and Seminole County, Oklahoma. Evidence was submitted indicating similar activities, percentage of ownership, drilling and completion methods and competent operators for both Silver Creek and Landmark.

Silver Creek demonstrated their activity in the area, ownership in this unit and the surrounding sections and the completion methods utilized as the factors that establish their selection as operator.

Landmark argued their years of experience, lower costs and completion methods as the factors that establish their selection as operator.

Both applicants provided extensive testimony concerning the factors normally considered by the Commission in operator contests. These factors and their consideration are documented in "A Primer on Forced Pooling of Oil and Gas Interests in Oklahoma," 50 Okl. B. J. 648 (1979) by Charles Nesbitt. The qualifications and factors presented by the parties were considered by the ALJ.

LANDMARK TAKES THE POSITION:

- 1) The Report of the ALJ is contrary to the law and to the evidence, is arbitrary, unreasonable and discriminatory, and fails to effect the ends of the prevention of waste and the protection of correlative rights as is required by applicable laws of the State of Oklahoma.
- 2) The ALJ failed to take into consideration that: (a) Landmark will drill a vertically deeper well in the Hunton and will frac into the Woodford; (b) Landmark is a local company headquartered in Seminole County where the well is to be drilled, while Silver Creek is located totally in Texas; (c) Silver Creek's proposed well is on the western edge of Silver Creek's "main core area," whereas the Landmark proposed well is in the heart of Landmark's core area; (d) Based on Silver Creek's title opinion, current ownership is Landmark with 252.65 acres, while Silver Creek has 203.03 acres; (e) Landmark's engineer has drilled ten horizontal wells in Payne County, using a rotary table rig for approximately \$1,000,000 less per well than Devon has drilled the same wells in the same area, thus providing a valid basis for the difference in the AFEs in this case; and (f) Silver Creek has no disposal well or plans for one in this area, whereas Landmark has already permitted one.
- 3) Wherefore, Landmark requests that the Report of the ALJ should be reversed and the pooling application of Landmark should be granted, designating Landmark as operator.

THE ALJ FOUND:

- 1) After taking into consideration all the facts, circumstances, testimony and evidence presented in this cause, it is the ALJ's recommendation that the application of Silver Creek filed in cause CD 201308764 be approved with Silver Creek as the designated unit operator. Further, the application of Landmark filed in cause CD 201402826 should be denied. The evidence presented was persuasive that Silver Creek has more activity in this area and has acquired a vast amount of acreage in the surrounding area. Silver Creek has drilled more wells, operates more wells and has experience in drilling horizontal wells.
- 2) Silver Creek proposed their application in this section prior to Landmark. Silver Creek justified their AFE costs as being necessary, better suited for the formation, increases long-term producibility and lowers risk. They substantiated that they are experienced and competent in planning, drilling and completing wells. They have experienced personnel, seismic data, ample facilities and documented exploration activity. Silver Creek had the majority of the factors in their favor.

POSITIONS OF THE PARTIES

LANDMARK

- 1) **Richard J. Gore**, attorney, appearing on behalf of Landmark, argues that Landmark should be the operator in Section 21, T8N, R5W, Pottawatomie and Seminole Counties, Oklahoma.
- 2) Landmark intends to drill a different well than Silver Creek; the difference being that Landmark wants to drill a Hunton well and perforate and frack into the Woodford. Silver Creek is proposing to drill a Woodford well and perforate and frack into the Hunton. Drilling into the Hunton will be more cost effective and economical. The Hunton is easier to drill as it is not a shale. It is a limestone.
- 3) Based in Seminole, Oklahoma, Landmark is a local company. It is only a few minutes drive from the subject lands to Landmark's location. Being close to the subject lands will also reduce costs having to drive back and forth. Silver Creek is located in Gainesville, Texas.
- 4) The Silver Creek well is on the edge of their core area and they only plan to drill a single well at the moment. If they are satisfied with the wells "producibility", they will consider additional wells if it fits "into their development profile." While the subject lands are in the middle of Landmark's core area and they plan to drill multiple wells.
- 5) Landmark is planning on drilling a saltwater disposal ("SWD") well for the first well and all other wells. They plan to charge only the actual operating expenses of the SWD well to the producing well, making it more economic.
- 6) Landmark is the majority interest holder when you consider the 62 top lease acres of Silver Creek that are vested in Landmark, and which Landmark owns title to, which gives Landmark over 250 acres and Silver Creek just over 200 acres.
- 7) Landmark's engineer has drilled over 200 horizontal wells and has recently drilled ten horizontal Woodford and Mississippian wells in Payne County in Oklahoma competing against Devon. Landmark drilled these ten wells with a rotary rig for \$1 million less each than Devon was drilling them for. Thus, Landmark's lower AFE is factually based.

