

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

FILED
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CORPORATION COMMISSION
OF OKLAHOMA

APPLICANT:	FAIRWAY ENERGY, LLC)	
)	
RELIEF SOUGHT:	POOLING)	CAUSE CD NO.
)	201408884
)	
LEGAL DESCRIPTION:	SECTION 22, TOWNSHIP 17)	
	NORTH, RANGE 7 WEST,)	
	KINGFISHER COUNTY,)	
	OKLAHOMA)	
)	
APPLICANT:	CHAPARRAL ENERGY, LLC)	
)	
RELIEF SOUGHT:	POOLING)	CAUSE CD NO.
)	201409259
)	
LEGAL DESCRIPTION:	SECTION 22, TOWNSHIP 17)	
	NORTH, RANGE 7 WEST OF)	
	THE IM, KINGFISHER COUNTY,)	
	OKLAHOMA)	

REPORT OF THE OIL AND GAS APPELLATE REFEREE

These Causes came on for hearing before **Keith T. Thomas**, Administrative Law Judge for the Corporation Commission of the State of Oklahoma, on the 6th day of May, 2015, 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: **Russell J. Walker**, attorney, appeared on behalf of applicant, Fairway Energy, LLC ("Fairway"); **John R. Reeves**, attorney, appeared on behalf of applicant, Chaparral Energy, LLC ("Chaparral"); and

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 23rd day of July, 2015, 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 4th day of September, 2015. After considering the arguments of counsel and the record contained within these Causes, the Referee finds as follows:

STATEMENT OF THE CASE

CHAPARRAL TAKES EXCEPTION to the recommendation of the ALJ that the pooling application of Fairway in Cause CD 201408884 be granted, while the pooling application of Chaparral in CD 201409259 be denied.

In these two causes Fairway and Chaparral seek an order pooling interests and adjudicating the rights and equities of oil and gas owners in Section 22, T17N, R7W, Kingfisher County, Oklahoma. Both Applicants are seeking the pooling of said oil and gas interests for a 640-acre drilling and spacing unit. Fairway intends to develop the Oswego common source of supply, while Chaparral intends to develop the Big Lime and the Oswego common sources of supply. Fairway is requesting that the pooling order name Blake Production Company, Inc. ("Blake") as the operator of the unit well. Chaparral is asking that the Commission issue a pooling order naming Chaparral as the operator of the drilling and spacing unit. Order No. 641398 issued in Cause CD 201409098 created a 640-acre horizontal drilling and spacing unit in Section 22, T17N, R7W, Kingfisher County, Oklahoma for the Big Lime and Oswego common sources of supply. These two causes were heard together. Each of the Applicants is seeking to have their application for a pooling order approved, while asking that the Commission deny the other Applicant's application.

CHAPARRAL TAKES THE POSITION:

1) The ALJ erred in recommending that the "Pooling Application of Fairway Energy, LLC in Cause CD 201408884 be granted, while the Pooling Application of Chaparral Energy, L.L.C. in CD 201409259 be denied." Furthermore, the ALJ erred in designating Fairway as the operator under the pooling order to be entered in Cause CD No. 201408884. The ALJ initially states that Fairway is requesting that Blake be the designated operator under the pooling order; however, throughout the analysis of the ALJ Report, the ALJ references

"Fairway" as the party to be designated as operator. The recommendations of the ALJ are contrary to law and to the evidence presented. Such recommendations are arbitrary, unreasonable and discriminatory, and if adopted, would not prevent or assist in preventing the various types of waste and would not protect or assist in protecting correlative rights.

2) The ALJ states that "it is worth noting that Fairway was the first to file its application," but that "it was not by a significant amount of time." The ALJ failed to point out that the only application filed by Fairway covering the section involved herein is its pooling application. The ALJ failed to consider that in its efforts to develop the section involved herein, Chaparral has filed proceedings to space the Big Lime and Oswego separate common sources of supply in such section, for a waiver of the consent requirement for such spacing, for location exceptions for the Big Lime and Oswego separate common sources of supply in such section and for pooling rights in the Big Lime and Oswego separate common sources of supply in such section. In addition, Chaparral has filed a similar set of proceedings covering the Mississippian common source of supply in the section covered hereby. Chaparral has been very active in attempting to obtain necessary orders from the Commission to develop the section involved herein, while Fairway has not.

