No. 23-0772

In the Supreme Court of Texas

ELSIE OPIELA and
ADRIAN OPIELA, JR.
Petitioners
v.
RAILROAD COMMISSION OF TEXAS and
MAGNOLIA OIL & GAS OPERATING, LLC
Respondents

On Petition for Review from the
Court of Appeals for the Third Judicial District at Austin
Cause No. 03-21-00258-CV

PETITION FOR REVIEW OF ELSIE OPIELA and ADRIAN OPIELA, JR.

John B. McFarland
State Bar No. 13598500
William Christian
State Bar No. 00793505
Marianne W. Nitsch
State Bar No. 24098182
Mark A. Stahl
State Bar No. 24125420
GRAVES, DOUGHERTY, HEARON & MOODY, PC
401 Congress Ave., Suite 2700
Austin, Texas 78701
(512) 480-5600 Tel
(512) 480-5804 Fax

Attorneys for Petitioners

IDENTITY OF PARTIES AND COUNSEL

PARTIES	COUNSEL
Elsie Opiela and Adrian Opiela, Jr. *Petitioners*	John B. McFarland jmcfarland@gdhm.com William Christian wchristian@gdhm.com Marianne W. Nitsch mnitsch@gdhm.com Mark A. Stahl mstahl@gdhm.com GRAVES, DOUGHERTY, HEARON & MOODY, PC 401 Congress Ave., Suite 2700 Austin, Texas 78701 (512) 480-5600 In the trial court and court of appeals: Guillermo A. Alarcón Mary A. Keeney Nicholas M. Miller GRAVES, DOUGHERTY, HEARON & MOODY, PC

PARTIES	COUNSEL
Railroad Commission of Texas *Respondent*	Kellie E. Billings-Ray kellie.billings-ray@oag.texas.gov Shelly Doggett shelly.doggett@oag.texas.gov OFFICE OF THE ATTORNEY GENERAL Environmental Protection Division P.O. Box 12548 (MC-066) Austin, Texas 78711-2548 In the trial court and court of appeals: Priscilla M. Hubenak OFFICE OF THE ATTORNEY GENERAL
Magnolia Oil & Gas Operating, LLC *Respondent*	Mark Hanna mhanna@scottdoug.com Stephanie Kover skover@scottdoug.com Jane M.N. Webre jwebre@scottdoug.com SCOTT DOUGLAS & MCCONNICO LLP 303 Colorado Street, Suite 2400 Austin, Texas 78701 Thomas R. Phillips tom.phillips@bakerbotts.com Jason Newman jason.newman@bakerbotts.com Travis L. Gray travis.gray@bakerbotts.com BAKER BOTTS L.L.P. 98 San Jacinto Blvd., Suite 1500 Austin, Texas 78701

TABLE OF CONTENTS

INDEX OF AUTHORITIES

Cases **Page(s)**

INDEX OF AUTHORITIES (CONT.)

Statutes **Page(s)**

Rule

Secondary Authority

STATEMENT OF THE CASE

Nature of the Case	Judicial review of an order of the Railroad Commission of Texas.
Trial Court Judge	Judge Karin Crump.
Trial Court	53rd District Court of Travis County.
Trial Court Disposition	The trial court reversed the Commission's order and remanded to the Commission.
Parties in the Court of Appeals	Appellants: Railroad Commission of Texas Magnolia Oil & Gas Operating LLC Appellees: Elsie Opiela Adrian Opiela, Jr.
Court of Appeals	Third Court of Appeals, at Austin.
Participating Justices	Chief Justice Darlene Byrne authored the opinion of the court, joined by Justice Edward Smith. Justice Chari L. Kelly authored a dissenting opinion.
Citation of Opinion	*R.R. Comm'n of Tex. v. Opiela*, ___ S.W.3d ___, No. 03-21-00258-CV, 2023 WL 4284984 (Tex. App.—Austin June 30, 2023, pet. filed).
Appellate Court Disposition	The court of appeals affirmed the trial court's judgment in part, reversed in part, and remanded the cause to the Commission. The Opielas' motion for rehearing was denied. There are no motions for rehearing or en banc reconsideration pending.

STATEMENT OF JURISDICTION

This Court has jurisdiction over this appeal from a final judgment because this Petition presents questions of law that are important to the jurisprudence of the State. Tex. Gov't Code § 22.001(a).

ISSUES PRESENTED

1. The Commission grants Production Sharing Agreement ("PSA") permits for horizontal wells that cross multiple tracts of land without requiring the operator to follow the established procedures for pooling, as long as the owners of at least 65% of the royalty interest in each tract crossed by the wellbore have signed a PSA. The court of appeals upheld the validity of the Commission's practice, on the ground that combining tracts through a PSA is not the same as pooling.

Did the court of appeals err in concluding that the Commission has the authority to issue a permit for a PSA well because production through a PSA well is not the same as pooling?

2. The Commission's rules for multi-tract horizontal wells have never been adopted pursuant to the rulemaking procedures in the Administrative Procedure Act.

Are the Commission's rules for multi-tract horizontal wells that were applied in this case invalid?

3. The Opielas' lease contains a provision that prohibits pooling "in any manner whatever."

Did the Commission err in refusing to consider this anti-pooling provision of the lease in determining whether the operator had a good-faith claim to drill a horizontal well across the Opielas' tract?

INTRODUCTION

This case presents important questions of contract and administrative law with far-reaching effects for the property rights of mineral owners.

One stick in the bundle of property rights held by a mineral owner is the right to consent (or not) to the pooling of their interests with other tracts of land. Texas law has long respected a royalty owner's right to withhold consent to the pooling of their interests with other tracts. The Legislature has authorized "forced pooling" only in the limited circumstances allowed by the Mineral Interest Pooling Act ("MIPA"). Until recently, the Commission has granted drilling permits for multi-tract wells only when the tracts are pooled.

In recent years, however, the Commission has relaxed these requirements and now routinely issues drilling permits for horizontal wells that cross multiple tracts without contractual authority to pool the tracts. The Commission has applied new ad hoc rules without following the MIPA's procedures and without adopting formal rules through the Administrative Procedure Act ("APA"). Here, the Commission applied these ad hoc rules to permit a horizontal well even though the Opielas' lease expressly prohibits pooling.

The Court should grant review to address (a) the scope of the Commission's authority to issue permits for multi-tract horizontal wells in the absence of consent and in reliance on rules adopted outside

the APA's formal rulemaking process and (b) the contractual right of operators to drill such wells.

STATEMENT OF FACTS

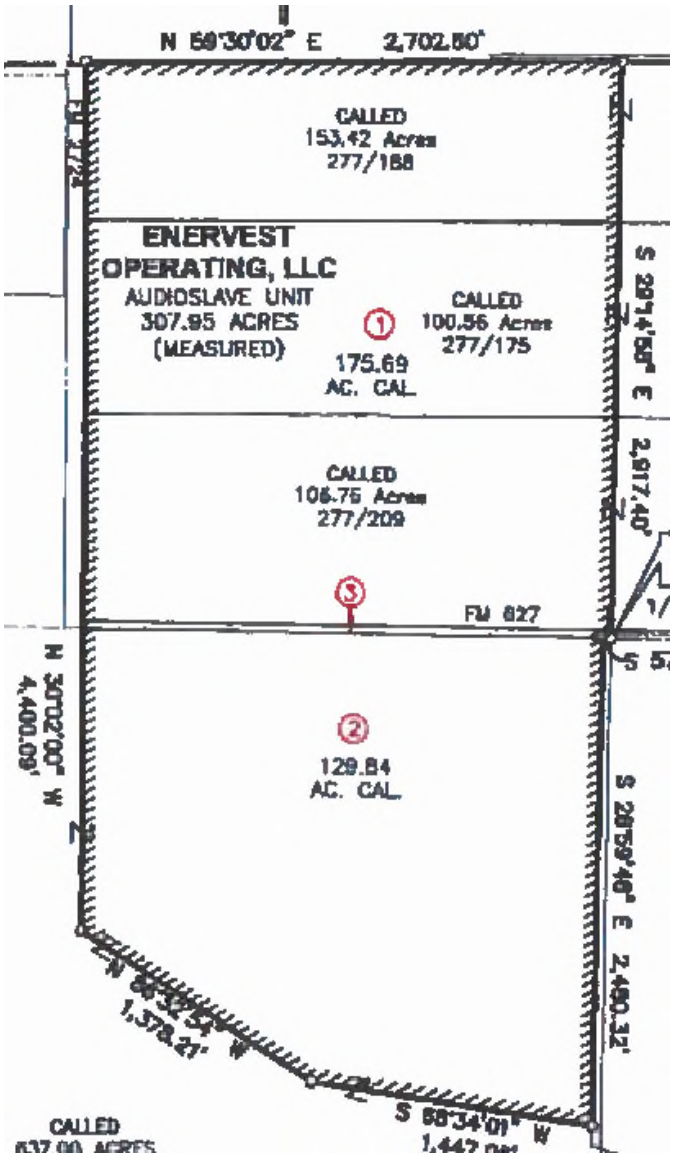
The court of appeals correctly stated the nature of the case.

The Opielas own the mineral estate in a 637-acre tract of land in Karnes County. The Opielas' mineral interest is subject to an oil and gas lease ("Lease") that includes a clause that prohibits pooling: "Nothing contained herein shall authorize the Lessee in any manner whatever to pool said land or any part of the same for oil." 4RR.569. Magnolia Oil & Gas Operating, LLC is the current operator of the Lease.

A. Proceedings before the Commission

In May 2018, Magnolia's predecessor, EnerVest Operating LLC, applied to the Railroad Commission of Texas for a well permit for the Audioslave Well A 102H Well ("Audioslave Well"). 3RR.103.

EnerVest proposed the Audioslave Well as a horizontal well traversing three separate tracts, including the tract in which the Opielas are the lessors. The following plat excerpt shows the three tracts within the proposed unit for the Audioslave Well: (1) the "Pawelek Lease"; (2) the Opiela Lease; and (3) land owned by the State under Highway FM 827, which divides the Pawelek and Opiela tracts:



3RR.513

EnerVest sought to drill the well as an "allocation well." An allocation well crosses two or more tracts of land under lease to the same operator, but the tracts are not pooled and the mineral-interest owners have not consented to the multi-tract well or reached an agreement on how to allocate production from the well for purposes of paying royalties. 2 Ernest E. Smith & Jacqueline L. Weaver, *Tex. Law*

of Oil & Gas § 9.9(B)[1] at 9-170 (2nd ed. 2023). In the absence of such an agreement, the operator "allocates" production from the well among the tracts crossed by the well according to a formula determined by the operator. *Id.* § 9.9(B)[2] at 9-172.

The Opielas filed a complaint with the Commission, contending that the proposed allocation well could not be drilled on their property without their consent, especially considering the Lease's express prohibition on pooling "in any manner whatever." 3RR.101; 4RR.569. Without ruling on the Opielas' complaint, the Commission issued the drilling permit. 5RR.102.

A few months later, Magnolia acquired the Lease from EnerVest and completed the Audioslave Well. 3RR.82. Magnolia then filed an amended application with the Commission for a permit to operate the Audioslave Well as a "Production Sharing Agreement" ("PSA") well. 3RR.806. In a PSA, the parties agree on how production will be allocated among the tracts crossed by the well. For a PSA well permit, the Commission requires the operator to show that at least 65% in interest of the mineral and royalty owners in each tract crossed by the wellbore have signed a PSA (the "65% Rule"). *App 1* at 16–17. The Opielas—who hold the executive rights under the Lease—have not signed a PSA or otherwise consented to the drilling of the Audioslave Well.