8) The ALJ was mistaken when he stated that Silver Creek has more activity in the area. Silver Creek is active on lands over 12 miles away from the subject lands where Landmark already has operations. Silver Creek has drilled 23 wells since 2012 and they operate 45 wells while Landmark operates 37 wells in the Seminole/Pottawatomie County area. The ALJ also stated that Silver Creek has more wells but their testimony was they had not completed some of these wells

9) The AFE submitted by Landmark was much less than Silver Creek's, and therefore interest holders would more realistically consider participating. Although Silver Creek stated they were over estimating in the AFE, it still presents a higher barrier for interest holders considering participation.

10) The ALJ stated he considered experience of personnel, seismic data, facilities and documented exploration activity in naming Silver Creek operator. However, Landmark has equivalent personnel, ample facilities that are more closely located. In this formation seismic data is irrelevant and Landmark has plenty of documented exploration activity.

SILVER CREEK

1) **John C. Moricoli, Jr.**, attorney, appearing for Silver Creek, contends that the ALJ properly considered and weighed all evidence and witness testimony and credibility when reaching his decision to name Silver Creek the operator.

2) Landmark incorrectly stated that seismic data was not needed while drilling the proposed wells. According to Clayton Snyder, Silver Creek's testifying geologist, seismic data must be collected so that all faults, especially smaller faults can be identified. If the well bore were to hit an unaccounted for fault, it could cause the drill to get out of zone which would take a good deal of time and effort to get back into the zone, or the worst-case scenario is you simply cannot drill any further, ending up shortening the horizontal component. This would restrict the production of the well causing it to become potentially uneconomic. Silver Creek has collected 3-D data for the targeted well formation.

3) As a company, Silver Creek has drilled and completed 250-300 wells, approximately 100 in Oklahoma, including 46 horizontal wells in Hughes and Seminole Counties. Silver Creek also has a full host of experienced employees to handle all aspects of the drilling process showing they are more capable of being the operator in the subject lands.

4) There is a discrepancy in the acreage Landmark claims to own. Landmark says 62 acres in the N/2 SW/4 are held by production. However, the Catherine #38 well holding production consists of a single pipe sticking out of the ground and is not currently producing. There is no equipment around it and the grass surrounding the well is overgrown, indicating the well hasn't commercially produced for sometime. That being the case, the leases in Silver Creek's view, have terminated. Silver Creek has since acquired these leases giving Silver Creek majority ownership with 58% and Landmark with 42% ownership.

5) Landmark stated it was planning to drill a SWD well and that Silver Creek was not. This was a misstatement of the facts. Silver Creek will drill a SWD well once the proposed well is completed and determined to produce economically. It is illogical to drill a disposal well before determining whether the subject well produces economically and an unnecessary cost to those participating in the well.

6) Silver Creek is active in Hughes and Seminole Counties some 12 miles away as stated by Landmark. But what Landmark failed to state is that Landmark is not active in this area either. Silver Creek is actively operating horizontal wells, which is evidence that they can properly operate wells on the subject lands.

RESPONSE OF LANDMARK

1) Due to drilling activity in Seminole County there is no need for seismic data. The area has been drilled extensively and an operator can get the data from existing well logs and faults can be identified from existing well logs as well.

2) Landmark has shown they can drill this well for less money and operate it for a lot less money, and therefore, the well will last a lot longer. Silver Creek has much higher overhead costs compared to Landmark, allowing the state and interest holders to make more money because the well will be able to operate longer.

3) The disagreement regarding ownership of the 62 acres is not something that the Commission can decide. Plus, there is an extenuating circumstance as to why the well intended to hold production is not producing. The SWD well that the Catherine #38 well was using shut down and Landmark didn't have any place to put the salt water, and hauling saltwater would make the well uneconomic, so they shut the Catherine #38 well in. Landmark is trying to fix the SWD well, but the company's head has liver cancer and has not been able

to get out and get the SWD well fixed. This is a circumstance the Commission can look into and decide whether the situation allows for an extension to hold the Landmark leases.