3) The ALJ properly determined that the major issue in controversy in these matters is which company should be designated as operator under the order to be entered in these causes. Chaparral requested and asserted that it should be designated as operator. In reaching his recommendation that "Fairway" should be designated as operator, the ALJ states that he "had to consider the cohesive nature of each team" and that it is an important factor that "the staff at Fairway has changed only slightly during the drilling of the last twelve wells in the area." The ALJ goes on to state that the "Chaparral personnel have not been the same team throughout the drilling of its wells in the immediate area." These findings are contrary to the evidence presented, in that the team at Chaparral which has been involved with the fourteen horizontal wells in the Oswego common source of supply that have been drilled by Chaparral has remained substantially the same. The team at Chaparral that was involved with drilling the last nine horizontal wells in the Oswego common source of supply has remained exactly the same.

(4) The ALJ states that "the Fairway team collectively possesses superior expertise." The ALJ erred in making such a conclusion in that there is no evidence presented concerning the parties who are on the "Fairway team" or their level of expertise, except that Fairway has had the same technical team in place for last ten wells drilled by Fairway. Such a determination that the "Fairway team" is collectively superior to Chaparral's team is not supported by the evidence. The ALJ failed to point out that Chaparral has drilled the Ooid well in the Oswego common source of supply which is the best Oswego well in Kingfisher County and shows the expertise of the team at Chaparral in drilling,

completing and operating horizontal wells in such common source of supply. Furthermore, Chaparral has drilled, completed and produced over 250 horizontal wells in the Bakken, the Cleveland Granite Wash, the Mississippian, the Marmaton, the Woodford and the Oswego which has provided a substantial amount of experience and expertise that is applicable to drilling a horizontal well in the Oswego common source of supply in the section involved herein. Furthermore, Chaparral has conducted a special micro seismic project in regard to the Oswego common source of supply to analyze the effects of fracture stimulation in such common source of supply, including fracture lengths, so as to be able to design fracture stimulations jobs to be more effective and economic. The ALJ failed to mention that Chaparral has run radioactive tracers in wells to determine the effectiveness of using a Packers Plus system as opposed to a "plug and perf" system and that the results of such tracers has shown that the Packers Plus system is more effective and economic. Fairway uses the "plug and perf" system and not the more effective and economic Packers Plus system.

5) The ALJ determined that there "appears to be slightly less than a 6.5% difference between the two cost estimates presented to the Court" in the AFEs presented by the parties. The ALJ found that "the difference between the cost estimates of the parties is seen as being negligible". The ALJ erred in failing to recognize or even point out that the cost estimate presented on behalf of Fairway did not include significant and important items such as plugs for its "plug and perf" system, pipelines for disposal of produced water, salt water transfer pump, sufficient cement for the three strings of pipe in Fairway's proposed well and a vapor recovery unit.

6) The ALJ found that "Fairway has a slightly larger acreage position in the drilling and spacing unit than does Chaparral." The ALJ goes on to find that the difference in the acreage position "may be small; however the fact that Fairway has the majority is not insignificant." The difference in ownership between Fairway and Chaparral is approximately nine acres in a unit comprised of 640 acres (or 1.41% of the unit). The ALJ erroneously treats nine acres as "not insignificant" or as being significant, but fails to state why it is significant. There was no evidence presented that the fact Chaparral has nine acres less than Fairway would in anyway impact the manner in which Chaparral would develop the lands involved herein. In this regard the ALJ failed to point out that in addition to the significant interest of Chaparral in Section 22, T17N, R7W of the IM, Kingfisher County, Oklahoma, Chaparral owns substantial interests in the sections offsetting said Section 22. The ALJ failed to point out that Fairway owns no interest in any of the sections offsetting said Section 22. Furthermore, the ALJ failed to point out that in T17N, R7W of the IM, Chaparral owns a total of 1,900 acres of leasehold and is in the process of finalizing the acquisition of an additional 1,600 acres. The area in and around said Section 22 is a core area for Chaparral concerning the

development of the Oswego and Mississippian separate common sources of supply.

7) The ALJ states that "Fairway has a lease that will expire on December 10, 2015." The ALJ failed to point out that the existence of such lease and its expiration date was not presented until rebuttal testimony as an afterthought. In response to such statement, Chaparral said that it would commence operations in said Section 22 on or before December 10, 2015. Chaparral is proposing to drill a horizontal well in the Mississippian common source of supply in said Section 22 in addition to its proposed horizontal well in the Oswego common source of supply in such section. Chaparral has a rig under contract which is scheduled to commence operations in said Section 22 in September, 2015 at a surface location in the SE/4 of said Section 22. Operations on the location for such well must be commenced prior to September, 2015 when such rig will become available and therefore, operations will be commenced in said Section 22 in sufficient time to preserve any lease the primary term which expires on December 10, 2015.