The Opielas amended their complaint, objecting to the permitting of the Audioslave Well as a PSA well. 3RR.355. After an evidentiary hearing, the Commission's Examiners issued a Proposal for Decision that recommended denial of the Opielas' complaint, concluding that Magnolia had provided a satisfactory showing of a good-faith claim to operate the Audioslave Well. *App 1*. In reaching this conclusion, the Examiners applied the Commission's 65% Rule:

- "For a PSA, the operator certifies to the Commission that at least 65% of the mineral and working interest owners from each tract have signed an agreement as to how proceeds will be divided."
- "Magnolia certified to the Commission that at least 65% of the mineral and working interest owners from each of the three tracts traversed have signed an agreement as to how proceeds will be divided."
- "The Commission has previously determined that one written oil and gas lease covering the tracts the well traverses is a reasonably satisfactory showing of a good faith claim to operate an allocation well. It follows that written agreements with 65% of the mineral interest owners of each tract is sufficient to get a permit to operate a well, in this case a PSA well."

App 1 at 16–17. The Commission adopted the Proposal for Decision and denied the Opielas' complaint. *App 2*.

B. Proceedings in the trial court

The Opielas appealed the Commission's denial of their complaint. CR.465. Following a hearing, the trial court reversed the Commission's Final Order, holding that the Commission had erred in:

1. Adopting rules for allocation and PSA wells without complying with the requirements of the APA;
2. Concluding that it had no authority to review an applicant's authority under a lease to drill a well;
3. Failing to consider the anti-pooling clause of the Opielas' lease when determining whether Magnolia had a good-faith claim to operate the Audioslave well;
4. Finding that Magnolia had shown a good-faith claim to drill and operate the Audioslave well.

App 3. The court remanded the case to the Commission for further proceedings consistent with its judgment. *App 3*.[1]

C. Proceedings on appeal

The Commission and Magnolia appealed the trial court's final judgment. A divided court of appeals reversed in part, affirmed in part, and remanded the case to the Commission. *App 4*.

The majority held that the Commission had not erred in failing to consider the Lease's anti-pooling clause in issuing a permit, reasoning that operating a PSA well is different from pooling and the

[1] The Opielas have also filed a separate lawsuit against Magnolia in Karnes County District Court, Cause No. 18-06-00153-CVK, asserting that Magnolia breached the Lease by drilling the well. 5RR.340. That case remains pending, with a motion for summary judgment filed by the Opielas under advisement.

Commission has no power to determine property rights under the Lease. *App 4* at 17. The court of appeals nevertheless held that the Commission had erred in finding Magnolia had shown a good-faith claim of right to drill the Audioslave Well because the Commission had misapplied the 65% Rule by improperly relying on "consents to pool" to reach the 65% threshold. *App 4* at 23. The court of appeals did not decide whether the Commission's 65% Rule was valid, because the two-justice majority believed that resolution of that issue was "not necessary to final disposition of the appeal." *App 4* at 20.

The dissenting justice would have held that the Commission could rely on consents to pool to satisfy the 65% Rule and also would have decided the merits of whether the rule complies with the APA. *App 5*.

SUMMARY OF THE ARGUMENT

This case asks this Court to review whether the Railroad Commission of Texas may issue permits for horizontal wells that cross multiple tracts of land when the mineral and royalty interest owners have not consented to pooling the tracts. For three reasons, this Court should reverse the court of appeals' judgment.

First, the Commission has adopted and applied an invalid rule that allows an operator to obtain a permit without pooling when only 65% of the affected mineral interest owners in each tract have signed a "Production Sharing Agreement." The Commission does not have the authority to adopt such a rule, because combining tracts for production purposes requires either valid pooling authority or compliance with the procedures of the Mineral Interest Pooling Act.

Second, the Commission's "65% Rule" is invalid because the Commission adopted it without following the formal rule-making procedures required by the Administrative Procedures Act.

Third, the Commission improperly ignored a clause in the Opielas' Lease that prohibits pooling "in any manner whatever." This clause is relevant to whether an operator has a "good faith" claim to drill a well. And the clause prohibits the drilling of the multi-tract well at issue here in the absence of the Opielas' consent. The court of appeals erred by holding otherwise.

ARGUMENT

I. The Commission's 65% Rule for permitting PSA wells is invalid.

The Commission has no formal rule authorizing permits for allocation or PSA wells. The agency instead has adopted informal policies outside the APA's formal rulemaking procedures that are "hidden in the arcana of Railroad Commission forms, rejected staff Proposals for Decision, individual well permits with disclaimers, and legislative committee proposals." 2 Smith & Weaver, *Tex. Law of Oil & Gas* § 9.9[B][1] at 9-168.

One of these informal rules is the 65% Rule, under which the Commission grants a permit for a PSA well when the operator certifies that at least 65% in interest of the mineral- and working- interest owners from all of the affected tracts have agreed on how to divide the proceeds from the well. The Commission relied on the 65% Rule in denying the Opielas' complaint. *App 1* at 17. This Court should declare the 65% Rule invalid and hold that the Commission had no authority to grant the PSA permit.

A. The evolution of the Commission's treatment of PSA and Allocation Wells.

Before PSA and allocation wells, pooling was available only through Statewide Rule 40 or the Mineral Interest Pooling Act ("MIPA"). Statewide Rule 40 is a specific, APA-compliant rule that addresses pooled units and that requires the operator to have

"appropriate contractual authority" to pool. 16 Tex. Admin. Code §3.40(a). With the MIPA, the Legislature granted the Commission limited authority to "establish a unit and pool all the interests in the unit" to drill a well without mineral and royalty owner consent. Tex. Nat. Res. Code § 102.011. With the advent of horizontal drilling—where wellbores may extend miles underground from a well's surface location—operators have sought new methods to combine tracts into a single horizontal-well drilling unit without the need to form a formal pooled unit.[2]

The Commission initially protected the rights of mineral owners, issuing permits for PSA wells only when 100% of the owners in the proposed drilling unit had signed a PSA. 3.RR.749. But in 2008 the Commission changed course by adopting rules that lowered the threshold for obtaining these permits. On the ruling of two of the three Commissioners, the Commission directed its staff "that wells that are permitted based on a production sharing agreement should be approved when the usual criteria are met and the operator certifies that at least 65% of the working and royalty interest owners in each component tract have signed the production sharing agreement."

---

[2] *See generally* Bret Wells, *Allocation Wells, Unauthorized Pooling, and the Lessor's Remedies,* 68 BAYLOR L. REV. 1, 8–9 (2016); H. Phillip Whitworth & D. Davin McGinnis, *Square Pegs, Round Holes: The Application and Evolution of Traditional Legal and Regulatory Concepts for Horizontal Wells,* 7 TEX. J. OIL GAS & ENERGY L. 177, 179–81 (2011).

App 4 at 13. Since then, the Commission has used this 65% Rule to determine whether to issue a PSA well permit despite its appearing nowhere in the Commission's APA-compliant regulations.

The Commission then went a step further and began approving permits for "allocation" wells. For an allocation well, the operator need only represent that it has a lease authorizing production from each tract crossed by the wellbore, even though it may have no consent from any of the mineral owners to combine the tracts for purposes of drilling a horizontal well or how to allocate production. Instead, the operator represents that it will "allocate" production from the horizontal well according to a formula the mineral interest owners have not agreed to.

When the Commission first encountered requests for allocation wells, it rejected them outright, concluding that issuing such permits would exceed the Commission's statutory authority and violate the terms of the relevant leases. 3.RR.234. At some point, however, the Commission reversed course and began issuing allocation well permits without adopting any formal rule through the APA.

In sum, the Commission has developed policies for issuing permits for horizontal wells without complying with the APA, without determining whether it has authority to develop such policies, and without notice to the mineral interest owners whose property rights are affected by the Commission's actions, a trend recognized by scholars in the field:

> The informal, PSA/allocation well permitting system was becoming a standard part of the Railroad Commission's decision-making, even though no fieldwide or statewide rule authorized such. This situation may have developed so quietly because royalty interest owners did not receive notice of the permit applications for PSA or allocation wells, so the permitting process was largely hidden from their view.

2 Smith & Weaver, *Tex. Law of Oil & Gas* § 9.9[B][2] at 9-175.[3]

B. The Commission does not have the authority to grant a PSA well permit.

"[A]n agency can adopt only such rules as are authorized by and consistent with its statutory authority." *R.R. Comm'n of Tex. v. Lone Star Gas Co.*, 844 S.W.2d 679, 685 (Tex. 1992) (quotation omitted). "As a statutorily created body, the Commission has no inherent authority, and instead has only the authority that the Legislature confers upon it." *Tex. Coast Utils. Coal. v. R.R. Comm'n of Tex.*, 423 S.W.3d 355, 359 (Tex. 2014). The Commission's 65% Rule is beyond its statutory authority because it allows pooling of acreage without either royalty owners' consent or compliance with the MIPA. Tex. Nat. Res. Code §§ 102.001 *et seq.*; *see* 1 Smith & Weaver, *Tex. Law of Oil & Gas* § 4.8[B][2] at 4-160 ("Absent the use of the Mineral Interest Pooling Act, a lessee has no power to pool the leased estate with other land unless the lessor is expressly authorized to do so." (footnotes omitted)).

---

[3] An excellent history of the development of PSA and allocation wells and the controversy surrounding them is in 2 *Smith & Weaver, Tex. Law of Oil & Gas* § 4.8[B] and [C].

Historically, the Commission lacked authority to establish a unit to drill a well when the owners of the affected mineral estates failed to agree to combine their interests. As this Court noted, "[t]he orders of the Railroad Commission cannot compel pooling agreements that the parties themselves do not agree upon." *Jones v. Killingsworth*, 403 S.W.2d 325, 328 (Tex. 1965). So, "[a]lthough forced pooling of smaller tracts into one drilling unit . . . would have solved the problem, neither Texas courts nor the Railroad Commission was willing to accept such a solution without express statutory authority." Ernest E. Smith, *The Texas Compulsory Pooling Act*, 43 TEX. L. REV. 1003, 1004 (1965).

With the passage of the MIPA in 1965, the Legislature granted the Commission limited authority to compel pooling in the absence of consent. The MIPA includes important protections for the rights of mineral owners that are absent from the Commission's approval of well permits under the 65% Rule. First, the MIPA requires that the Commission must determine that an operator has made "a fair and reasonable offer to pool voluntarily." Tex. Nat. Res. Code § 102.013. Second, the MIPA requires at least 30 days' notice to "all interested parties" before a hearing on the application. *Id.* § 102.016. And third, the MIPA provides any person "affected by" a forced-pooling order the right of judicial review. *Id.* § 102.111.

Here, the Commission authorized Magnolia to drill a well across multiple leaseholds without showing consent of all of the mineral

owners, without showing that Magnolia had made a fair and reasonable offer to pool the tracts, and without proof of prior notice to all affected mineral owners. The Commission may not "exercise what is effectively a new power, or a power contradictory to the statute." *Tex. Coast Utils. Coal.*, 423 S.W.3d at 359 (quoting *Pub. Util. Comm'n of Tex. v. City Pub. Serv. Bd. of San Antonio*, 53 S.W.3d 310, 315 (Tex. 2001)). Thus, the Commission lacks authority to issue Magnolia a permit to combine multiple tracts for the purpose of drilling a well in the absence of consent to pool or compliance with the MIPA.

