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July 29, 2013

Marshall Enquist, Hearing Examiner
Richard Atkins, Hearing Examiner
c/o Docket Services
Railroad Commission of Texas
Oil & Gas Division
1701 N. Congress, Suite 12-123
Austin, Texas 78701

via Hand Delivery

Re: Oil & Gas Docket No. 02-0278952
Application of EOG Resources, Inc. to Drill Klotzman Lease (Allocation) Well No. 1H, Eagleville (EagleFord-2) Field, DeWitt County, Texas Status No. 744730, as an Allocation Well Drilled on Acreage Assigned from Two Leases

Dear Mr. Enquist and Mr. Atkins:

Attached for filing in the above referenced docket, please find the original and 13 copies of Katherine Larson Reilly and Melanie McCollum Klotzman (Protestants or Klotzmans) ***Protestants' Replies to Exceptions to the Proposal for Decision and Motion to Strike Attachments to Exceptions***. We have also enclosed a copy of this Reply on CD.

Please file in your usual manner, and return a file stamped copy to our courier.

Respectfully submitted,

Patrick F. Thompson

PFT/mah
Enclosure
cc: Service List

BEFORE THE

RAILROAD COMMISSION OF TEXAS

OIL & GAS DOCKET NO. 02-0278952
APPLICATION OF EOG RESOURCES, INC.
TO DRILL KLOTZMAN LEASE (ALLOCATION) WELL NO. 1H
EAGLEVILLE (EAGLEFORD-2) FIELD
DEWITT COUNTY, TEXAS
STATUS NO. 744730, AS AN ALLOCATION WELL
DRILLED ON ACREAGE ASSIGNED FROM TWO LEASES

PROTESTANTS' REPLIES TO EXCEPTIONS
TO THE PROPOSAL FOR DECISION
AND
MOTION TO STRIKE ATTACHMENTS
TO EXCEPTIONS

Katherine Larson Reilly and Melanie McCollum Klotzman (hereinafter "Protestants" or "Klotzmans") submit these Replies to the Exceptions filed in this docket by EOG Resources, Inc. ("EOG"), and by Pioneer Natural Resources USA, Devon Energy Production Company, Laredo Petroleum, Inc. and BP America Production Company ("Intervenors").[1] Protestants will also respond to the "amicus" filed in this docket by Intervenors' law firm on behalf of Woodbine Acquisition, LLC. This pleading also includes Protestants' Motion to Strike voluminous documents that were improperly attached to Intervenors' Exceptions.

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[1] Pioneer, Devon, Laredo and BP intervened in this proceeding and were represented by counsel who filed Exceptions on their behalf. Each of these entities also, inexplicably, filed letters with the Commissioners expressing their opposition to the Proposal for Decision. The reason for doing both is unclear unless intended to create the impression that opposition to the PFD is more widespread than it is.

The strenuous distortions of case holdings and regulatory law in EOG's and Intervenors' Exceptions do not change these facts:

- Combining acreage from separate leases to form drilling or proration units is "pooling" in Texas. EOG's and Intervenors' attempts to deny this are so unsupported that they cannot even come up with another word for the act.
- Ruling in favor of the landowners in this case does not require the Commission to "adjudicate title." The landowners have not asked the Commission to examine a single title document. The landowners prevail in this case based on a single *undisputed* fact – that EOG lacks the authority to pool. The rest of the decision is merely application of Commission Statewide Rules.
- The leading case authority on horizontal drilling, the *Leucke* case, does not authorize what EOG proposes to do – it prohibits it.
- Professor Ernest Smith does not bless the practice of drilling horizontal wells without pooling authority --- he warns operators to obtain the necessary amendments to their pooling authority before attempting it.
- Heavily qualified letters and Powerpoint presentations by Commission staff do not override lawfully adopted Commission rules and orders.
- Adoption of the Examiners' Proposed Decision will not cause the waste of a drop of oil or an mcf of gas. For the one-third-of-one-percent of the horizontal wells being drilled that may be affected by this decision, the

decision simply respects the landowners' rights to lease his or her minerals how and to whom he or she chooses. Operators who respect that right will be able to drill all wells necessary to maximize production.

1. EOG and Intervenors Exaggerate the Significance of "Allocation Wells"

Intervenors claim that adoption of the Examiners' Proposal for Decision will cause "enormous physical and economic waste" and will have "tremendous statewide impact on operators' ability to permit and drill horizontal wells."(Intervenors at 2 and 20.) This claim is false for two reasons: (1) the numbers don't support it; and (2) if the decision causes Intervenors to refrain from drilling any future wells, it is because the Intervenors elected not to obtain the rights necessary to drill the wells from the mineral owners.