8) The ALJ failed to state that Fairway had ceased all drilling operations in November, 2014 because the price of oil had declined and that whether Fairway drills the proposed well involved herein in the Oswego common source of supply in said Section 22 may depend upon the price of oil reaching \$65 per barrel. At the time of the hearing herein, the price of oil was within a few dollars of \$65 per barrel; however, at this time that is no longer the case. Given the current price of oil and the testimony of the witnesses for Fairway, there is a real possibility that Fairway will not drill any well in said Section 22 and will not commence operations on or before December 10, 2015. Chaparral is committed to drilling its proposed horizontal well in said Section 22 in the Oswego common source of supply.

9) While the ALJ Report appears to recommend that Fairway be the designated operator, Fairway recommended that Blake be the designated operator. The evidence showed that Blake currently holds no working interest in said Section 22 and will at most earn or acquire 3.2 acres. Chaparral owns 311 acres of working interest in said Section 22. A party currently owning no working interest in said Section 22, but having the potential right to earn up to 3.2 acres, should not be designated as operator to develop such section. The difference in the acres owned by Blake and Chaparral in said Section 22 is "not insignificant."

10) The ALJ Report finds that Fairway intends to utilize a Kelly rig and a pumping unit, while Chaparral intends to use a top-drive rig and submersible pump. The ALJ states that he is not convinced that the use of a top-drive rig and a submersible pump would result in a greater return on the operator's investment in the proposed horizontal well in the Oswego common source of supply and that no evidence was presented by Chaparral to dispute this

conclusion. The ALJ has ignored the evidence presented by Fairway that by using a submersible pump as opposed to a pumping unit, the production of fluid from a well could be increased from 400 barrels per day to 800 barrels per day. Furthermore, the evidence presented by Chaparral showed that by using a submersible pump, a well could produce up to 3,200 barrels of fluid per day. Based upon simple concepts of the time value of money, receiving production earlier than later would have a positive impact upon the return on the investment in the proposed horizontal well in the Oswego common source of supply in said Section 22. The ALJ ignored this evidence.

11) The ALJ concludes that there is not an issue as to whether a rig would be available to Fairway to drill its proposed horizontal well in said Section 22. The ALJ ignored the evidence presented that Chaparral has a rig under contract that is going to be available in September, 2015 to commence operations on its proposed horizontal well, while Fairway has made no effort to obtain a contract for a rig to drill its proposed well. The ALJ's conclusion as set out above as to Fairway obtaining a rig is mere speculation given Fairway's failure to make any effort to obtain a rig.

12) The ALJ further states that he does not believe that "the settlement of a surface use agreement by Fairway would delay the spudding of the well; and there was no testimony to contest this assumption." This conclusion by the AU again ignores the evidence presented that Fairway was not sure of where the surface location for its proposed horizontal well would be located and that Fairway had made no attempt to contact any surface owner in said Section 22 or any offset section to negotiate any surface use agreement. The evidence presented shows that as of the date of the hearing herein, Chaparral had been negotiating for two months with the surface owner the terms of a surface use agreement for the surface location of its proposed horizontal well and that after two months, Chaparral and the surface owner had reached an agreement concerning substantially all of the terms of the surface use agreement except for the amount to be paid for damages. The ALJ's assumption that the failure of Fairway to make any effort to obtain the right to a surface location would not delay the spudding of its proposed well is not based upon the evidence.

13) The ALJ properly states that Chaparral will drill three other wells (one being in said Section 22 and two others being in Section 27, T17N, R7W of the IM, Kingfisher County, Oklahoma) even if it is not named the operator in these proceedings, while Fairway's proposed horizontal well "may be the only well drilled by Fairway this year." The ALJ then concludes that if this proposed horizontal well is the only well drilled by Fairway in 2015, "it will obviously be the focus of that company's time and effort." This conclusion implies that Chaparral will not be focused on its proposed horizontal well in the Oswego common source of supply in said Section 22 because it is much more active in drilling wells in this area. This conclusion is contrary to the evidence presented and is illogical. This area is a core area for Chaparral in regard to

drilling, completing and producing wells and each well drilled in this area by Chaparral will have Chaparral's complete and total focus and attention. Chaparral has moved its field office from Stillwater to Hennessey (just north of said Section 22) to focus on developing this area, has moved a rig under long term contract to this area to drill numerous proposed horizontal wells through at least 2016, and has invested a substantial amount of time and money in acquiring a significant amount of working interests in this area (which efforts continue). Chaparral has constructed and will construct in this area sufficient infrastructure for exploration and development to justify the drilling of a disposal well to handle any water produced from its proposed wells in said Section 22. The area in and around said Section 22 is the area Chaparral will be focusing on for its exploration and development, and every well that Chaparral drills in this area will have the full attention and focus of the Chaparral employees involved with such wells.