- 4) It is not an uncommon practice to drill a SWD well before nearby wells start producing. Given the cost of hauling saltwater many operators drill a disposal well that will service three or four producing wells.
- 5) Landmark does operate 37 wells and 3 of those wells are horizontal wells.

CONCLUSIONS

The Referee finds the Report of the Administrative Law Judge should be affirmed.

- 1) The Referee finds the ALJ's recommendation that the application of Silver Creek in CD 201308764 be approved with the designation of Silver Creek as the unit operator should be affirmed. Also, the recommendation of the ALJ to deny the application of Landmark in CD 201402826 based upon the recommendation of Silver Creek as operator should be affirmed. The ALJ's recommendation is supported by the weight of the evidence and free of reversible error. The ALJ wrote a well-reasoned report setting forth an extensive summary of the evidence and balanced the normal factors considered by the Commission in the award of operations under a pooling application.
- 2) As the initial finder of fact, it is the ALJ's duty 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 (Okl. 1940); *Application of Choctaw Express Company*, 253 P.2d 822 (Okl. 1953).
- 3) In regard to the weight to be given opinion evidence, the Supreme Court stated in *Palmer Oil Corporation v. Phillips Petroleum Company*, 231 P.2d 997 (Okl. 1951):

...At the hearing herein the testimony adduced was chiefly that of petroleum engineers and geologists who testified on the basis of both personal surveys made and of an interpretation of the accumulated data in the hands of the Commission. The testimony of these experts was in direct conflict but that of each was positive upon the issue. Under the circumstances the objection is necessarily addressed to only the weight of

the evidence. Under the holding of this court and that of courts generally, *Chicago, R. I. & P. Ry. Co. v. Pruitt*, 67 Okl. 219, 170 P. 1143; 22 C.J. 728, sec. 823, 32 C.J.S., Evidence, § 567, p. 378, the weight to be given opinion evidence is, within the bounds of reason, entirely for the determination of the jury or of the court, when trying an issue of fact, it taking into consideration the intelligence and experience of the witness and the degree of attention he gave to the matter. The rule should have peculiar force herein where by the terms of the Act the Commission is recognized as having peculiar power in weighing the evidence. Since the evidence before the Commission was competent and sufficient if believed, to sustain the order we must, and do, hold that the order is sustained by the evidence and that the contention is without merit. *Ft. Smith & W. Ry. Co. v. State*, 25 Okl. 866, 108 P. 407; *Bromide Crushed Rock Co. v. Dolese Bros. Co.*, 121 Okl. 40, 247 P. 74.

4) The Commission has always focused on a number of different factors in the award of operations. Charles Nesbitt in his article Nesbitt, *A Primer On Forced Pooling of Oil and Gas Interests in Oklahoma*, 50 Okl.B.J. 648 (1979) set forth a good review of the factors considered and the importance that the Commission attaches to those factors.

5) Mr. Nesbitt states:

DESIGNATION OF OPERATOR

A deceptively important provision of the pooling order is the designation of the operator of the proposed well. In most cases the applicant already owns the majority interest in the spacing unit, and is routinely named operator. However, there are notable exceptions where a spirited battle occurs between lessees over operations. The working interest ownership of non-participating pooled owners inures to the operator, at least in absence of a claim by other participants to share therein. A lessee who is promoting the proposed well for a carried interest, or similar remuneration, has a significant financial stake in being designated operator.

Several factors are considered in the selection of the operator, the most important being working

interest ownership. All other things being equal, the owner of the largest share of the working interest has the best claim to operations. However, this is not always true, and other factors can outweigh majority ownership.

Second in importance is actual bona fide exploration activity. This is not a simple race to the courthouse, with the earliest applicant getting the nod, but involves such matters as when a well was first proposed and by whom, whether the proposed well is part of a multi-well exploration program, whether a rig has been contracted for, and so on.

Other factors having a bearing on the final selection include the number of wells operated in the vicinity, the extent of developed and undeveloped lease ownership, the availability of operating personnel and facilities, a comparison of proposed costs of drilling and operating the well, and, rarely, the relative experience and competence of the contenders for operating rights.