The court of appeals below held, however, that pooling authority was not necessary to drill the Audioslave well because "[p]ooling of tracts is not expressly required by Texas statutes or regulations for horizontal drilling of a wellbore that crosses property lines," *App 4* at 14, and "production through a PSA well is not the same as pooling under Texas law." *App 4* at 15. These holdings are erroneous. There is no functional distinction between pooling and PSA/allocation wells. Historically, pooling, "as commonly used by members of the petroleum industry," has been defined as "the integration of areas and interests in order to form a drilling unit." Robert E. Hardwicke, *Oil-Well Spacing Regulations and Protection of Property Rights in Texas*, 31 TEX. L. REV. 99, 100 (1952). Allocation wells and PSA wells, like pooled units, combine multiple tracts to create a single drilling unit. Like pooled units, allocation wells and PSA wells drain minerals from a

common reservoir or geologic formation. And like pooled units, allocation wells and PSA wells allocate production from a single well among multiple properties.

In an earlier case, the Austin Court of Appeals—contrary to its holding in this case—held that an operator needed pooling authority to drill a multi-tract horizontal well. *Browning Oil Co. v. Luecke*, 38 S.W.3d 625, 647 (Tex. App.—Austin 2000, pet. denied). In the absence of pooling authority, the court held that an operator seeking to drill a multi-tract horizontal well "must seek to negotiate a solution beneficial to both the lessee and the lessor or else forego drilling." *Id.* The court of appeals below cited *Luecke* several times, but did not reconcile *Luecke*'s holding with its conclusion that pooling is not required for a multi-tract horizontal well. *See also* Bret Wells, *Allocation Wells, Unauthorized Pooling, and the Lessor's Remedies*, 68 BAYLOR L. REV. 1, 25 (2016) ("[T]he act of combining separate tracts into a multi-tract unit for the purpose of obtaining a drilling permit is by definition 'pooling' under the historic definition of that term, and this historic definition of pooling was repeated without change by the Austin appellate court in *Browning Oil Co. v. Luecke* . . . .").

The Court should take this case to resolve the conflict over whether the Commission has the authority to permit such a well in the absence of consent or compliance with the MIPA and whether combining multiple leases for a horizontal well is "pooling."

C. The 65% Rule was not adopted in compliance with the Administrative Procedures Act.

"When an agency promulgates a rule without complying with the proper rule-making procedures, the rule is invalid." *El Paso Hosp. Dist. v. Tex. Health & Human Services Comm'n*, 247 S.W.3d 709, 715 (Tex. 2008). Here, the Commission's 65% Rule falls squarely within the APA's definition of a rule, was not properly promulgated under the APA, and does not qualify for any recognized exception to the formal rulemaking requirement. The rule is therefore invalid.

The APA broadly defines "rule" to include "a state agency statement of general applicability that" either "implements, interprets, or prescribes law or policy" or describes the agency's "procedure or practice requirements." Tex. Gov't Code § 2001.003(6)(A). "By 'general applicability,' the APA definition references statements that affect the interest of the public at large such that they cannot be given the effect of law without public input." *R.R. Comm'n of Tex. v. WBD Oil & Gas Co.*, 104 S.W.3d 69, 79 (Tex. 2003). Here, the Commission's 65% Rule is a "rule" under the APA because it applies generally throughout the State and implements the Commission's policy on issuing PSA well permits.

The Commission did not properly promulgate a rule enacting the 65%-threshold requirement for PSA wells. Under the APA, "the Legislature delegates formal rulemaking power to an agency in the

expectation that an agency will ordinarily adopt rules of general application through that power." *Rodriguez v. Serv. Lloyds Ins. Co.*, 997 S.W.2d 248, 255 (Tex. 1999). The APA's procedural requirements of notice, publication, and public comment "assures the public and affected persons are heard on matters that affect them and received notice of new rules." *Id.* The Commission did not publish the 65% Rule before adoption, and it did not give the public notice or an opportunity to comment on the requirement. As the court of appeals recognized, "the Commission has not adopted Administrative Code rules specific to PSAs, though it has requested information about PSAs through its forms and has granted permits for wells that were the subject of PSAs." *App 4* at 12 (footnote omitted).

Finally, the Commission's 65% Rule does not fall within one of the narrow exceptions justifying adoption outside the APA's procedures. Ad hoc rulemaking is limited to "exceptional" circumstances "when using the rulemaking procedure would frustrate the effective accomplishment of the agency's functions . . . for example, when the agency is construing a new rule or when a dispute deals with a problem that requires ad hoc resolution because the issue cannot be captured within the bounds of a general rule." *Rodriguez*, 997 S.W.2d at 255. The 65% Rule is not subject to the ad-hoc exception: the Commission has been relying upon it for over a decade.

D. The Commission's application of the 65% Rule prejudiced the Opielas' substantial rights.

"[A]n agency decision based on an invalid rule must be reversed and remanded to the agency if substantial rights of the appellant have been prejudiced thereby." *Tex. State Bd. of Pharmacy v. Witcher*, 447 S.W.3d 520, 527 (Tex. App.—Austin 2014, pet. denied); *see also* Tex. Govt' Code § 2001.174 (review under substantial evidence rule).

Here, the Commission's order denying the Opielas' complaint prejudiced the Opielas because it relies on the 65% Rule to find that Magnolia had a good-faith claim to operate the Audioslave Well. *App. 1*. Accordingly, this Court should reverse the court of appeals' judgment, affirm the trial court's judgment that the 65% Rule is invalid, and remand this case to the Commission.

II. Magnolia did not show a "good-faith claim" to drill the PSA well.

The Opielas objected to the issuance of a permit for the Audioslave Well—both as an allocation well and as a PSA well—on the ground that their Lease expressly prohibits pooling "in any manner whatever." 4.RR.569. The Commission, however, "simply ignored the anti-pooling clause as irrelevant to the Well permit." *App 4* at 16. The court of appeals agreed that the Commission could do so for two alternative reasons: (1) the Commission did not have to consider the anti-pooling clause, because the Commission has "no

power to adjudicate the applicant's rights under a lease or other relevant title documents," *App 4* at 18, and (2) even if the Commission did consider the clause, "the anti-pooling clause was not implicated" here because a "permit for horizontal drilling under a PSA is not pooling under Texas law." *App 4* at 18. Both of these holdings merit this Court's review and warrant reversal of the court of appeals' judgment.

A. The anti-pooling clause is relevant.

In *Magnolia Petroleum Co. v. Railroad Commission of Texas*, 170 S.W.2d 189 (Tex. 1943), this Court held that the Commission must ensure that a party seeking a drilling permit has a good-faith claim to do so because the Commission "should not do the useless thing of granting a permit to one who does not claim the property in good faith." *Id.* at 191. While the Commission lacks authority to make binding determinations of property rights, *id.*, the Commission does have the authority and duty to examine property rights in the performance of its regulatory responsibilities to determine whether an applicant has a good-faith claim. *See FPL Farming Ltd. v. Env't Processing Sys., LLC*, 351 S.W.3d 306, 313 (Tex. 2011) ("Consistent with our suggestion in *Magnolia Petroleum* that the Railroad Commission has the authority and obligation to look to the parties' legal status in determining whether a permit should be issued . . . ."). Here, the Commission has a duty to reject a permit when an applicant's claim of

right to drill a horizontal well is based on an instrument that explicitly prohibits such drilling.

The Commission's APA-compliant rule recognizes that a good-faith claim for creating a pooled unit requires "appropriate contractual authority." 16 Tex. Admin. Code § 3.40(a). Such a rule is consistent with courts' directives that the Commission deny drilling permits where a pooling agreement is not valid. *Cheesman v. Amerada Petroleum Corp.*, 227 S.W.2d 829, 831 (Tex. App.—Austin 1950, no writ). Here, the Opielas did not ask the Commission to resolve a title dispute, adjudicate property rights, or determine rights to possession. *See Magnolia*, 170 S.W.2d at 99 ("When [the Commission] grants a permit to drill a well it does not undertake to adjudicate questions of title or rights of possession."). They instead asked the Commission to consider whether Magnolia had a good-faith claim of right to drill the well under the Lease. Such a determination requires the Commission to consider the contractual authority claimed by the operator. An applicant cannot have a good-faith claim to drill a PSA well when the relevant legal instrument expressly prohibits the drilling of such a well. *Magnolia* thus does not bar consideration of the anti-pooling clause in the Lease when determining whether Magnolia has a good-faith claim to drill and operate a PSA well. The court of appeals erred by holding otherwise.

B. The anti-pooling clause prohibits the PSA well.

The court of appeals' alternative holding—that the anti-pooling clause does not prohibit a PSA well—is also erroneous. Because the Lease expressly prohibits pooling "in any manner whatever," 4.RR.569, Magnolia does not, as a matter of law, have a good-faith claim to include the Opielas' tract in *any* multi-tract well—whether as part of a traditional pooling unit or a PSA or allocation well. As discussed above, Section I(B), *supra*, the PSA well is simply pooling by another name, because it effectively combines separate tracts into one unit for the purposes of drilling a single well. The Lease's language bars Magnolia's attempt to combine the Opielas' property in its multi-tract well, whether as traditional pooling or a PSA well.

The Commission's refusal to consider the Lease's anti-pooling clause prejudiced the Opielas. This Court should reverse the court of appeals' judgment and remand to the Commission with instructions that the Lease does not allow permitting of a multi-tract well.

PRAYER

The Opielas pray that this Court grant Petition for Review, reverse the court of appeals' judgment, and affirm the trial court's final judgment. The Opielas pray for such other and further relief to which they may show themselves to be justly entitled.

Respectfully submitted,

/s/William Christian
John B. McFarland
State Bar No. 13598500
William Christian
State Bar No. 00793505
Marianne W. Nitsch
State Bar No. 24098182
Mark A. Stahl
State Bar No. 24125420
GRAVES, DOUGHERTY,
HEARON & MOODY, PC
401 Congress Ave., Suite 2700
Austin, Texas 78701
(512) 480-5600
(512) 480-5804 (fax)
jmcfarland@gdhm.com
wchristian@gdhm.com
mnitsch@gdhm.com
mstahl@gdhm.com

Attorneys for Petitioners

CERTIFICATE OF COMPLIANCE

This computer-generated document complies with the type-volume limitations of Tex. R. App. P. 9.4(i)(2)(D) because it contains **4489 words**, excluding the parts exempted by Tex. R. App. P. 9.4(i)(1). In making this certificate of compliance, I am relying on the word count of the computer program used to prepare the document.

/s/William Christian

CERTIFICATE OF SERVICE

I hereby certify that on November 22, 2023, a true and correct copy of the foregoing has been served electronically through eFile.TXCourts.gov on counsel of record for the other parties to this appeal.

/s/William Christian

APPENDIX 1
RRC Proposal for Decision

RAILROAD COMMISSION OF TEXAS
HEARINGS DIVISION

PROPOSAL FOR DECISION

OIL & GAS DOCKET NO. 02-0315435

COMPLAINT OF ELSIE OPIELA AND ADRIAN OPIELA REGARDING MAGNOLIA OIL & GAS OPERATING LLC'S (521544) AUDIOSLAVE A LEASE, WELL NO. 102H, PERMIT NO. 839487, SUGARKANE (AUSTIN CHALK) FIELD, KARNES COUNTY, TEXAS

EXAMINERS: Jennifer Cook, Administrative Law Judge
Petar Buva, Technical Examiner

PROCEDURAL HISTORY:
Hearing Date - January 23, 2019
Close of Record - June 20, 2019
Proposal for Decision Issued - August 30, 2019

APPEARANCES:
For Complainants Elsie Opiela and Adrian Opiela -
John McFarland and Nicholas C. Miller
Graves Dougherty Hearon & Moody

For Respondent Magnolia Oil & Gas Operating LLC -
Mark Hanna and Stephanie Kover
Scott Douglass & McConnico

Table of Contents

I. Statement of the Case

Elsie Opiela and Adrian Opiela ("Complainants") filed a complaint ("Complaint") against Magnolia Oil & Gas Operating LLC ("Respondent" or "Magnolia") regarding Respondent's drilling permit, Permit No. 839487, authorizing Respondent to drill a horizontal well, Well No. 102H (the "Well") on its Audioslave A Lease in the Sugarkane (Austin Chalk) Field in Karnes County, Texas. Complainants are mineral interest owners of one of the three tracts traversed by the Well. Complainants claim Magnolia lacks a good faith claim to operate the Well and request that the permit for the Well be revoked.