14) The ALJ points out that the location of the initial well to be drilled in said Section 22 is an issue of disagreement between the parties. Fairway intends to drill its proposed horizontal well in the Oswego common source of supply in the W/2 of said Section 22, while Chaparral intends to drill its proposed horizontal well in the Oswego common source of supply in the E/2 of such section. The ALJ fails to point out that Fairway agreed that eventually horizontal wells in the Oswego common source of supply would be drilled in the E/2 and in the W/2 of said Section 22 as well as in the approximate center of such section. The ALJ fails to point out that Fairway has not filed any location exception proceeding covering its proposed horizontal well in the W/2 of said Section 22, while Chaparral has filed a location exception proceeding covering its proposed horizontal well in the E/2 of said Section 22.

15) The ALJ in his Report states that "Chaparral stated that if it were named operator, there would be no casing point election" and that "since this Court is recommending Fairway be named the operator, it will be their decision as to what terms are to be offered." This recommendation is extremely puzzling and troubling in that it is unclear as to what the ALJ is recommending. It appears as if the ALJ is improperly recommending that Fairway, as the designated operator, should have the power to dictate and determine the terms that are to be offered to Chaparral under the pooling order, as opposed to having the Commission determine which terms are fair and reasonable.

16) The evidence further showed that the manner in which Chaparral plans to drill, complete and operate horizontal wells in the Oswego common source of supply is much more efficient, effective and economic than the procedures proposed by Fairway. Chaparral proposed to use a Packers Plus system which has been extraordinarily effective in developing the Oswego common source of supply, to use submersible pumps to increase the production from wells in the Oswego common source of supply and to use vapor recovery units so as to avoid wasting produced gas through venting or flaring. Chaparral's use of a

top-drive rig is necessary in order to ensure that if any problem is encountered in the drilling of its proposed horizontal well in the Oswego common source of supply, there will be sufficient power to handle any such problem. Chaparral is proposing to drill four wells from a single pad in said Section 22 which will allow various costs to be allocated to and shared by such wells, resulting in cost savings for each such well. Chaparral has a contract with Packers Plus under which Chaparral is ensured to receive the lower price in Oklahoma for the Packers Plus system, resulting in savings to all owners in the wells operated by Chaparral. Furthermore, Chaparral has employed a consultant to be used in obtaining numerous bids for goods and services to be used in Chaparral's proposed exploration and development in said Section 22 and the surrounding area, which results in Chaparral obtaining such goods and services at the most competitive prices.

17) The ALJ has recommended denial of Chaparral's application in Cause CD No. 201409259. The application of Chaparral covers the Big Lime common source of supply in addition to the Oswego common source of supply, while Fairway's application is limited solely to the Oswego common source of supply. Chaparral treats the Big Lime common source of supply as a secondary objective, but one that may be developed in said Section 22. By denying Chaparral's application, the ALJ has effectively stopped any development at this time of the Big Lime common source of supply in said Section 22 and has created an unnecessary impediment to the development of such common source of supply in such section in the future.

18) Chaparral respectfully requests that the Commission not adopt the Report of the ALJ filed in these causes on July 23, 2015 and that the Commission enter a pooling order in both of these pooling proceedings covering the Big Lime and Oswego separate common sources of supply in the 640-acre horizontal well units formed therefore in Section 22, T17N, R7W of the IM, Kingfisher County, Oklahoma and designating Chaparral as the operator under such pooling order.

THE ALJ FOUND:

1) 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 pooling application of Fairway in Cause CD 201408884 be granted, while the pooling application of Chaparral in CD 201409259 be denied.

2) This Court states that the Supreme Court of Oklahoma has long held that the jurisdiction to determine operatorship in a pooling dispute lies with the Corporation Commission. *Superior Oil Co. vs. Oklahoma Corporation Commission*, 242 P.2d 454 (Okl. 1952) and *Texas Oil and Gas Corporation vs. Rein*, 534 P.2d 1277 (Okl. 1974).