The "start date" for "allocation wells" is April 2010, when Mr. Lineberry wrote the letter to Mr. Sullivan that Intervenors assert authorized "allocation wells." Between that date and the date of the hearing in this docket, the Commission issued 18,335 permits for horizontal wells. (PFD at 18) Of those, 55 were "allocation wells." *Id.* Therefore, during the entire period in which "allocation well" permits were issued, they accounted for just three tenths of one percent of all the horizontal wells permitted. This means that 99.7% of the time, operators were able to drill the horizontal wells they desired without resorting to an end-run around their lack of pooling authority. If EOG and Intervenors were less intransigent in their negotiations with mineral owners, the number would be even higher.

EOG and Intervenors have attempted to interject evidence from outside the record by asserting in their Exceptions that additional "allocation well" permits have been issued since the hearing in this docket. They claim fifty additional permits have been issued. Because the Commission also proceeded to issue non-"allocation well" permits to horizontal wells during this time, there is no reason to believe that the percentages discussed above have changed. So we are still talking about an order that will affect, at most, one third of one percent of the horizontal wells being drilled. In addition, the assertion that additional permits have been issued is suspect as an argument because, according to EOG's attachment, the majority of such permits issued were sought by EOG and the Intervenors. Their argument is akin to a Defendant arguing that his questionable conduct should be excused because he has done it several more times since the trial.

EOG, Intervenors and the few other operators who have objected to the Examiner's Proposed Decision have the capacity to turn a proposed "allocation well" into a standard well by simply acquiring the necessary rights from the mineral owner. As counsel for EOG stated at the hearing in this docket, "None of the other allocation permits have pooling authority. If they did we wouldn't be here. We would be forming pooled units." (Transcript, p. 17) Adoption of the Proposal for Decision will not cause the waste of a single drop of oil or mcf of gas, but it will restore order to the Commission's permitting process and prevent drilling permits from being used as tools by a small minority of operators to run roughshod over the property rights of mineral owners.

2. In Denying the Permit, the Commission is Not "Adjudicating Title," It is Enforcing Its Own Rules

Despite EOG's and Intervenors' insistence to the contrary, Protestants and the Commission's Examiners are fully aware of the fact that the Commission does not have the authority to adjudicate title. This is a red herring. Protestants are not asking the Commission to adjudicate title. Protestants are asking the Commission to enforce its own rules – rules that require an operator seeking to combine acreage from separate leases into a single drilling unit to represent in good faith that it has the right to do that. Statewide Rule 40 has required that for more than thirty years --- and it has never been amended to make an exception for when the operator chooses to label his well an "allocation well."

The Klotzmans did not introduce any leases or title documents into the record. EOG did. It is not necessary to examine a single title document to decide in favor of the Klotzmans. All parties agree that EOG does not have the right to pool the subject acreage. That is not in dispute and does not require determination by the Commission. That fact having been established, all the Commission needs to do to find in favor of the Klotzmans is to enforce its own rules.

3. Creating a Drilling Unit from Separate Leases Requires Authority to Pool

In their Exceptions, EOG and Intervenors assert repeatedly that the Commission's Examiners are confused about what constitutes "pooling." The Commission's Examiners are not confused – despite the best efforts of EOG and Intervenors to obscure the issue.

EOG and Intervenors assert that because what EOG is doing does not achieve a

cross-conveyance of interests, it is not "pooling." This is akin to a person saying that they do not need a license to drive because they are not driving, they're speeding. The fact that EOG is not creating something that includes all of the elements of a 1950's traditional-lease-language "pooled unit" does *not* mean that EOG is not "pooling." As the Examiners correctly note, combining acreage from separate tracts for purposes of creating a drilling or proration unit *is* "pooling." Statewide Rule 40 makes that clear.[2] EOG tries to refute this by pointing out that the Court in *Leucke* said that "the grant of a permit to drill does not result in the valid pooling of the separately owned interests within the drilling unit." (EOG p.5) EOG turns the meaning of that passage on its head. One of the important holdings of the Court in *Leucke* is that the operator violated the pooling provisions in the relevant lease by creating a unit that improperly diluted the Lueckes' interests. In the quoted passage, the Court is saying that the issuance of a permit by the Commission did not fix that problem – the operator failed to create a valid unit because he violated the terms of the lease. In that respect, *Leucke* is important here for two reasons: (1) the Court clearly holds that the right to pool – and the proper execution of that right – are relevant when completing a horizontal well across lease lines; and (2) the issuance of a permit by the Commission cannot fix an operator's lack of pooling authority or failure to exercise that right in conformity with the terms of the lease.