6) As noted in said article, the ownership position of the parties and the actual bona fide exploration activity were factors that were given important consideration by the ALJ. In the present case there are a number of factors presented for consideration. The ALJ acknowledged those considerations.

7) With regard to the ownership consideration, there is an ownership disagreement concerning 62 acres of held by production acreage in the N/2 SW/4 of Section 21. Silver Creek is claiming the 62 acres and Landmark is claiming them also. The testimony was that the Catherine #38 well claimed to be held by production by Landmark consists of a single pipe sticking out of the ground and is not currently producing. There is no equipment around the area and the grass surrounding the well is overgrown indicating the well hasn't commercially produced for some time. Silver Creek therefore claims that Landmark's leases have therefore terminated. This well has not sold any production since 2011. Silver Creek has therefore taken new leases covering all or a portion of that tract. They have taken by lease 62 of the 80 acres. With the disputed 62 acres, that would give Silver Creek 265 acres and Landmark would have 205 acres.

8) In the lands offsetting Section 21 Silver Creek owns interest in Sections 15, 22, 27 and 29. Silver Creek does not own any interest in four sections offsetting Section 21, Sections 16, 17, 20 and 28. Silver Creek owns 204 acres in Section 15, 302 acres in Section 22, 80 acres in Section 27 and 4 acres in

Section 29. The Woodford prospect runs from eastern Hughes County in T6N, R11E to Cleveland County in T7N, R1W. This is a total of 125,000 net acres in this area. The Silver Creek holdings are in Cleveland County, a part of McClain County, the majority of Pottawatomie County, Seminole County and Hughes County. Section 21 falls right in the middle of this total area. The evidence reflected there are 23 wells since December 2012 that have been permitted and drilled by Silver Creek but are not completed and producing at this time. There are also currently 22 producing wells. With a total of 45 operated Woodford wells in the area. Silver Creek has drilled and completed 250 to 300 wells, approximately 100 wells in Oklahoma, including 46 horizontal wells in and around Hughes and Seminole Counties.

9) The AFE of Landmark had a total well cost of \$2,553,350 while Silver Creek's AFE has a total well cost of \$3,809,900. Silver Creek uses a rig with a top drive capability which gives the functionality they need to minimize the risk associated with the drilling operation. Landmarks' AFE is for rotary table rig. The testimony was that the Silver Creek current AFE is conservative because Silver Creeks wants to prepare their partners for unforeseen scenarios based upon the risks associated with the operation. This gives the participants the best estimate of cost and Silver Creek would rather do this than give an AFE with the cheapest cost that they think they can possibly drill the well and then have to make a cash call. Silver Creek however believes they can drill and complete this well for less than the AFE cost depicted.

10) Landmark asserts that seismic data is not necessary to drill the proposed wells. Silver Creek asserts seismic data must be collected so that all smaller faults can be identified. If the wellbore were to hit an unaccounted for fault, it could cause the drill bit to get out of zone and require time and money to get back into the zone, with a possibility of shortening the horizontal component.

11) The ALJ's Report in his Recommendations and Conclusions, page 19, states:

...The evidence presented was persuasive that Silver Creek has more activity in this area and has acquired a vast amount of acreage in the surrounding area. Silver Creek has drilled more wells, operates more wells and has experience in drilling horizontal wells.

* * *

Silver Creek proposed their application in this section prior to Landmark. Silver Creek justified their AFE costs as being necessary, better suited for the formation, increases long-term producibility and

lowers risk. They substantiated that they are experienced and competent in planning, drilling and completing wells. They have experienced personnel, seismic data, ample facilities and documented exploration activity. Silver Creek had the majority of the factors in their favor.

12) The ALJ determined that the balance of the factors support Silver Creek as operator. After reviewing the transcript and considering these factors to determine a proper operator of a well within a drilling and spacing unit, the Referee believes that the ALJ has made a determination that should be affirmed.

RESPECTFULLY SUBMITTED THIS 8th day of December, 2014.


Patricia D. MacGuigan
OIL & GAS APPELLATE REFEREE

PM:ac

xc: Commissioner Anthony
Commissioner Douglas
Commissioner Murphy
James L. Myles
ALJ Michael Norris
Richard J. Gore
John C. Moricoli, Jr.
Michael L. Decker, OAP Director
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