3) Both of the applicants recognized that the issue in controversy is which company will be the designated operator of the drilling and spacing unit. Apart from who would be the operator, there was little else in dispute. During the hearing of these two cases it became clear that both parties are capable operators and either could successfully conduct operations on the proposed unit. Although it was not by a significant amount of time, it is worth noting that Fairway was the first to file its application.

4) Each party has extensive experience in the area. Fairway has drilled a larger number of Oswego wells in the general area, but in uncontested testimony Chaparral stated it has drilled over 250 horizontal wells. While Chaparral is a much larger company, Fairway is an operator with numerous wells in the State of Oklahoma. Both parties are based in Oklahoma City and both possess adequate staff to oversee the development of the unit. This Court rejects any implication that the relatively youthful Chaparral staff is somehow inexperienced or incapable of successfully conducting professional operations. It must also be stated that this Court does not believe that Chaparral is a superior operator by virtue of its size. Due to the fact that the exploration and production teams promoted by each party appeared to be adequately qualified, this Court had to consider the cohesive nature of each team. The fact that the staff at Fairway has changed only slightly during the drilling of the last 12 wells in the area is an important factor. The Chaparral personnel have not been the same team throughout the drilling of its wells in the immediate area. After hearing the testimony of the witnesses this Court concludes that as to operating an Oswego well in this unit, the Fairway team collectively possesses superior expertise.

5) This Court was not surprised that the two parties prepare an AFE in a different manner. An AFE is an estimate only. After looking at the AFE of each party this Court takes note of the fact that even with significant differences in the drilling and completion methods, the cost estimates of the parties is close. There appears to be slightly less than a 6.5% difference between the two cost estimates presented to the Court. Even though Chaparral adjusted their AFE to reflect lower costs, it can be expected that by the time the well is drilled that Fairway will also see some price reductions in the required services, equipment and materials. Again, it must be stated that an AFE is only an estimate of costs; therefore, the difference between the cost estimates of the parties is seen as being negligible.

6) Fairway has a slightly larger acreage position in the drilling and spacing unit than does Chaparral. The difference in the acreage position may be small; however the fact that Fairway has the majority is not insignificant. Additionally, it is of great import that Fairway has a lease that will expire on December 10, 2015. Chaparral did not mention that any of its leases will be expiring soon.

7) The parties differed on the use of certain drilling and production equipment. Fairway intends to utilize more conventional methods by its use of a Kelly rig and a pumping unit. This Court is not convinced that a top drive rig and submersible pump would result in a greater return on the operator's investment in the planned Oswego well. No evidence was presented by Chaparral to dispute this conclusion. Fairway has a relationship with a drilling contractor in the area. Chaparral currently has a rig under contract and the contracted rig would move from other Chaparral locations to Kingfisher County to drill this and other Chaparral wells. Since neither party challenged the other's assumption as to rig availability, this Court must infer that each party believes rig availability would not be an issue.

8) Although Fairway knows the surface owner and has been in contact with said owner, it is waiting on the outcome of the instant case to negotiate use of the surface and build a location. Chaparral is in the process of negotiating use of the surface. This Court does not believe that the settlement of a surface use agreement by Fairway would delay the spudding of the well; and there was no testimony to contest this assumption. Chaparral stated it will drill three other wells even if it is not named the operator of the contested unit. Mr. Vernon stated this may be the only well drilled by Fairway this year. If this well is the only well drilled by Fairway in 2015, it will obviously be the focus of that company's time and effort.

9) The location of the initial well in the unit is an issue of disagreement of the parties. Fairway intends to drill its well in the W/2 of Section 22, while Chaparral intends to drill its well in the E/2 of the section. Fairway stated it does not believe the Oswego to be as promising in the E/2. However, as the operator of the unit, Fairway would not be precluded from seeking Commission approval for the drilling of an increased density Oswego well.

10) Chaparral agrees with Fairway's assessment of fair market value, election times for payment, and what Fairway would offer Chaparral if Fairway were to be named operator. On one point the parties do not agree. Chaparral stated that if it were named operator, there would be no casing point election. This Court finds the terms offered by Fairway to be equitable. Therefore, since this Court is recommending that Fairway be named the operator, it will be their decision as to what terms are to be offered.

11) Additionally, when parties disagree as to who will operate a unit, it is within the discretion of the ALJ, as the finder of fact, to determine who will be the operator and make a recommendation to the Commission. *Grisson Oil Corporation vs. Oklahoma Corporation Commission*, 99 P.2d 134 (Okl. 1940) and *Palmer Oil Corporation vs. Phillips Petroleum Company*, 231 P.2d 997 (Okl. 1951). After hearing each party plead their case it is the recommendation of the ALJ that the pooling application of Fairway be granted, and that the pooling application of Chaparral be denied.