When EOG and Intervenors argue that mere issuance of an "allocation well" permit will not create a forced pooling of separate tracts, they are attempting to obscure

[2] Professor Smith also makes it clear: "Pooling is the process of combining small tracts into an area of sufficient size to merit a well permit under the field's applicable spacing rule." 2 Smith & Weaver, Texas Law of Oil and Gas, §11.1[B].

the issue by posing it backwards. Protestants know full well that issuance of a permit will not create a pooling of their minerals --- because Protestants' leases do not give EOG the power to pool its acreage for oil --- and, as the Examiner's correctly observe, that power originates with the mineral owner and must be conveyed to the operator before the operator may utilize it. The Examiners have correctly found that the permit EOG seeks cannot be issued because EOG does not have the authority to drill the well as proposed. Drilling the well as proposed will, by necessity, involve combining acreage from separate leases to create the drilling unit. Under the Commission rules and the subject leases, that is "pooling" and EOG was not granted the authority to pool. The cases and authorities cited by EOG and the Intervenors for the proposition that issuance of a Railroad Commission drilling permit does not "effect" pooling are completely beside the point. No one disputes that holding. The real issue is that an operator must have the contractual right to pool *before* he may combine acreage from separate tracts for a drilling unit. EOG does not have that right and therefore it cannot satisfy the Commission's requirements for a drilling permit.

4. The Permit Sought by EOG Would Violate Commission Rules

The Examiners correctly found that "There is no Texas statute, Commission statewide rule or Commission final order authorizing the permitting of 'allocation wells.'" (FF No. 10) EOG and Intervenors challenge this Finding, but then fail to identify *any* statute or Commission rule that even mentions "allocation wells," much less authorizes permits for them. EOG asserts merely that the Commission has "broad

authority" to issue drilling permits, which misses the point. Intervenors assert, surpisingly, that EOG complied with applicable rules because EOG "properly filed a PSA-12." (Intervenors p.14) The form PSA-12 is entitled "Production Sharing Agreement Code Sheet" and it requires operators to provide the "Sharing Agreement Name" and "Description of the Individual Tracts Contained Within the Production Sharing Agreement."[3] But EOG, by its own admission, *had no Sharing Agreement* with the mineral owners. How can an operator "properly" complete a form that asks for the name of the subject Sharing Agreement and for a description of property covered by the Sharing Agreement, when there is no Sharing Agreement? The fact that Intervenors assert that this is a "proper" way for an operator to apply for an "allocation well" permit is an excellent indication of how a small minority of operators have distorted Commission procedures in the pursuit of improper permits.

Intervenors assert that EOG's application does not violate Commission Statewide Rule 40's requirement that the operator file a Form P-12 "because the Form P-12 applies to pooled units, and EOG has not formed a pooled unit." Intervenors failed to read Rule 40. The rule *begins* with the statement: "An operator may pool acreage, in accordance with appropriate contractual authority and applicable field rules, *for the purpose of creating a drilling unit or proration unit* by filing an original certified plat delineating the pooled unit and a Certificate of Pooling Authority, Form P-12." 16 Tex. Admin. Code §3.40(a) (emphasis added). It is impossible for EOG to deny that it is combining acreage

[3] Intervenors incongruously assert (on p. 16) that "It is not clear what the source is of Proposed Finding of Fact 10b's statement that the PSA-12 is 'intended' for production sharing agreement wells." Intervenors submit that it should be clear from the title and the wording of the form itself.

from separate leases for purposes of creating a "drilling unit." Rule 40 therefore requires the filing of a Form P-12. Rule 40 specifically provides that "The operator shall file the Form P-12 and certified plat: (A) with the drilling permit application when two or more tracts are joined to form a pooled unit *for Commission purposes to obtain a drilling permit."* 16 Tex. Admin. Code §3.40(5)(emphasis added).