The Well is a horizontal well that has been identified by Respondent to the Railroad Commission ("Commission" or "RRC") as a Production Sharing Agreement ("PSA") wellbore. Complainants assert the Commission does not have authority to issue drilling permits for wells in which the operator relies on PSAs for its right to operate. Complainants maintain that the underlying oil and gas lease for one of the tracts does not grant pooling authority, and as mineral interest owners they have not consented to pool or signed a PSA; thus, Magnolia does not have a good faith claim. Complainants also claim the Well does not meet the criteria established by Commission precedent for qualifying as a PSA well because Magnolia relies on various types of agreements as PSAs, such as consents to pool.

Respondent asserts that the Commission does have authority to issue drilling permits for PSA wells. Respondent maintains that for PSA wells, the Commission requires additional documentation than required for allocation wells. Respondent argues that since PSA wells require more documentation than allocation wells and the Commission has already determined the documentation—underlying written agreements for all tracts produced from—is sufficient for it to approve a drilling permit, it follows that PSAs are also sufficient. Respondent further maintains that the agreements it has do qualify as PSAs as that term is defined in Commission guidance. All are written agreements containing a method to allocate production, which is what is required in the definition of PSA in Commission forms.

The Administrative Law Judge and Technical Examiner (collectively "Examiners") respectfully submit this Proposal for Decision ("PFD") and recommend the Commission deny Complainants' request that the permit for the Well be revoked.

II. Jurisdiction and Notice[1]

Sections 81.051 and 81.052 of the Texas Natural Resources Code provide the Commission with jurisdiction over all persons owning or engaged in drilling or operating oil or gas wells in Texas, and the authority to adopt all necessary rules for governing and regulating persons and their operations under the jurisdiction of the Commission.

---

[1] The hearing transcript in this case is referred to as "Tr. at [pages]." Complainants' exhibits are referred to as "Complainants Ex. [exhibit nos.]." Respondent's exhibits are referred to as "Respondent Ex. [exhibit nos.]."

Complainants served the Complaint to Respondent on May 11, 2018.[2] On October 16, 2018, the Hearings Division of the Commission sent an Agreed Scheduling Order to Complainants and Respondent, setting a hearing date of January 23, 2019. Consequently, the parties received more than 10 days' notice. The hearing was held on January 23, 2019, as noticed. Complainants and Respondent appeared and participated at the hearing.

III. Applicable Legal Authority

Complainant alleges the Commission's current operator of record, Respondent, does not have a good faith claim to operate the Well because Respondent's contractual lease does not authorize pooling and they believe such an authorization is necessary to drill a horizontal well across multiple tracts. A good faith claim is defined in the Texas Natural Resources Code and in Commission rule as:

> A factually supported claim based on a recognized legal theory to a continuing possessory right in the mineral estate, such as evidence of a currently valid oil and gas lease or a recorded deed conveying a fee interest in the mineral estate.[3]

IV. Discussion of Evidence

Complainant provided exhibits and no witnesses. Respondent provided exhibits and one witness.

A. Background facts.

The Complaint regards Respondent's drilling permit, Permit No. 839487, authorizing Respondent to drill the Well. The Well has been identified to the Commission as based on a PSA.[4] Originally, the drilling permit application for the Well identified the well as an allocation well, and Enervest Operating, L.L.C. was identified as the operator. Thereafter the permit was amended to be identified as a PSA well with Respondent as the operator. According to Commission guidance, both allocation wells and PSA wells are horizontal wells in which the producing wellbore traverses more than one tract.[5] For an allocation well, the operator represents to the Commission that it holds leases covering each tract traversed by the wellbore.[6] For a PSA, the operator certifies to the Commission

---

[2] *See Magnolia Oil & Gas Operating LLC's Closing Brief* ("Respondent's Closing Brief") at 4-5.
[3] Tex. Nat. Res. Code § 89.002(11); 16 Tex. Admin. Code § 3.15(a)(5).
[4] *See, e.g.* Respondent Ex. 1 at 2.
[5] Examiners Ex. 1 at 7. In Respondent's closing brief, Respondent requests that official notice of *Oil & Gas Division Form P-16 Instructions and Guidelines for Drilling Permit Application (Form W-1)*, last revised February 2019, which discusses PSA and allocation wells. Respondent's Closing Brief at 7. The Examiners agreed that the document should be part of the record. On June 13, 2019, the Examiners issued a letter proposing to take official notice of the document and referring to it as Examiners Exhibit 1. The deadline for any party to object was June 28, 2019. There was no objection.
[6] *Id.*

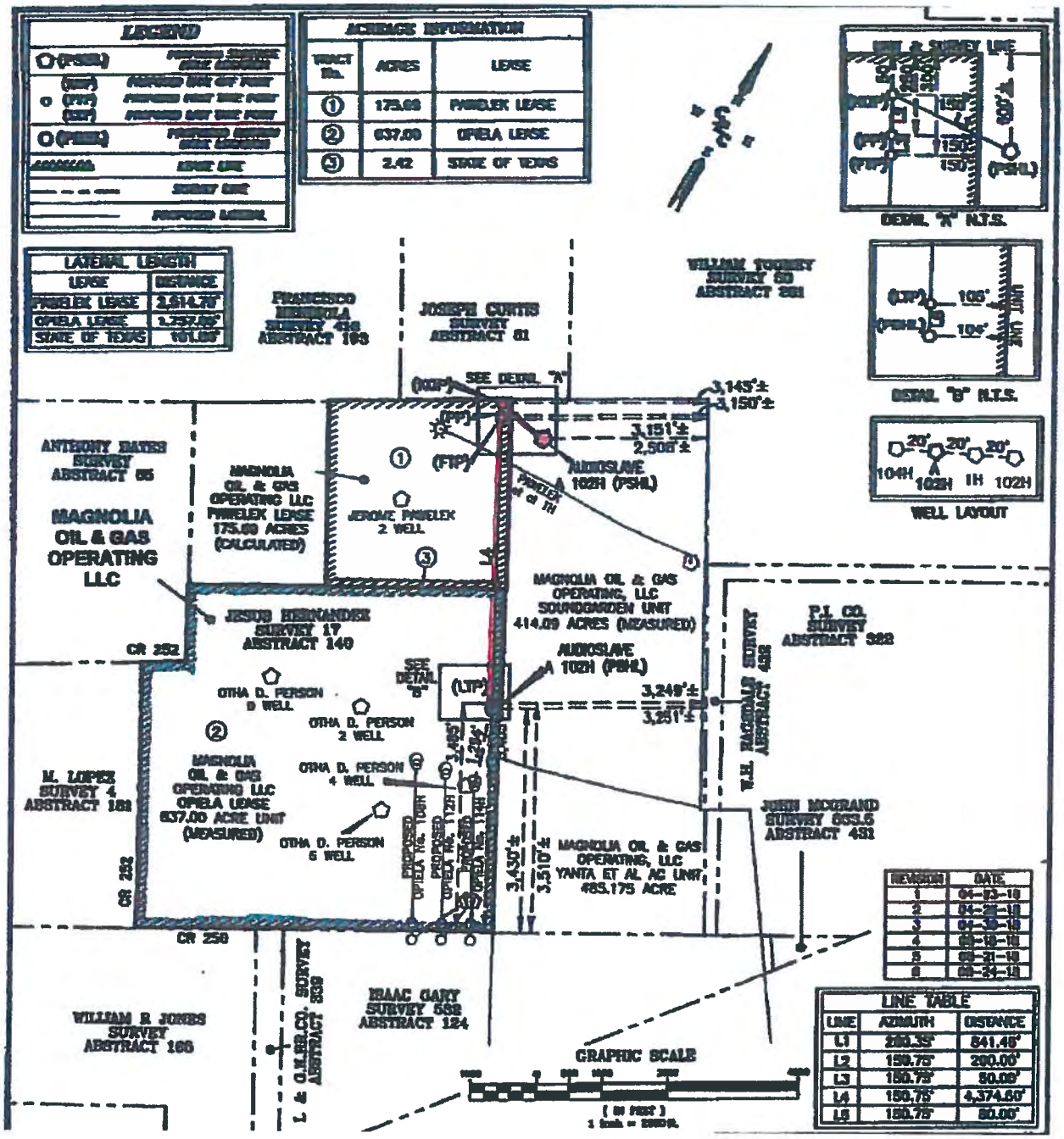
that at least 65% of the mineral and working interest owners from each tract have signed an agreement as to how proceeds will be divided.[7]

The chronology of the Well follows:

May 1, 2018:	Enervest Operating, L.L.C. files an application to drill the Well via the Commission's Form W-1, *Application for Permit to Drill, Recomplete or Re-enter* ("Form W-1"), identifying the Well as a new horizontal well. The Well was identified as an allocation well.[8]
May 3, 2018:	The Commission approves the application and issues the drilling permit for the Well.[9]
May 7, 2018:	The Well was spudded.[10]
August 29, 2018:	An amended application is filed listing Respondent as the operator. The Well is identified as a PSA well.[11]
August 30, 2018:	The amended permit for the Well listing Respondent as the operator is issued by the Commission.[12]

The Well traverses three tracts. An excerpt from the plat for the Well follows on the next page.[13]

[7] *Id.*
[8] Respondent Ex. 1 at 2, Attachment 2.
[9] Respondent Ex. 1 at 2, Attachment 3.
[10] Respondent 1 at 2.
[11] Respondent 1 at 2, Attachments 1, 2.
[12] *Id.*
[13] Respondent Ex. 1 at Attachment 2.



The Well (in red) is located near and is parallel to the eastern boundary of the tracts. The top tract labeled ① is referred to as the Pawelek Tract. Tract ② is referred to by the parties as the Person Tract. Tract ③ is a state highway that runs between the two tracts and is referred to as the Highway Tract. The first take point is in the northeast corner of the Pawelek Tract and traverses the Pawelek Tract and the Highway Tract and goes on to the Person Tract.[14]

[14] *Id.*; Tr. at 16-18.

Respondent provided a Declaration ("Declaration") of Denise Ojeda Speer ("Declarant") in support of Magnolia.[15] Declarant is a landman and an employee of Enervest as the Manager—Land, Magnolia South. Declarant reviewed documentation regarding the three tracts traversed by the Well, including title opinions and the chains of titles for the tracts, in preparing the Declaration.[16] The Declaration has underlying documentation as attachments.

Complainants are successors to a contractual lease covering the Person Tract. Complainants own the executive interest and 1/4th of the royalty interest in the Person Tract. Complainants have not signed a PSA, a consent to pool or a ratification of a pooled unit for the Well.[17] Regarding the Person Tract, 65.625% of the mineral interest owners signed either a PSA, consent to pool or ratification of unit, all setting forth a method of dividing proceeds.[18] While the mineral interest owners who signed the documents have a non-executive interest, Declarant states that deeds creating non-executive interests indicate that the holders of the non-executive interests retain and hold the right to pool.[19]

Regarding the Pawelek Tract, the underlying contractual lease provides pooling authority and contains a method of dividing proceeds. 68.993% of the mineral interest owners are either lessors or have ratified the contractual lease.[20] Regarding the Highway Tract, the General Land Office ("GLO") has signed a pooling agreement which contains a method of dividing proceeds. The GLO represents 100% of the mineral interests in the Highway Tract.[21]

B. Summary of Complainants' Evidence and Argument

Complainants assert that Commission rules do not define or mention PSA or allocation wells and consequently there is no authority for the Commission to issue PSA permits or allocation well permits.[22] Complainants claim Respondent does not have a good faith claim because they have not consented to pool or signed a PSA for the Person Tract. Complainants further assert Respondent has failed to secure the requisite percentage of PSAs from the necessary parties.[23] Complainants request that the drilling permit for the Well be revoked.