POSITIONS OF THE PARTIES

CHAPARRAL

- 1) **John R. Reeves**, attorney appearing on behalf of Chaparral, contends their pooling application, CD 201409259, should be granted and Chaparral should be named operator under the pooling order. They also state that the ALJ erred when analyzing Fairway as the operator against Chaparral instead of Blake who is the operator Fairway is requesting. Furthermore by denying Chaparral's application the Commission is impeding the Big Lime from production.
- 2) Fairway has the majority interest in the unit with a nine acre difference from Chaparral. Chaparral states that this difference in interest is in no way significant. There is no evidence to show this affects the way the well will be drilled and the ALJ erred in considering this as a significant difference. Chaparral has also moved their headquarters to the area to establish a core for their future production. This is further proven by the fact that Chaparral owns a significant amount of acreage, 1900 acres, in the surrounding area and in the township. Fairway owns none. Blake, the operator Fairway is petitioning for, has a zero percent interest in the unit. Chaparral contends the ALJ should have compared the interest of Blake to the interest of Chaparral. Then there would be a significant difference according to Chaparral.
- 3) Fairway stated that their lease ends in December 2015. Chaparral will commence drilling in September 2015. Chaparral contends they already have authorization to drill the Oswego from the surface owners and by drilling in September this will save Fairway's lease. Saving Fairway's lease should not be an issue about who should be operator.
- 4) Fairway stated that oil prices will determine whether or not they drill this well and that oil prices have caused them to cease production in the past. Knowing where oil prices are right now Chaparral contends that they are concerned about whether Fairway will even drill a well. Chaparral further states they are committed to drilling this well. Their commitment is proven by the several applications they have filed and their negotiations with surface owners. Chaparral has been very active in obtaining authorization to develop this section, much more than Fairway who has only filed a spacing and pooling application.

5) Chaparral contends that the ALJ erred when analyzing the cohesive nature of each team. Chaparral's team has been the exact same for the last 11 Oswego wells they have drilled and they contend their expertise is proven by the information they have gained in trying to develop the Oswego. The finding of Fairway's superior expertise is not supported by the record. The only evidence provided was the expertise of the engineer who testified and his son who prepared the AFE, no one else on the team.

6) Chaparral argues, when the ALJ concluded there was not much difference in the two AFEs, he failed to recognize certain things were left off the Fairway AFE. Things like disposal wells, cement, pipe casing, and a vapor recovery unit were all left off Fairway's AFE but were included in Chaparral's. Chaparral argues these additions to Fairway's AFE would show a more accurate AFE and a larger difference in cost.

7) Finally Chaparral argues that the production equipment they will use will allow for a quicker rate of return for the interest owners and will drill the well more effectively, efficiently, and economically. Fairway admitted that this type of equipment can increase the flow of fluid from the well. Chaparral also states that the equipment that Fairway will be using is too small, cannot overcome problems that may arise, and will not produce effectively. Furthermore Chaparral has their rig ready to drill because this is a core area of production for them.

FAIRWAY

1) **Russell J. Walker**, attorney appearing on behalf of Fairway, contends there are four criteria the Commission uses to ascertain designation of an operator and Blake who is owned by Fairway and is being recommended as operator by Fairway meets all four criteria. First, the company who initiates the act by filing for spacing and pooling first. Second, the company who has the majority interest. Third, the company who can drill a less expensive well. Finally, the company who is better qualified to be the operator.

2) Fairway filed for spacing and pooling first. Fairway states that Chaparral raced to file 13 days later.

3) Fairway owns the majority interest. They bought acreage in the unit first and for the sole purpose of drilling. Once Fairway captured the majority interest in order to be named operator then they stopped buying. Fairway contends that both pooling applications should be granted so the Big Lime can be included, but Fairway should be named operator.

4) Fairway argues that Chaparral's production procedures are unnecessary and therefore Fairway can operate a less expensive well. Fairway has drilled 12 Oswego wells one of which was drilled for \$342,000 cheaper than the AFE estimated for that well and that was when costs were a lot higher than they are now. The rig Fairway will be using can be procured for a substantial amount less per day than the rig Chaparral will be using. Fairway contends the difference in pricing for the rigs is due to Chaparral using a larger rig that is unnecessary. The Chaparral rig will drill a little faster than the top drive rig that Fairway will use but its cost outweighs its production.