An operator who combines acreage from separate leases to create a drilling or proration unit is "pooling" the acreage for purposes of Statewide Rule 40. Commission rules and forms allow an operator to combine acreage from separate leases for such purposes only if they have authority to do so from the respective mineral owners. On the Form P-12 itself, the operator is directed to "separately list each tract committed to the pooled unit by *authority granted to the operator*." §3.40(a)(2)(A)(emphasis added). Statewide Rule 40 also contains other provisions intended to protect the interests of mineral owners "for which pooling authority does not exist." §3.40(b)&(c).

The activity EOG proposes is the activity regulated by Rule 40. Minerals from one lease will be commingled with minerals from a separate lease and produced through a single well. When performed pursuant to a claimed right to produce from both tracts, that is "pooling" for Commission purposes and Commission rules require that the operator have the explicit authority from the mineral owner. That authority may come from a traditional pooling clause or from a separate agreement such as a Production Sharing Agreement.

EOG has argued that, because the well is completed on both tracts, the result is not "pooling." It is, they argue, as if there were a well completed on each tract. That,

however, is not true. Production from separate leases through a horizontal well that crosses the lease line cannot be separately measured. It can only be allocated by some formula that is either entirely arbitrary or, at best, an attempt to approximate the volume of hydrocarbons produced from each lease. That would not be true if there were separate wells completed on each lease.

A lessor's right to actual measurement of the hydrocarbons produced from his lease is protected by Statewide Rule 26 (and the lessor's lease). Even if it were proper to regard EOG's proposed horizontal well as "a well on each tract," the way EOG proposes to operate the wells would violate Rule 26.

Rule 26 requires all "oil and other liquid hydrocarbons" to be measured "before the same leaves the lease from which they are produced." 16 Tex. Admin. Code §3.26(a)(2). Obviously, production from the non-surface-location lease will leave that lease without being measured. It is impossible for EOG to operate the proposed well in compliance with Rule 26. Rule 26 provides for exceptions when the two tracts "have identical working interest and royalty interest ownership in identical percentages" or when no protest to the proposed commingling is received after 21 days' notice to all working and royalty interest owners and other specified conditions are met. §3.26(b)(1)(C). These exceptions do not apply to EOG's requested permit. Tr. at 51. The Klotzmans are therefore entitled to the protections afforded by Rule 26.

Intervenors attempt to excuse an allocation well's compliance with Rule 26 by asserting that Rule 26 exists only so that the Commission can enforce allowables and that it is therefore inapplicable to allocation wells because "An allocation well, on the other

hand, is treated as a single well for regulatory purposes and is assigned only one allowable." (Intervenors p.14) There are at least two problems with this excuse. First, it is not true that Rule 26 exists solely for the purpose of enforcing allowables. If that were true, Rule 26 would not include a provision that allows an exception if the affected mineral owners consent. Obviously, one of the purposes of Rule 26 is to protect mineral owners. Second, Intervenors are inconsistent about whether an "allocation well" is one well or multiple wells for regulatory purposes. When seeking to avoid the requirement that an applicant for an "allocation well" permit certify that he has pooling authority, Intervenors contend that an "allocation well" is the equivalent of "multiple wells" producing from all of the traversed tracts. For the Intervenors, an "allocation well" is "multiple wells" when that is necessary to evade one regulation, but a "single well" when needed to evade another.

Far from being "in compliance with" Commission rules, EOG's requested permit would violate Statewide Rule 40 and would inevitably result in a violation of Statewide Rule 26. See Tr. at 131.

5. Issuance of "Allocation Well Permits" is Not a "Well Established" or "Well Reasoned" Practice

EOG and Intervenors contend that the issuance of "allocation permits" such as the permit sought by EOG in this case is a "well established" and "well reasoned" practice. It is neither.

As the Commission's Examiners correctly note, the Commissioners have never adopted a rule or order, or statement of policy, or *anything* authorizing the issuance of the type of drilling permit EOG seeks here. (PFD p.18) In fact, the Commissioners actions have been to the contrary. In 2009, the Commissioners voted unanimously to adopt a recommended decision that rejected Devon's proposal to make "allocation wells" part of the field rules for the Carthage (Haynesville Field). Oil & Gas Docket No. 06-026200.[4] The Proposal for Decision adopted in that case stated that the practice would be "unprecedented in Commission practice" and would "far exceed the Commission's statutory authority."[5] On another occasion, two of the Commissioners voted to approve a Production Sharing Agreement well permit *if* the operator could represent that he had at least 65% of the mineral ownership in each tract signed on.[6] EOG does not profess to have a Production Sharing Agreement with the mineral owners.