In Complainants' contractual lease, there is no authority to pool in that it has been stricken from the form lease. Complainants maintain there is no authority to pool and Complainants have not signed any PSA. Complainants assert that consequently, Respondent cannot comply with the terms of the contractual lease; it cannot pay royalites from the production of hydrocarbons from the leased premises because Respondent

---

[15] Respondent Ex. 1; Tr. at 34-35.
[16] *Id.* at 2-3.
[17] Respondent Ex. 1 at 2-3; Tr. at 18-29.
[18] Respondent Ex. 1 at 3-8, Attachments 5 at 1, 6-16.
[19] Respondent Ex. 1 at 7.
[20] Respondent Ex. 1 at 2, 8-12, Attachments 5 at 2, 17-21.
[21] Respondent Ex. 1 at 12, Attachment 22.
[22] *Closing Brief by Complainants Elsie Opiela and Adrian Opiela, Jr.* at 2 (filed February 21, 2019) ("Complainants Closing Brief");
[23] *Id.*; Tr. at 35-37.

cannot measure what portion comes from the leased premises and instead must estimate production.[24]

Complainants argue that allocation wells violate Statewide Rule 26. Complainants argue that Statewide Rule 26 requires all liquid hydrocarbons to be measured before leaving the lease. Complainants maintain that an allocation well violates Statewide Rule 26 because the hydrocarbons come from more than one lease and are not measured before leaving each lease because there is only one wellhead.[25]

Complainants also claim allocation wells violate Statewide Rule 40.[26] Statewide Rule 40 contains requirements regarding pooling.[27] Complainants maintain that operators who want to combine acreage from separate leases to form a drilling unit are required to create a pooled unit.[28]

Complainants assert that even if the Commission does have the authority to approve permits for PSA wells, Respondent has not met the Commission's requirements for qualifying for a PSA well. Complainants maintain that the PSAs Respondent relies on include pooling consents and unit ratifications which do not qualify as PSAs.

Complainants maintain that the mineral interest owners of the Person Tract, the same tract for which Complainants are mineral interest owners, who signed agreements with Respondent are non-participating royalty owners who do not have authority to authorize Respondent to pool or to sign PSAs.[29]

C. Summary of Respondent's Evidence and Argument

Respondent's only witness was expert witness, James Clark. Mr. Clark is a consulting petroleum engineer with almost 30 years of industry experience. He has testified before the Commission in the past.[30]

Mr. Clark testified that Commission practice is to issue permits for allocation wells and PSA wells. For an allocation well, the Commission requires the applicant to have a contractual agreement, such as a lease, for each tract that the proposed well traverses. For a PSA well, the Commission requires that each tract that the well traverses have at least 65% of the mineral and working interest owners who have signed an agreement. When amending the permit for the Well, Respondent represented that 100% of the working and mineral interest owners had signed an agreement for the Pawelek Tract and the Highway Tract. It represented that 100% of the working interest owners and 65.62% of the mineral interest owners for the Person Tract had signed agreements. Mr. Clark asserts that Respondent could have applied for an allocation well because it has

---

[24] Complainants Closing Brief at 8, Exhibit P.
[25] Tr. at 75-79; Complainants Ex. 19-20; Complainants Closing Brief at 13-15; *see also* 16 Tex. Admin. Code § 3.26(a)(2).
[26] Complainants Closing Brief at 13-14.
[27] 16 Tex. Admin. Code § 3.40.
[28] Complainants Closing Brief at 13.
[29] Complainants Closing Brief at 17-18.
[30] Tr. at 41-42; Respondent Ex. 2.

contractual agreements covering all three tracts. Respondent chose to file as a PSA well because it does meet the 65% threshold. Mr. Clark testified that allocation wells do not require the additional information required when designating a well as a PSA well.[31]

Mr. Clark researched Commission records and provided information about how many allocation wells and PSA wells the Commission approved in 2017 and 2018. The information is summarized in the table below:[32]

	Allocation wells in 2017	**PSA wells in 2017**	**Allocation wells in 2018**	**PSA wells in 2018**
New permit applications approved	1647	285	2688	327
Total permit applications approved (new and amendments)	2130	381	3577	456

Mr. Clark opined that in his experience, the Well meets the standards required by the Commission to qualify as a PSA well. All the PSAs relied on by Respondent are agreements in writing that contain a method of allocating production. Respondent relies on various types of documents, such as consents to pool, that also contain a method of allocating production. Mr. Clark testified he is not aware of any form PSA that the Commission requires and that the applicant provides a representation that it has PSA agreements and does not provide the underlying documentation; the Commission generally does not see the actual PSAs.[33]

Regarding the mineral interest owners of the Person Tract who have signed written agreements with Respondent, Respondent maintains that they did retain the right to pool. Respondent maintains that their mineral interests were "carved out" of the mineral estate and the right to pool was part of the rights carved out.[34]

V. Examiners' Analysis

The Examiners recommend the Commission deny the motion to dismiss that Applicant filed while this case was pending. The Examiners recommend the Commission find that Respondent provided a reasonably satisfactory showing of a good faith claim to operate the Well, and deny Complainants' request that the permit for the Well be revoked.

---

[31] Tr. at 47-63, 110-111; Respondent Ex. 4; Examiner Ex. 1 at 4; *See also* Respondent Ex. 5-8.
[32] Tr. at 63-64; Respondent Ex. 9.
[33] Tr. at 69-71; 82-85.
[34] *Magnolia Oil & Gas Operating, LLC's Closing Brief* at 15-16; Respondent Ex. 1 at Attachments 8, 9.

A. The Examiners recommend denial of Respondent's motion to dismiss because it is based on the *Klotzman* case, which involved an allocation well, not a PSA.

While this case was pending, Magnolia filed a motion to dismiss claiming the Commission has already rejected Complainants' arguments in the *Klotzman* case ("*Klotzman*")[35] and the *Monroe* case ("*Monroe*")[36]. Both are resulted in Commission final orders. The issues in *Klotzman* and *Monroe* are whether the Commission can issue permits for allocation wells and whether having contractual leases for all tracts to be traversed by the allocation well is sufficient for a good faith claim. In those cases, the Commission concluded that it does have authority and obtaining contractual oil and gas leases for each tract traversed is sufficient to show a good faith claim.

In this case, the issues regard a PSA well, and not an allocation well. Neither *Klotzman* nor *Monroe* address PSA wells. Additionally, one issue in this case is whether the PSAs relied upon by Magnolia are sufficient for the Commission to approve a drilling permit for the Well. The Examiners recommend the Commission deny the motion to dismiss.

B. Consistent with past Commission practice, the Examiners recommend the Commission find it has authority to grant drilling permits for wells on tracts covered by PSAs.

The Examiners find Complainants' assertion that Commission rules do not authorize the Commission to approve permits for wells covered by a PSA uncompelling. The Commission has already determined that it has authority to issue drilling permits for allocation wells. On September 24, 2013, the Commission entered a final order in *Klotzman* concluding that an operator with an oil and gas lease had a sufficient good faith claim to drill an allocation well. The Commission rejected the argument that an applicant must show it has pooling authority to establish it has a good faith claim to drill an allocation well.

On December 18, 2017, the Commission, through the Hearings Division, entered an order in *Monroe*, dismissing the complaint as unnecessarily duplicative. In *Monroe*, the complainants were mineral interest owners requesting a drilling permit for an allocation well be revoked, alleging the operator did not have authority to drill an allocation well and the Commission does not have authority to approve a permit for an allocation well. In *Monroe,* the Commission found that *Monroe* involved the same issue that was decided in *Klotzman* because in *Klotzman*, the Commission concluded that it did have authority to issue permits for allocation wells and a contractual oil and gas lease covering

---

[35] Tex. R.R. Comm'n, *Application of EOG Resources, Inc. for its Klotzman Lease (Allocation), Well No. 1H,(Status No. 744730), Eagleville (Eagleford-2) Field, Dewitt County, as an Allocation Well Drilled on Acreage Assigned from Two Leases*, Oil and Gas Docket No. 02-0278952 (Final Order issued Sept. 24, 2013).

[36] Tex. R.R. Comm'n, *Complaint of Monroe Properties, Inc., et al. that Devon Energy Production CO, L.P. Does Not Have a Good Faith Claim to Operate the N I Helped 120 (Alloc) Lease, Well No. 6H, Phantom (Wolfcamp) Field, Ward County, Texas*, Oil and Gas Docket No. 08-0305330 (Order of Dismissal issued Dec. 18, 2017) and (order denying motion for rehearing issued Feb. 13, 2018).

all tracts to be traversed by the subject well is a sufficient showing of a good faith claim to operate.

In this case, there is no dispute that Magnolia has written agreements covering all tracts to be traversed by the Well. In addition, Magnolia has written agreements with over 65% of the mineral interest owners in each tract, giving it the right to operate this Well. For the same reasons found in *Klotzman* and *Monroe*, the Examiners find Complainants' claim that the Commission does not have authority to issue permits for PSA wells uncompelling. According to section 81.051 of the Texas Natural Resources Code:

> The [C]ommission has jurisdiction over all . . . oil and gas wells in Texas . . . and . . . persons owning or engaged in drilling or operating oil or gas wells in Texas.[37]

Complainants offer no precedent that the Commission does not have jurisdiction to regulate PSA wells. Since according to the Natural Resources Code, the Commission has jurisdiction over "all" oil wells, it is reasonable to conclude the Commission has jurisdiction to regulate PSA wells. It appears that Complainants do not dispute jurisdiction but instead claim that since there is no Commission rule addressing PSA wells, there is no authority for the Commission to issue permits for PSA wells.

Commission rules require a permit to drill "any oil well."[38] The Commission has adopted rules providing a process for obtaining drilling permits for wells. The standard for determining whether the operator can get a permit is whether the operator has a "good faith claim" to operate. This is in Commission rule and has been acknowledged by the Texas Supreme Court.[39]

The Examiners are not persuaded that the Commission has to adopt a rule to expressly address each type of documentation or contractual arrangement that can be utilized to show a good faith claim to operate a well. The Texas Supreme Court has already provided a standard for such demonstration. According to the Court—consistent with Commission rules—the standard for an operator to demonstrate a right to operate sufficient to obtain a permit is: "a reasonably satisfactory showing of a good faith claim" to operate the well.[40] The Commission is not required to adopt rules specifying what qualifies as a good faith claim.