5) Finally, Fairway contends that both Chaparral and Fairway are good operators but the Commission must decide who is the better operator of this unit in the Oswego. Fairway has much more experience in this vicinity than Chaparral. Fairway contends that because of their experience in this area they know what production equipment is more cost effective. Chaparral spending more on their equipment to get revenues upfront is unnecessary in this area and will not grant a better return. Fairway contends that the Oswego has been depleted in certain areas and that is why they buy selectively. The amount of land owned by Chaparral should not be a deciding factor in who becomes operator.

6) Fairway also wants to make a concession to Chaparral to prove that Fairway will be drilling a well. Fairway will start the well within 150 days and if it is not started by Blake due to the price of oil then Chaparral can have the last 30 days to drill. Fairway will turn it over and let them drill.

RESPONSE OF CHAPARRAL

1) Chaparral agrees with Fairway about the four criteria the Commission analyzes. Firstly, the company who initiated and prosecuted the action is more important than a ministerial filing. The difference of interest in Fairway and Chaparral is only nine acres and this is not significant enough to prove a difference in operations. Chaparral contends that they will be able to drill more effectively, economically, and efficiently.

2) Chaparral contends that their production equipment is necessary. It complies with the EPA and the power behind their rig is needed to overcome any problems that may arise. Chaparral argues they have put in the time and effort into developing the Oswego and their way is a more efficient way.

3) Chaparral accepts the concession offered by Fairway. If the well is not commenced within 150 days Chaparral will take over. Finally, the broad

statement made by the ALJ about the terms of the order gives the operator too much authority. The Commission is the one who makes the determination about what provisions are to be in the order.

CONCLUSIONS

The Referee finds the Report of the Administrative Law Judge should be affirmed in part, reversed in part and modified in part.

1) The Referee finds the ALJ's recommendation to appoint Fairway as operator under the pooling order to issue in CD 201408884, Fairway's application, is supported by the weight of the evidence and free of reversible error. The ALJ is the initial finder of fact. It is the ALJ's duty to observe the demeanor of the witnesses, assess their credibility, and assign the 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); and *Palmer Oil Corporation v. Phillips Petroleum Corporation*, 231 P.2d 997 (Okl. 1951). However, the Referee would reverse the ALJ concerning the denial of Chaparral's pooling application in CD 201409259 and would grant said application, which includes the request to include production from the Big Lime common source of supply if found productive, but would appoint Fairway as the operator in the Chaparral case. The Commission in Cause CD No. 201409098 pursuant to Order No. 641398 formed 640 acre horizontal well units in Section 22 for the Big Lime and Oswego common sources of supply.

2) The Referee would also recommend that the pooling order to issue in Causes CD 201408884 and CD 201409259 appointing Fairway as operator should include the allowance of a casing point election as one of the terms of the pooling order, along with all of the other terms as agreed to by Chaparral and Fairway and provided for in the ALJ's Report. In addition, there should be a provision included in the pooling order to issue from Cause CD 201408884 and Cause CD 201409259 that Fairway/Blake as operator will have 150 days to start the well after the pooling order issues and then Chaparral can have the last 30 days to drill this well pursuant to said order if Blake/Fairway fails to do so within the 150 days allowed.

3) The Supreme Court in *Texas Oil and Oil Gas Corporation v. Rein*, 534 P.2d 1277 (Okl. 1974) states:

We have previously held that the Commission has considerable discretion in determining which owner is entitled to drill and operate the unit well. *Superior Oil Co. v. Okla. Corp. Commission*, 206 Okl. 213, 242 P.2d 454.

4) The Commission has always focused on a number of different factors in the award of operations. Charles Nesbitt in his Oklahoma Bar Journal article, entitled "A Premier 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 the Commission attaches to them.

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 nonparticipating 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.

5) It is noted in Nesbitt's article, the ownership position of the parties and the actual bona fide exploration activity are the two factors of most importance. The ALJ reviewed those factors in his award of operations. Fairway has the largest working interest position, with Fairway having 9 acres more interest in the 640 acre unit than Chaparral. Fairway is the interest owning/title holding company in the area while Blake is the operating entity. Blake and Fairway are both owned by Blake Vernon and Fairway will assign interest to Blake if Fairway is named operator.