Despite the fact that there has never been any action by the Commissioners authorizing "production allocation wells" -- and despite that fact that the Commission has never sought to amend or repeal rules that prohibit them (Statewide Rules 40 and 26), EOG and Intervenors insist on calling the issuance of such permits "an established practice."

Intervenors contend that there have "historically" been three procedures for granting drilling permits for wells that traverse multiple leases. Intervenors describe these three methods as: (1) pooling, "where the applicant has the right – and desires—to

[4] The Examiners in this proceeding took official notice of the file in Docket No. 06-026200.
[5] PFD in Docket No. 06—026200 at 14.
[6] Railroad Commission Minutes of Formal Commission Actions, September 9, 2008.

pool acreage from the tracts to be traversed"; (2) production sharing agreement wells "where the applicant seeks and obtains requisite approvals from parties with an interest in the well in the form of a production sharing agreement"; and (3) "allocation wells." (Intervenors p. 3) This set of procedures does not make sense. If the approvals obtained from parties to drill Production Sharing Agreement wells are "requisite" --- as Intervenors themselves describe them, what sense does it make to have an option like "allocation wells" where no agreement at all from the interest holders in the well is required? In fact, Intervenors and EOG obviously believe that it is proper to obtain an "allocation well" permit without even providing notice to the parties with interests in the well.

Typically, when Commission rules provide an alternative means of obtaining a permit that excuses compliance with some of the normal requirements for such a permit, the rule includes some sort of check in the procedure – such as the requirement that the applicant provide notice to affected parties and give them 15 or 21 days to protest the proposed permit. But under EOG's and Intervenors' version of "allocation well" permit procedures, there is no such check. An operator merely needs to call his well an "allocation well" in his application and he is instantly excused from the normal requirements of certifying his right to pool or acquiring the "requisite" approvals from parties with interests in the well. Why? EOG and Intervenors contend that an applicant for an allocation well must have the right to produce from the tracts to be traversed, but that is also true for pooled unit wells and production sharing agreement wells. In EOG's and Intervenors' system, what is a drilling permit applicant required to prove or do in

order to be excused from certifying his right to pool or obtaining agreements from mineral owners? Nothing. That doesn't make sense. It is like saying: "You can get a driver's license by: (1) proving your age and passing the driver's test; or (2) proving that you have been issued a valid driver's license in another state; or (3) just asking for it, without doing anything else."

EOG's and Intervenors' insistence that EOG is entitled to the requested drilling permit is a collateral attack on the Commission's existing rules. In arguing that EOG is entitled to the requested permit without certifying its right to pool the affected acreage, EOG and Intervenors are asserting that the Commission has no right to enforce Statewide Rule 40. If that is what EOG and Intervenors believe, their remedy is to sue the Commission to have Rule 40 declared invalid, not to simply insist that it be ignored.

Intervenors state in their Exceptions that the "allocation question is not implicated by an application for a permit to drill," but one of those very Intervenors, Laredo Petroleum, contradicted that statement when it described the procedure for issuing "allocation well" permits in its letter to the Commissioners: "Under this third approach, *provided the allocation method by which ultimate production will be apportioned appears reasonable*, the permit has been granted (until the recent PFD)." (Laredo Ltr. Dated July 15, 2013, emphasis added.) The fact that an Intervenor critical of the Examiner's Proposed Decision cannot remain consistent in its description of "allocation well" criteria from one pleading to the next serves to demonstrate that there is, in fact, no "well established" or "well reasoned" process for considering or issuing "allocation well"

permits. The process has been conducted *outside of* existing Commission regulations and is therefore a source of confusion even for its proponents.

6. EOG and the Intervenors Misrepresent the Court's Holding in *Leucke*

In their Exceptions, both EOG and Intervenors misrepresent the holding of the Third Court of Appeals in *Browning Oil Co., Inc. v. Leucke*, 38 S.W.3d 625 (Tex. App. – Austin, 2000, pet denied). *Leucke* held that the drilling of a horizontal well across different lease tracts, with no authority to pool, violated the express terms of the Leuckes' lease.

In *Leucke* the royalty owners, the Leuckes, brought suit against the operator, Browning Oil Company, alleging that Browning violated the pooling provisions in the respective leases when it completed a horizontal well across three leases. The pooling provisions included anti-dilution features that the Leuckes alleged were violated by the shape and composition of the unit for the horizontal well. On that point, the Leuckes prevailed in the trial court and the Court of Appeals upheld that decision, rejecting the operator's argument that the special attributes of horizontal drilling somehow excused compliance with the pooling provisions in the lease. The Court held: "Nothing in the pooling provisions limits their applicability to vertical wells. . . . Indeed, it is because the provisions were not specifically limited to vertical wells that Lessee attempted to amend the provisions to gain authority to further dilute the Leuckes' share in horizontal well units." *Id.* at 640.