Complainants claim PSA wells, as well as allocation wells, violate Statewide Rules 26 and 40. In *Klotzman* and *Monroe*, the Commission did not find these arguments persuasive, and the Examiners are not persuaded in this case. Complainant acknowledges, "Since the Klotzman case, no court has addressed the legality of PSA or allocation wells."[41] Complainant further acknowledges "significant disagreement exists

---

[37] Tex. Nat. Res. Code § 81.051(a)(2), (a)(4); *see also, e.g.,* Tex. Nat. Res. Code ch. 85.
[38] *See, e.g.,* 16 Tex. Admin. Code § 3.5(a).
[39] *See, e.g., Magnolia Petroleum Co. v. R.R. Comm'n of Tex.*, 170 S.W.2d 189, 191 (Tex. 1943); 16 Tex. Admin. Code § 3.15(a)(5); *see also Trapp v. Shell Oil Co.*, 198 S.W.2d 424, 437-38 (Tex. 1946).
[40] [cite]
[41] Complainants Closing Brief at 5.

among the legal community as to the legality of allocation wells."[42] The Commission's authorization of PSA wells has been in consonance with Commission rules as indicated by the history of approval of both allocation and PSA wells.[43]

Complainants' reliance on *Browning Oil Co. v. Luecke*,[44] ("*Browning* case") is misplaced. The *Browning* case was decided prior to the *Klotzman* case and considered in the *Klotzman* case. The *Browning* case does not establish that pooling authority is required for authority to drill an allocation well. For example, Ernest Smith, Professor of Law at the University of Texas School of Law and co-author of the *Texas Law of Oil & Gas* treatise, has written an article on this issue and concludes that pooling authority is not required to drill an allocation well.[45] Regarding the *Browning* case, he states:

> *Browning* does not hold that, where a lease is silent on pooling, a lessee is required to obtain pooling authority before the lessee can drill a horizontal well that crosses lease lines. And the result that Browning dictates—i.e. that each lessor whose tract is traversed by the horizontal well should be paid the royalties due under his or her lease—is exactly the result that should obtain for the horizontal allocation well.[46]

For these reasons, the Examiners recommend the Commission find it does have authority to issue permits for PSA wells in addition to allocation wells.

C. The Examiners recommend the Commission find Respondent has provided a reasonably satisfactory showing of a good faith claim and deny Complainants' request for relief.

The Examiners recommend Complainants' request for relief be denied. The Examiners recommend the Commission find there was a reasonably satisfactory showing of a good faith claim to operate the Well and the permit for the Well should not be revoked.

Complainants allege Respondent does not have a good faith claim to operate the Well. A good faith claim is defined in Commission rule as:

> A factually supported claim based on a recognized legal theory to a continuing possessory right in the mineral estate, such as evidence of a currently valid oil and gas lease or a recorded deed conveying a fee interest in the mineral estate.[47]

---

[42] *Id.*
[43] *See, e.g.,* Respondent Ex. 9.
[44] 38 S.W.3d 625 (Tex. App.—Austin 2000, pet. denied).
[45] Ernest E. Smith, *Applying Familiar Concepts to New Technology: Under the Traditional Oil and gas Lease, A Lessee Does Not Need Pooling Authority to Drill a Horizontal Well that Crosses Lease Lines,* TEX. J. OF OIL, GAS, AND ENERGY LAW Vol. 12:1 (2017).
[46] *Id.* at 10.
[47] 16 Tex. Admin. Code § 3.15(a)(5).

The origin of the "good-faith claim" requirement comes from the Texas Supreme Court in *Magnolia Petroleum Co. v. Railroad Commission of Texas.*[48] In discussing the Commission's authority to grant a drilling permit, the Court stated:

> The function of the Railroad Commission in this connection is to administer the conservation laws. When it grants a permit to drill a well it does not undertake to adjudicate questions of title or rights of possession. These questions must be settled in the courts.[49]

The Court went on to state:

> Of course, the Railroad Commission should not do the useless thing of granting a permit to one who does not claim the property in good faith. The Commission should deny the permit if it does not reasonably appear to it that the applicant has a good-faith claim in the property. If the applicant makes a reasonably satisfactory showing of a good-faith claim of ownership in the property, the mere fact that another in good faith disputes his title is not alone sufficient to defeat his right to the permit; neither is it ground for suspending the permit or abating the statutory appeal pending settlement of the title controversy.[50]

The Commission does not adjudicate questions of title or right to possession, which are questions for the court system.[51] A showing of a good faith claim does not require an applicant to prove title or a right of possession. It is sufficient for an applicant to make a reasonably satisfactory showing of a good faith claim.[52]

PSAs are what Respondent relies on for a good faith claim. Complainants claim they, as mineral interest owners of the Person Tract, have not consented to pooling and have not signed a PSA such that Magnolia lacks the authority necessary to operate the Well. Complainants also assert that Magnolia's PSAs are insufficient because Magnolia relies on various types of written agreements as PSAs, including consents to pool. Complainants provide no legal authority for what qualifies as a PSA. Complainants acknowledge that there is no legal precedent regarding what authorization is required for allocation wells or PSA wells and that legal minds differ. While Complainants' claims may rise to a bona fide lease dispute, such will not defeat a good faith claim.

The Commission has previously determined that one written oil and gas lease covering the tracts the well traverses is a reasonably satisfactory showing of a good faith

---

[48] *Id.; see Magnolia Petroleum Co. v. R.R. Comm'n of Tex.*, 170 S.W.2d 189, 191 (Tex. 1943); *see also Trapp v. Shell Oil Co.*, 198 S.W.2d 424, 437-38 (Tex. 1946); Rosenthal v. R.R. Comm'n of Tex., 2009 WL 2567941, *3 (Tex. App.—Austin 2009, pet. denied); *Pan Am. Petroleum Corp. v. R.R. Comm'n of Tex.*, 318 S.W.2d 17 (Tex. Civ. App.—Austin 1958, no writ).

[49] *Magnolia Petroleum Co. v. R.R. Comm'n of Tex.*, 170 S.W.2d 189, 191 (Tex. 1943).

[50] *Id.* at 191 (emphasis added).

[51] *Id.; see also Trapp v. Shell Oil Co.*, 198 S.W.2d 424, 437-38 (Tex. 1946); Rosenthal v. R.R. Comm'n of Tex., 2009 WL 2567941, *3 (Tex. App.—Austin 2009, pet. denied) (mem. op.); 56 Tex. Jur. 3d Oil and Gas § 737, Adjudication of title to property and contract rights.

[52] *Id.*

claim to operate an allocation well.[53] It follows that written agreements with 65% of the mineral interest owners of each tract is sufficient to get a permit to operate a well, in this case a PSA well.

Complainants claim even if PSAs were enough to show a good faith claim, some of Magnolia's PSAs do not qualify as PSAs, such as consents to pool. According to the instructions for Form P-16 *Acreage Designation,* which is a form filed when applying for a drilling permit, the term PSA is defined as follows:

> **PSA (PRODUCTION SHARING AGREEMENT WELLBORE):** For purposes of this document, a horizontal wellbore crossing two or more tracts/leases and for which the operator certifies that at least 65% of the MINERAL and WORKING interest owners from each tract within the developmental unit have signed an agreement as to how proceeds will be divided. The wellbore need not be perforated within each tract of the developmental unit.[54]

The pertinent language in the definition defines a PSA as a written agreement containing "agreement as to how proceeds will be divided." Complainants do not argue that any of the documents relied on by Respondent fail to contain an agreement as to how proceeds will be divided. Instead, Complainants argue that the definition should be narrowly construed to preclude certain types of documents, such as consents to pool. Yet, Complainants offer no legal authority for such construction.

It is sufficient for an applicant to make a reasonably satisfactory showing of a good faith claim, and another's good faith dispute of title or possessory interest will not defeat the good faith claim.[55] While Complainants may have established there is a bona fide lease dispute as to whether Magnolia has a right to operate, that is insufficient to defeat Magnolia's good faith claim. The Examiners recommend the Commission deny Complainants' request that the permit for the Well be revoked.

VI. Recommendation, Proposed Findings of Fact and Proposed Conclusions of Law

Based on the record and evidence presented, the Examiners recommend the Commission find Respondent provided a reasonably satisfactory showing of a good faith

---

[53] Tex. R.R. Comm'n, *Complaint of Monroe Properties, Inc., et al. that Devon Energy Production CO, L.P. Does Not Have a Good Faith Claim to Operate the N I Helped 120 (Alloc) Lease, Well No. 6H, Phantom (Wolfcamp) Field, Ward County, Texas*, Oil and Gas Docket No. 08-0305330 (Order of Dismissal issued Dec. 18, 2017) and (order denying motion for rehearing issued Feb. 13, 2018) ("*Monroe*"); Tex. R.R. Comm'n, *Application of EOG Resources, Inc. for its Klotzman Lease (Allocation), Well No. 1H,(Status No. 744730), Eagleville (Eagleford-2) Field, Dewitt County, as an Allocation Well Drilled on Acreage Assigned from Two Leases*, Oil and Gas Docket No. 02-0278952 (Final Order issued Sept. 24, 2013) ("*Klotzman*").

[54] Examiners Ex. 1 at 7.

[55] *Magnolia Petroleum Co. v. R.R. Comm'n*, 170 S.W.2d 189, 191 (Tex. 1943); *see also Trapp v. Shell Oil Co.*, 198 S.W.2d 424, 437-38 (Tex. 1946); Rosenthal v. R.R. Comm'n of Tex., 2009 WL 2567941, *3 (Tex. App.—Austin 2009, pet. denied) (mem. op.); 56 Tex. Jur. 3d Oil and Gas § 737, Adjudication of title to property and contract rights.

claim to operate the Well, deny Complainants' request to have Magnolia's permit revoked, and adopt the following findings of fact and conclusions of law.

Findings of Fact

1. Elsie Opiela and Adrian Opiela ("Complainants") filed a complaint ("Complaint") against Magnolia Oil & Gas Operating LLC ("Respondent" or "Magnolia") regarding Respondent's drilling permit, Permit No. 839487, authorizing Respondent to drill a horizontal well, Well No. 102H (the "Well"), on its Audioslave A Lease in the Sugarkane (Austin Chalk) Field in Karnes County, Texas. Complainants request that the permit for the Well be revoked.

2. Complainants served the Complaint to Respondent on May 11, 2018. On October 16, 2018, the Hearings Division of the Commission sent an Agreed Scheduling Order to Complainants and Respondent, setting a hearing date of January 23, 2019. Consequently, the parties received more than 10 days' notice. The hearing was held on January 23, 2019, as noticed. Complainants and Respondent appeared and participated at the hearing.

3. Magnolia is the current record operator of the Well, and Magnolia has classified the Well as a Production Sharing Agreement ("PSA") wellbore on Commission forms.

    a. On May 1, 2018, Enervest Operating, L.L.C. files an application to drill the Well via the Commission's Form W-1, *Application for Permit to Drill, Recomplete or Re-enter* ("Form W-1"), identifying the Well as a new horizontal well. The Well was identified as an allocation well.

    b. On May 3, 2018, the Commission approved the application and issued the drilling permit for the Well.

    c. On May 7, 2018, The Well was spudded.

    d. On August 29, 2018, an amended application was filed listing Respondent as the operator. The Well was identified as a PSA well.

    e. On August 30, 2018, the amended permit for the Well listing Respondent as the operator was issued by the Commission.

4. The Well traverses three tracts referred to as the Pawelek Tract, the Person Tract and the Highway Tract, which is a state highway that runs between the other two tracts. The first take point is in the northeast corner of the Pawelek Tract and traverses the Pawelek Tract and the Highway Tract and goes on to the Person Tract. Respondent has written agreements covering all three tracts.

5. Complainants are successors to a contractual lease covering the Person Tract. Complainants have not signed a PSA, a consent to pool or a ratification of a pooled unit for the Well.

6. Magnolia designated the Well as a PSA well on Commission forms.

7. For a PSA, the operator certifies to the Commission that at least 65% of the mineral and working interest owners from each tract have signed an agreement as to how proceeds will be divided.

8. Regarding the Person Tract, 65.625% of the mineral interest owners signed either a PSA, consent to pool or ratification of unit, all setting forth a method of dividing proceeds.