6) Fairway was the first to file its present application in CD 201408884 on December 23, 2014 with Chaparral filing its application on December 19, 2014 in Cause CD 201409259. Fairway allowed Chaparral's spacing to go forward in Cause CD 201409098 because Fairway did not object to including the Big Lime common source of supply in the spacing of this unit, and that's why Fairway did not object at the hearing in the present causes to the granting of both Chaparral's pooling application and Fairway's pooling application so that the Big Lime common source of supply could be included.

7) The testimony reflected that Fairway's cost for drilling the well would be less expensive than Chaparral's. Fairway does not believe that a vapor recovery unit would be necessary as the volatile organics out of the Oswego do not need a vapor recovery unit. Fairway has drilled approximately 12 wells in the Oswego and one that was drilled approximately a year before the present hearing, which was when costs and prices were a lot higher, was drilled in 19 days, with spud to completion 21 days total, and with the setting of pipe, it cost \$342,000 less than the \$2,754,900 that was submitted for the drilling of the present well in this proceeding. The AFE submitted by Fairway is \$2,754,900 while Chaparral's is \$2,945,077. The parties disagree as to which drilling and production equipment is most effective. Fairway utilizes a Kelly rig and a pumping unit while Chaparral uses a top drive rig and a submersible pump. The top drive rig will drill faster but cost more. Both Chaparral and Fairway have rig availability. While Chaparral's equipment will provide more revenues upfront, the equipment is more expensive. The Referee agrees that if you spend a lot more money to get your revenues up front it's not necessarily a better rate of return. Fairway has the same technical team in the last ten Oswego wells that it has drilled and has drilled 12 wells back to back ending in November 2014. The Oswego is approximately 30 feet thick with six to eight feet of pay that is better. The Oswego is not a consistent common source of supply. Fairway holds approximately 8,000 acres in the general area while Chaparral has completed ten horizontal Oswego wells and has experience drilling horizontal wells. Chaparral has a drilling rig under contract in Alfalfa County that will move to Kingfisher County to drill wells for Chaparral.

8) Fairway gave testimony that Fairway is not interested in Section 15 to the north of Section 22 or Section 27 to the south of Section 22 as Fairway does not think it would contain good Oswego. Chaparral uses microseismic to

attempt to evaluate the condition of a reservoir and the testimony reflected that microseismic works very well in the 500 foot thick reservoir like the Mississippian but hardly works at all in the 30 foot thick reservoir like the Oswego.

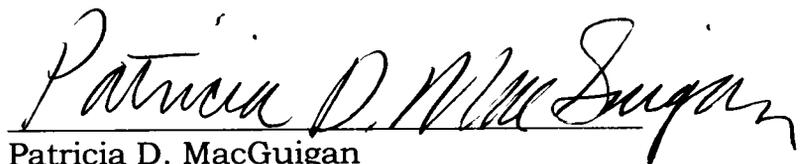
9) Chaparral is in the process of obtaining a surface agreement with the surface owner while Fairway is waiting until the outcome of the instant cause will negotiate use of the surface and build a location. Fairway intends to drill its well in the W/2 of Section 22 while Chaparral intends to drill its well in the E/2 of Section 22. The geology concerning the Oswego is in dispute by Chaparral and Fairway. Fairway does not believe the Oswego to be as promising in the E/2.

10) The Referee finds that the recommendation by Fairway to grant operations to Fairway for the first 150 days of the 180 day period for commencement, with operations then flowing automatically to Chaparral for the last 30 days if Fairway fails to timely commence the well, is reasonable and should be a provision in the order to issue in these matters.

11) The Commission can offer a casing point election under a pooling order and has done so in the past. The Commission does have the power to provide for a casing point election as one of the terms of the pooling order when it is warranted. The Commission has often granted a casing point election when there is evidence establishing that such term or condition is "just and reasonable and will afford to the owner of such tract in the unit the opportunity to recover or receive without unnecessary expense his just and fair share of oil and gas." A casing point election is not a matter of right. *Holmes v. Corporation Commission*, 466 P.2d 630 (Okl. 1970). In the present case the Referee would recommend that such a term is reasonable to negate an advantage and to protect the correlative rights of the participants. Therefore, a casing point election should be allowed and provided for in the order to issue in these causes.

12) The Referee notes that the ALJ considered all of the factors as is normal in operator fights. 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 20th day of October, 2015.


Patricia D. MacGuigan
OIL & GAS APPELLATE REFEREE

PM:ac

xc: Commissioner Anthony
Commissioner Murphy
Commissioner Hiett
James L. Myles
ALJ Keith T. Thomas
Russell J. Walker
John R. Reeves
Michael L. Decker, OAP Director
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