The operator next contended that his actions were justified because the completion of a horizontal well that complied with the lease pooling provisions would have been uneconomic. The Court of Appeals rejected that argument as well, holding: "If these Lessees determined that drilling a horizontal well on an eighty acre unit was economically impractical, they could have attempted to expand their pooling authority . . They could have sought field-wide regulatory action . . . Failing that, they could have exercised the option of not drilling a well on the Leuckes' tracts. What they could not do was pool the Leuckes' interests beyond the authority expressed in the leases." *Id.* at 642.

Far from holding that pooling authority is unnecessary for the completion of a horizontal well, as EOG and Intervenors contend, the Court in *Leucke* held that the driller of a horizontal well was bound by the pooling provisions in the leases. In fact, the court offers some advice to operators planning to drill horizontal wells, noting: "Indeed several legal articles and treatises have advised lessees to seek amendments to existing leases prior to drilling horizontal wells." *Id.* (citations omitted) EOG should heed the Court's advice.

7. EOG's and Intervenors' Reliance on the Smith Letter is Misplaced

EOG's and Intervenors' reliance on the Smith letter is misplaced for three reasons: (1) as a letter solicited by one of the parties for a proceeding in 2009, it is neither valid evidence in this case nor a citable authority; (2) by its own terms, it does not address or even consider regulatory issues; and (3) the proposition for which EOG and Intervenors

cite the letter is flatly contradicted by Professor Smith's statements in an authority that *is* citable – his treatise on Oil & Gas Law co-authored with Prof. Jacqueline Weaver.

Professor Smith's letter is not expert opinion testimony. Professor Smith's statements were not sworn. He was never a witness and he was never subject to cross-examination or to clarifying questions from the Examiners. His letter is not a learned treatise or widely accepted authority. It is a letter solicited by a party to the case. In contrast, the Smith statements relied upon by the Examiners in the Proposal for Decision are from an accepted learned treatise. Those are the only Smith statements that warrant consideration.

In the letter solicited by Intervenors' counsel and relied upon extensively in EOG's and Intervenors' Exceptions, Professor Smith never addresses Railroad Commission rules or enabling statutes. He never addresses regulatory questions, such as the issuance of disputed permits, at all. In fact, when Intervenors' counsel solicited the letter, he instructed Professor Smith that "it is not necessary to consider the need for regulatory approvals." (Smith letter pp. 1-2) In the letter, Professor Smith said he honored that instruction.

Professor Smith states repeatedly and explicitly in the letter that his opinion is premised on the assumption that the subject leases contained "traditional pooling clauses" and that pooling authority has been properly exercised. (Smith letter pp. 1, 9) That would distinguish the scenario on which he was opining from this case. Intervenors have contended that those statements are, essentially, irrelevant because the pooling authority granted by the leases in the hypothetical presented to Professor Smith had already been

exercised by the operator with respect to the subject tracts. If that is true, it begs the question of why Professor Smith's opinion is so carefully and explicitly premised on the existence of that pooling authority.

Lastly, but also important, the opinions that EOG and Intervenors attribute to Professor Smith based on the letter are flatly contradicted by what Professor Smith states explicitly in his treatise, Texas Law of Oil & Gas, Ernest E. Smith and Jacqueline Lang Weaver (Lexis/Nexis Matthew Bender 2013).

In part 4.8[C][2] of his treatise, addressing express provisions of oil and gas leases in Texas, Professor Smith takes up the issue of how horizontal drilling affects the rights that operators must acquire from mineral owners:

> "Other changes in both printed form and special additions thereto may be necessary if the lessee anticipates engaging in new or experimental drilling techniques. To maximize the benefits of horizontal drilling, a lessee may need considerable flexibility in determining how much acreage to pool, for the size of the proration unit permitted a horizontal well is based on the length of the horizontal well bore and so is not determined until after a well has been completed. *The lessee also needs to assure that it is authorized to pool land into the long, relatively narrow unit which is consistent with the model used in setting the proration allowable for horizontal wells within the field."*

(emphasis added)

Professor Smith clearly does not believe, as EOG and Intervenors contend, that pooling authority is irrelevant to the completion of horizontal wells.