9. Regarding the Pawelek Tract, the underlying contractual lease provides pooling authority and contains a method of dividing proceeds. 68.993% of the mineral interest owners are either lessors or have ratified the contractual lease.

10. Regarding the Highway Tract, the General Land Office ("GLO") has signed a pooling agreement which contains a method of dividing proceeds. The GLO represents 100% of the mineral interests in the Highway Tract.

11. Magnolia certified to the Commission that at least 65% of the mineral and working interest owners from each of the three tracts traversed have signed an agreement as to how proceeds will be divided.

12. According to the instructions for Form P-16 *Acreage Designation,* which is a form filed when applying for a drilling permit, the term PSA is defined as follows:

> **PSA (PRODUCTION SHARING AGREEMENT WELLBORE):** For purposes of this document, a horizontal wellbore crossing two or more tracts/leases and for which the operator certifies that at least 65% of the MINERAL and WORKING interest owners from each tract within the developmental unit have signed an agreement as to how proceeds will be divided. The wellbore need not be perforated within each tract of the developmental unit.

13. All of the written agreements relied on by Magnolia as PSAs contain an agreement as to how proceeds will be divided.

14. Magnolia has PSAs with at least 65% of all mineral interest owners and working interest owners for each of the tracts traversed by the Well.

15. The Commission has previously determined that written oil and gas leases covering the tracts the well traverses are a reasonably satisfactory showing of a good faith claim to operate an allocation well. It follows that written agreements

with 65% of all mineral interest owners and all working interest owners for each tract the well produces from is sufficient to get a permit to operate a well, in this case a PSA well.

16. Magnolia has a good faith claim to operate the Well.

17. Complainants claim that their contractual lease covering the Person Tract does not contain pooling authority and Complainants have not signed a PSA such that Magnolia does not have a right to drill the Well. Complainant also claims that some of the documents relied on by Magnolia are not PSAs and some of the mineral interest owners of the Person Tract who did sign agreements did not have authority.

18. While Complainants may have a bona fide lease dispute as to whether Magnolia has a right to operate, that is insufficient to defeat Magnolia's good faith claim.

19. While the Complainants may have a bona fide lease dispute with Magnolia, the determination of whether there has been a breach and the appropriate remedy is outside the jurisdiction of the Commission.

Conclusions of Law

1. Proper notice of hearing was timely issued to persons entitled to notice. *See, e.g.,* Tex. Gov't Code §§ 2001.051, 052; 16 Tex. Admin. Code §§ 1.42, 1.45.

2. The Commission has jurisdiction in this case. *See, e.g.,* Tex. Nat. Res. Code § 81.051.

3. Respondent provided a reasonably satisfactory showing of a good faith claim to operate the Well. 16 Tex. Admin. Code § 3.15(a)(5).

4. Complainants' request that the Commission revoke Respondent's permit for the Well should be denied.

Recommendations

The Examiners recommend the Commission find Respondent provided a reasonably satisfactory showing of a good faith claim to operate the Well, and deny Complainants' request that the permit for the Well be revoked.

Respectfully,

Jennifer Cook
Administrative Law Judge

Petar Buva
Technical Examiner

APPENDIX 2
RRC Final Order

RAILROAD COMMISSION OF TEXAS
HEARINGS DIVISION

OIL & GAS DOCKET NO. 02-0315435

COMPLAINT OF ELSIE OPIELA AND ADRIAN OPIELA REGARDING MAGNOLIA OIL & GAS OPERATING LLC'S (521544) AUDIOSLAVE A LEASE, WELL NO. 102H, PERMIT NO. 839487, SUGARKANE (AUSTIN CHALK) FIELD, KARNES COUNTY, TEXAS

FINAL ORDER

The Commission finds that after statutory notice in the above-docketed case, heard on January 23, 2019, the presiding Administrative Law Judge and Technical Examiner have made and filed a Proposal for Decision containing findings of fact and conclusions of law, which was served on all parties of record, and that this proceeding was duly submitted to the Railroad Commission of Texas at a conference held in its offices in Austin, Texas.

The Commission, after review and due consideration of the Proposal for Decision and the findings of fact and conclusions of law contained therein, and any exceptions and replies thereto, hereby adopts as its own the findings of fact and conclusions of law contained therein, and incorporates those findings of fact and conclusions of law as if fully set out and separately stated herein.

IT IS ORDERED that Elsie Opiela and Adrian Opiela's complaint requesting the Commission find that Magnolia Oil & Gas Operating LLC does not have a good faith claim to operate the Audioslave A Lease, Well No. 102H, Permit No. 839487 is **DENIED**.

It is further **ORDERED** by the Commission that this order shall not be final and effective until 25 days after the Commission's Order is signed, unless the time for filing a motion for rehearing has been extended under Tex. Gov't Code § 2001.142, by agreement under Tex. Gov't Code § 2001.147, or by written Commission Order issued pursuant to Tex. Gov't Code § 2001.146(e). If a timely motion for rehearing of an application is filed by any party at interest, this order shall not become final and effective until such motion is overruled, or if such motion is granted, this order shall be subject to further action by the Commission. Pursuant to Tex. Gov't Code § 2001.146(e) and 16 Tex. Admin. Code § 1.128(e), the time allotted for Commission action on a motion for rehearing in this case prior to its being overruled by operation of law is hereby extended until 100 days from the date the Commission Order is signed.

Each exception to the Proposal for Decision not expressly granted herein is overruled. All requested findings of fact and conclusions of law which are not expressly adopted herein are denied. All pending motions and requests for relief not previously granted or granted herein are denied.

Signed on October 1, 2019.

RAILROAD COMMISSION OF TEXAS

CHAIRMAN WAYNE CHRISTIAN

Christi Craddick

COMMISSIONER CHRISTI CRADDICK

COMMISSIONER RYAN SITTON

ATTEST

Deputy

SECRETARY

APPENDIX 3
Trial Court Final Judgment

No. D-1-GN-20-000099

ELSIE OPIELA AND ADRIAN OPIELA, JR.,	§	IN THE DISTRICT COURT OF
Plaintiffs,	§	
v.	§	TRAVIS COUNTY, TEXAS
RAILROAD COMMISSION OF TEXAS,	§	
Defendant,	§	
MAGNOLIA OIL & GAS OPERATING LLC,	§	
Intervenor.	§	53RD JUDICIAL DISTRICT

FINAL JUDGMENT

On April 13, 2021, this suit for judicial review of the Railroad Commission of Texas's (the "Commission") Final Order in Oil & Gas Docket No. 02-315435, *Complaint of Elsie Opiela and Adrian Opiela Regarding Magnolia Oil & Gas Operating LLC's (521544) Audioslave A Lease, Well No. 102H, Permit No. 839487, Sugarcane (Austin Chalk) Field, Karnes County, Texas*, was heard. Plaintiffs Elsie Opiela and Adrian Opiela, Jr., Defendant Railroad Commission of Texas, and Intervenor Magnolia Oil & Gas Operating LLC ("Magnolia") appeared through counsel. The Court admitted the administrative record into evidence.

The Court, having considered the pleadings, the briefs, and the administrative record, and having heard the arguments of counsel for the parties, is of the opinion that the Commission's Final Order signed on October 1, 2019, which is the subject of this cause, should be and is hereby REVERSED AND REMANDED.

IT IS THEREFORE ORDERED, ADJUDGED, AND DECREED THAT:

1. The Commission erred in adopting rules for allocation and Production Sharing Agreement ("PSA") well permits without complying with the requirements of the Administrative Procedure Act, Tex. Gov't Code § 2001.001 et seq., and further erred in applying those rules by issuing well permits for the Audioslave A 102H Well (the "Audioslave Well").
2. The Commission erred in concluding it has no authority to review whether an applicant seeking a well permit has authority under a lease or other relevant title documents to drill the well.
3. The Commission erred in failing to consider the pooling clause of the lease covered by the Audioslave Well in deciding that Magnolia has a good faith claim to operate the well.
4. The Commission erred in finding that Magnolia showed a good faith claim of right to drill the Audioslave Well.
5. The Court remands this matter to the Commission for further proceedings consistent with this judgment.

IT IS FURTHER ORDERED that costs are to be borne by the party that incurred the cost. This is a final judgment disposing of all claims and parties and is appealable.

SIGNED this 12th day of May, 2021.

JUDGE KARIN CRUMP
250TH DISTRICT COURT

APPENDIX 4
Court of Appeals Opinion

TEXAS COURT OF APPEALS, THIRD DISTRICT, AT AUSTIN

NO. 03-21-00258-CV

Railroad Commission of Texas and Magnolia Oil & Gas Operating LLC, Appellants

v.

Elsie Opiela and Adrian Opiela, Jr., Appellees

FROM THE 53RD DISTRICT COURT OF TRAVIS COUNTY
NO. D-1-GN-20-000099, THE HONORABLE KARIN CRUMP, JUDGE PRESIDING

O P I N I O N

This appeal arises from the complaint by Elsie Opiela and Adrian Opiela, Jr., (Opielas) about a permit issued by the Railroad Commission of Texas to Magnolia Oil & Gas Operating LLC (collectively, Appellants) to drill a horizontal oil well from one parcel of land, through another, and into land with minerals leased in part from the Opielas. The dispute centers on the laws, regulations, and judicial and Commission decisions concerning pooling of tracts of land for purposes of oil production along with production-sharing agreements (PSAs) and allocation wells—methods of designating how to share production. The Opielas' lease prohibits pooling "in any manner whatever" for oil production, and the Opielas did not sign a consent to pool or a PSA. Nevertheless, after a previous operator obtained an allocation-well permit, Magnolia obtained an amended permit to drill a PSA well upon the Commission's finding that Magnolia had made a good-faith showing that it had the right to drill and operate a horizontal well in the minerals owned by the Opielas because at least 65% of their fellow interest holders

had assented to share the production in some way. The Commission denied the Opielas' complaint that Magnolia lacked a good-faith claim to operate the Audioslave A 102H Well (the Well).

The trial court reversed the Commission's order and remanded this cause to the Commission, concluding that the Commission erred in finding that Magnolia showed a good-faith claim of right to drill the Well. The trial court also concluded that the Commission erred in adopting and applying rules for PSA well permits, deciding that the Commission lacked the authority to review whether an applicant seeking a well permit has right under a lease or other relevant title documents to drill the Well, and failing to consider the pooling clause in the Opielas' lease.

Appellants contend on appeal that existing rules adopted through formal notice-and-comment rulemaking provide an adequate framework for the Commission to issue well permits for unpooled multi-tract horizontal wells. The Commission contends that substantial evidence supported its conclusion that Magnolia was entitled to a drilling permit. Magnolia contends that the trial court erred by holding that the Commission is required to evaluate whether an operator has both a valid lease and pooling authority when drilling a horizontal well across multiple tracts. Magnolia also contends that the trial court required the Commission to exceed its jurisdiction by adjudicating disputes between private parties over the authority to drill horizontal wells.

We will affirm the trial court's judgment in part, reverse in part, and remand the cause to the Commission for further proceedings.