EOG should be required to do what the great majority of other operators in Texas have done prior to combining acreage from separate leases for horizontal drilling units – acquire the necessary pooling rights from the mineral owner.

8. EOG Cannot Meet the Requirements for the Permit It Seeks, Regardless of Whether the 2010 Permit to Devon Was Valid

In their Proposal for Decision, the Examiners distinguish the first well to receive an "allocation well permit" – Devon's Taylor-Abney-Obanion Well --- from the well EOG seeks to drill, noting that the leases on the tracts for the Devon well must have included pooling authority because Devon sought to drill across three pooled units. In contrast, the leases on the tracts for which EOG seeks a permit do not confer authority to pool for oil production. In their Exceptions, Intervenors argue that this distinction is "irrelevant" because Devon did not represent to the Commission on its drilling application that it was pooling the three units. EOG likewise contends that the existence of pooling authority in the Devon leases was irrelevant because the fact that the operator had the authority to create the original three pooled units "does not mean that that they possessed authority to pool the acreage comprising the allocation unit on which the well was being drilled." (EOG p.10) It is true that the fact the leases gave authority to create the original pooled units does not necessarily mean that they also gave authority to create the new unit for Devon's horizontal well – but it does not necessarily mean that they did not give such authority, either. The distinction noted by the Examiners is real –- in the leases involved in the Devon case, the mineral owners conferred the power to pool on the operators. In the leases involved in this case, they did not. Devon and EOG may both now contend that the distinction is irrelevant, but that does not appear to be the position taken in the Smith letter that Devon supplied and that Mr. Lineberry may have relied upon.

The most extraordinary part of this discussion is EOG's statement regarding other operators who may have previously pooled portions of the acreage in their leases. He says that such "does not mean that they possessed the authority to pool the actual acreage comprising the allocation unit on which the well is being drilled." That is true. He goes on to say: "Indeed, if these allocation well permit applicants possessed pooling authority for the wells they wanted to drill, they would have permitted such wells on pooled units and not as allocation wells!" (EOG p.10) This is probably also true, because a prudent operator will not resort to an unauthorized, legally questionable and risky approach such as an "allocation well" when a perfectly legal alternative is available.

9. Intervenors Improperly Attached Non-Record Evidence to Their Exceptions

With a few exceptions[7], the documents attached to Intervenors' Exceptions as "Intervenor's Exhibits" are improper attempts to circumvent the Commission's rules regarding the introduction of evidence in contested cases. Devon, Laredo, Pioneer and BP all intervened in the EOG proceeding. Their counsel was present during the hearing and had the opportunity to present evidence. Intervenors chose instead to wait until after the evidentiary record was closed, and the Proposal for Decision issued, to introduce their numerous "exhibits." Intervenors' actions not only denied the other parties the opportunity to cross-examine witnesses regarding the "exhibits" or to rebut them or address them in closing arguments, Intervenors also denied the Examiners the opportunity to address the "exhibits" in the Proposal for Decision.

[7] Attachments C and D are already in the record. Protestant does not object to Attachments C and D.

The Commission's procedural rules specifically provide that, "no exhibit shall be filed in any proceeding after the hearing has been completed" unless specifically requested by the commission, the Legal Division Director or the Examiner. 16 Tex. Admin. Code §1.106(d). No such request was made in this case. Intervenors cannot request "official notice" of the attachments either. "A party's motion for official notice must be made or filed *prior to the conclusion of the evidentiary hearing*." 16 Tex. Admin. Code §1.102(b)(emphasis added). The evidentiary hearing in this docket concluded more than seven months ago.

Intervenors' excuse for their untimely request is that, until the Proposal for Decision was released, Intervenors could not have anticipated that the Proposal would contain statements "not consistent with Commission practices" on allocation wells. This is disingenuous. The hearing in this docket was about a permit sought by EOG --- *not* by any of the Intervenors --- to drill a well on two tracts in which the Intervenors own absolutely no interest. Devon and the others intervened in the hearing precisely because they believed that the decision could have an impact beyond the Klotzman lease – there was no other reason for them to intervene. The Intervenors simply chose to sit on their "exhibits" until long after all other parties' opportunities for presenting evidence were past. The Intervenors cannot justify disregarding the Commission's procedural rules and the rules of evidence based on the fact that they "could not have reasonably anticipated" that the Klotzmans would be given the relief they were seeking – the denial of an invalid permit.

The Intervenors' actions here are akin to a defendant, having chosen to rest after the prosecution presented its case, changing his mind after hearing the jury's "guilty" verdict.

Aside from being untimely, Intervenors' attachments are not competent evidence. They are neither sponsored by a witness nor certified. If offered for the truth of anything asserted therein, they are hearsay. Their inclusion is a threat to the integrity of this proceeding. Protestants move that the non-record attachments to Intervenors' Exceptions be struck.

10. The Intervenor's About-Face on Rulemaking

Intervenors assert that the Proposal for Decision as drafted will have "statewide impact" but that the notice of the proceeding was provided "only to EOG and Klotzman." Intervenors assert that if the Commission is inclined to adopt the Examiners' proposed decision, the Commission must proceed through rulemaking. (Intervenors p.20-21) This assertion is both wrong and hypocritical. It is wrong, because the Klotzmans are merely asking the Commission to apply its own existing rules and deny EOG the requested permit. No rule requires adoption or amendment in order for the Commission to grant the Klotzmans the relief they seek. It is hypocritical because the operators who invented "allocation wells," who include the Intervenors, made no effort to "provide notice" to other potentially affected parties, such as mineral owners, when they persuaded Commission staff to issue the first "allocation well" permits. They did not propose that the Commission adopt a new rule or that the Commission amend an existing rule. In fact,

when mineral owners subsequently proposed to the Commission that it initiate a rulemaking to address the chaos and confusion surrounding the issuance of "allocation wells," the Intervenors opposed it.

It is illogical for the Intervenors to take the position that a practice can become "well established" and "historic" at the Commission when its existence is reflected only in a few staff letters and powerpoint presentations, but to insist that before that practice can end or be modified, the Commission must adopt a rule.

No rule was adopted or amended before the first "allocation well" was permitted. No order was issued by the Commission in a contested case.[8] (PFD p. 18) Without notice to anyone, a small group of operators persuaded staff to issue permits that denied mineral owners the protections afforded them by Statewide Rules 40 and 26. The Klotzmans are merely asking the Commission to enforce those rules. That does not require a rulemaking.

11. The Woodbine Amicus

The premise of the Woodbine amicus is that the Commission does not have the authority to require that an operator have pooling authority before combining acreage from separate leases to create a drilling unit. Woodbine provides no citation for this proposition and it is false. Statewide Rule 40 provides that an operator seeking to combine acreage from separate tracts to form a drilling or proration unit must file the

[8] Importantly, neither EOG nor the Intervenors object to Finding of Fact No. 7 which states that "Commission staff members do not speak for the Commission," and "Only a majority of the three elected Commissioners speak definitively for the Commission."

appropriate forms and represent to the Commission that it has the right perform that combination -- the right to pool the affected acreage. No party has argued that the Commission lacks the authority to adopt or enforce Statewide Rule 40.

Woodbine tries to obscure this issue by suggesting that the Commission is creating some new right in the mineral owner or taking away some right held by the operator. It is not. It is merely basing the administration of its rule on the rights currently held by the parties. Texas law is clear that the right to pool is one of the rights vested in the mineral owner, a part of the mineral estate. That right, like the right to drill, can be granted or withheld. Absent an express grant of pooling rights to the lessee, the lessee has no authority to pool or combine the leased premises with other lands for purposes of drilling and producing the well. An essential part of the right to pool is an agreement on how production from the pooled well will be allocated among tracts in the unit. EOG seeks a permit to drill a well without any such authority from the lessee. Commission rules require that EOG demonstrate its right to pool. It has failed to do so. Its permit should be denied.

CONCLUSION

The Klotzmans respectfully request that the Commission adopt the Examiners' Proposal for Decision, without changes, enforce its existing rules, and deny EOG's application for a permit to drill the Klotzman Lease (Allocation) Well No. 1H.

Respectfully submitted,

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Certificate of Service

I certify that on July 29, 2013, a copy of the foregoing Protestants' Replies to Exceptions to the Proposal for Decision was sent by **regular mail**, or by **email** if so indicated, to the persons listed below.

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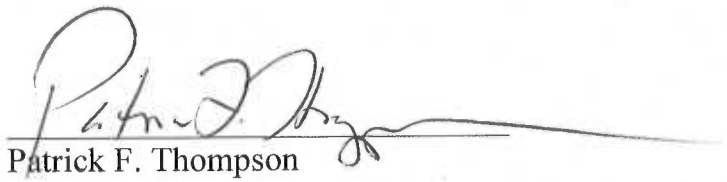

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