BACKGROUND

Pooling, PSAs, and, to a lesser extent, allocation wells are central to this dispute. "Pooling" refers to the combining of tracts from more than one oil and gas lease for the drilling of a well where production from any of the tracts in the pooled unit is treated as production from all of the tracts. *See Hooks v. Samson Lone Star, LP*, 457 S.W.3d 52, 62 (Tex. 2015). Like pooling, PSAs and allocation wells link adjacent properties for the production of minerals,[1] but Texas statutes and regulations do not expressly require pooling of tracts as a prerequisite for every horizontal drilling of a wellbore that crosses property lines. An allocation well is "a horizontal well that traverses the boundary between two or more leases that have not been pooled and for which no agreement exists among the royalty owners as to how production will be shared." Clifton A. Squibb, *The Age of Allocation: The End of Pooling As We Know It?*, 45 Tex. Tech L. Rev. 929, 930 (2013). Absent agreement, production is allocated to the owners of the mineral estate in the tract where minerals are captured by the wellbore. *Id.* at 934. Under a PSA, the interest owners on the various tracts agree how production from a multitract well will be shared irrespective of where take points are. *See* E. Smith & J. Weaver, Tex. Law of Oil & Gas § 9.9(B), at 9-167-70 (2d Ed. 2020).

The Opielas are among the successors to the mineral interest of Otha Person and Myra Person, who leased their land (the Tract) for mineral exploration in 1955. The lease authorized a one-eighth royalty on oil produced from the Tract and stated that "[n]othing contained herein shall authorize Lessee in any manner whatever to pool said land or any part of

[1] Magnolia submitted and the Commission accepted as showing good faith consents to pooling by some royalty owners as the equivalent of signing the PSA and a good-faith claim of right to drill.

the same for oil, and for the production of oil from said land under this lease . . . ." The Opielas own 25% of the royalty interest and the remaining 75% of the royalty interest is owned by more than thirty interest holders who are not parties to this appeal.

EnerVest Operating, LLC, applied to the Commission on May 1, 2018, for a drilling permit for an allocation oil well. EnerVest proposed to drill on one property and direct the Well horizontally to cross under a road before entering the Tract underground. On May 2, 2018, the Opielas filed a complaint asking the Commission to refrain from issuing the permit because EnerVest did not have authority to pool the Tract with any other property. The day after the complaint was filed, the Commission issued the permit upon finding that EnerVest showed a good-faith claim to the right to drill into the Tract. EnerVest began drilling four days after the permit was issued, which was before the Opielas served their complaint on EnerVest. EnerVest responded that it did not need to pool the tracts crossed by the wellbore under Commission decisions in *Devon* and *Klotzman*. *See* Texas R.R. Comm'n, *Complaint of Monroe Properties, Inc., et al. that Devon Energy Production Co, L.P. Does Not Have a Good Faith Claim to Operate the N l Helped 120 (Alloc) Lease, Well No. 6H, Phantom (Wolfcamp) Field, Ward County, Texas*, Docket No. 08-0305330 (Dec. 18, 2017) (order of dismissal) ("*Devon*"); Texas R.R. Comm'n, *Application of EOG Resources, Inc. for its Klotzman Lease (Allocation) Well No. 1H, (Status No. 744730), Eagleville (Eagleford-Z) Field, Dewitt County, as an Allocation Well Drilled on Acreage Assigned from Two Leases*, Docket No. 02-0278952 (Sept. 24, 2013) (final order) *("Klotzman")*. EnerVest conveyed its interest to Magnolia before the contest was resolved.

On August 29, 2018, Magnolia applied for a permit on the Well to be drilled as a PSA well. As part of their application, Magnolia submitted a Form W-1 and Form P-16 as

required for applicants seeking a permit for a horizontal well. *See* 16 Tex. Admin. Code §§ 3.5, .40(g) (2018) (currently codified at § 3.40(i)), .86.[2] Neither the Form W-1 in the record nor the 2016 version of Form P-16 or the instructions for filling out the form in effect in 2018 defined a PSA well or mention a threshold percentage of signatories to a PSA.[3]

The Commission issued Magnolia the permit on August 30, 2018. The permit included this disclaimer:

> Commission Staff expresses no opinion as to whether a 100% ownership interest in each of the leases alone or in combination with a "production sharing agreement" confers the right to drill across lease/unit lines or whether a pooling agreement is also required. However, until that issue is directly addressed and ruled upon by a Texas court of competent jurisdiction it appears that a 100% interest in each of the leases and a production sharing agreement constitute a sufficient colorable claim to the right to drill a horizontal well as proposed to authorize the removal of the regulatory bar and the issuance of a drilling permit by the Commission, assuming the proposed well is in compliance with all other relevant Commission requirements.

The Opielas amended their complaint about the EnerVest permit on September 28, 2018 to challenge the permit issued to Magnolia. The Opielas contended that Magnolia

---

[2] All citations to the Texas Administrative Code will be to the version in effect in 2018 when the applications were made, unless otherwise noted.

[3] *See* Texas R.R. Comm'n 2016 Form P-16 for Acreage Designation (available at https://web.archive.org/web/20160804030249/http://www.rrc.texas.gov/media/31924/p-16p-final.pdf); *see also* Texas R.R. Comm'n 2016 Form P-16 Instructions (available at https://web.archive.org/web/20160804030249/http://www.rrc.texas.gov/media/31920/p-16-instructions-final.pdf). In Magnolia's reply in support of its motion to dismiss the Opielas' complaint about the permit, filed December 7, 2018, Magnolia states that Form P-16 was "last revised January 2016." The instructions to Form P-16 were revised in February 2019 and finalized in June 2019—after the application, permit, complaint, and hearing in this case. *See* Tex. R.R. Comm'n, *Complaint of Elsie Opiela and Adrian Opiela Regarding Magnolia Oil & Gas Operating LLC's (521544) Audioslave A Lease, Well No. 102H, Permit No. 839487, Sugarkane (Austin Chalk) Field, Karnes County, Tex.*, Oil & Gas Docket No. 02-0315435, 4-5, n.5,7 (Aug. 30, 2019) (PFD).

could not have a good-faith claim to operate the Well because the Opielas' lease did not authorize pooling of the Tract with others for oil production.

The hearings examiners heard the complaint on January 23, 2019, and issued their proposal for decision (PFD) on August 30, 2019. Tex. R.R. Comm'n, *Complaint of Elsie Opiela and Adrian Opiela Regarding Magnolia Oil & Gas Operating LLC's (521544) Audioslave A Lease, Well No. 102H, Permit No. 839487, Sugarkane (Austin Chalk) Field, Karnes County, Tex.*, Oil & Gas Docket No. 02-0315435, 4-5, n.7 (Aug. 30, 2019) (PFD). The examiners found that the Commission had previously determined that written oil leases covering tracts the Well traverses are a reasonably satisfactory showing of a good-faith claim to operate an allocation well, and that written agreements with 65% of all mineral and working interest owners for each tract the Well produces from would be sufficient to get a permit to operate a well. The examiners also found that Magnolia had PSAs—which they found included a PSA, consent to pool, or ratification of unit—with over 65% of the mineral and working interest owners. The PFD also included conclusions of law that Magnolia provided a reasonably satisfactory showing of a good-faith claim to operate the Well and that denied the Opielas' request that the Commission revoke Magnolia's permit. The Commission adopted the findings and conclusions in the PFD as its own in its Final Order ("the Order").[4]

The Opielas sought judicial review. Among their contentions, the Opielas argued that the Commission granted the permit pursuant to informal rules regarding PSA and allocation wells that were promulgated outside the APA and do not fall within any recognized exception to the requirement of formal rulemaking; they contended that rules for allocation and PSA well

[4] Because the Commission adopted the PFD's findings and conclusions in its Final Order, we will sometimes refer to the findings and conclusions as those of the Commission.

permits are not found in the administrative code. They argued that the Commission erred by adopting its findings from previous contested cases stating that the Commission lacks jurisdiction to review Magnolia's authority under the lease because the lease does not allow Magnolia to drill the PSA well. The Opielas contended that Magnolia does not have a good-faith claim of right to drill a well and that the issuance of the permit violated the Commission's informal rules because the agreements used to reach the 65% threshold included consents to pool. The Opielas contended that the Commission disregarded Texas Supreme Court precedent by concluding it has no jurisdiction to review whether an operator seeking a well permit has a good-faith claim under the lease to drill a well. The Opielas contended that the Commission failed to examine the lease and title documents under which Magnolia claims authority to drill the Well. The Opielas argued that the Commission erred in finding that Magnolia had shown a good-faith basis for the right to drill the Well because their lease prohibits the lessee from pooling this tract with others, does not permit allocation of production, and thus requires that any royalty be attributable to production solely from their tract.

The trial court concluded as follows:

1. The Commission erred in adopting rules for allocation and Production Sharing Agreement ("PSA") well permits without complying with the requirements of the Administrative Procedure Act, Tex. Gov't Code § 2001.001 et seq., and further erred in applying those rules by issuing well permits for the Audioslave A 102H Well (the "Audioslave Well").

2. The Commission erred in concluding it has no authority to review whether an applicant seeking a well permit has authority under a lease or other relevant title documents to drill the well.

3. The Commission erred in failing to consider the pooling clause of the lease covered by the Audioslave Well in deciding that Magnolia has a good faith claim to operate the well.

4. The Commission erred in finding that Magnolia showed a good faith claim of right to drill the Audioslave Well.

The trial court remanded the cause to the Commission, and this appeal followed.

STANDARDS OF REVIEW

A court may not substitute its judgment for the judgment of the state agency on the weight of the evidence on questions committed to agency discretion but:

> shall reverse or remand the case for further proceedings if substantial rights of the appellant have been prejudiced because the administrative findings, inferences, conclusions, or decisions are:
>
> (A) in violation of a constitutional or statutory provision;
> (B) in excess of the agency's statutory authority;
> (C) made through unlawful procedure;
> (D) affected by other error of law;
> (E) not reasonably supported by substantial evidence considering the reliable and probative evidence in the record as a whole; or
> (F) arbitrary or capricious or characterized by abuse of discretion or clearly unwarranted exercise of discretion.

Tex. Gov't Code § 2001.174(2). Courts examine whether there is some reasonable basis in the record for the action taken by the agency, not whether the agency reached the correct conclusion. *Railroad Comm'n v. Torch Operating Co.*, 912 S.W.2d 790, 792 (Tex. 1995). Courts review an agency's legal conclusions for errors of law and its findings of fact for support by substantial evidence. *Westlake Ethylene Pipeline Corp. v. Railroad Comm'n*, 506 S.W.3d 676, 681 (Tex. App. 2016). We may not substitute our judgment for the agency's on the weight of the evidence on questions committed to the agency's discretion, but we are not bound by errors of law. *See* Tex. Gov't Code § 2001.174; *Office of Pub Util. Counsel v. Texas-N.M. Power Co.*, 344 S.W.3d 446, 450 (Tex. App.—Austin 2011, pet. denied).

Whether substantial evidence supports the agency's decision is a question of law. *Texas Comm'n on Envtl. Quality v. Maverick County*, 642 S.W.3d 537, 547 (Tex. 2022). Courts presume that the Commission's order is supported by substantial evidence, and the complaining party has the burden to overcome that presumption. *Id*. Substantial evidence does not mean a large or considerable amount of evidence but is such relevant evidence as a reasonable mind might accept as adequate to support a finding of fact. *Lauderdale v. Texas Dep't of Agric.*, 923 S.W.2d 834, 836 (Tex. App.—Austin 1996, no writ). Where an agency has specialized knowledge, the court may defer to the agency's expertise and responsibility to develop regulatory policy. *In re SWEPI L.P. d/b/a Shell Western E & P*, 103 S.W.3d 578, 587 (Tex. App.—San Antonio 2003, no pet.).

Courts interpret agency regulations using the same principles we apply when construing statutes. *Patients Med. Ctr. v. Facility Ins.*, 623 S.W.3d 336, 341 (Tex. 2021). We start with the rule's plain text. *Maverick County*, 642 S.W.3d at 544. We must first determine what the rule's text means before deciding whether the agency's interpretation contradicts the text. *Id*. Courts will uphold an agency's interpretation of its own rule if the interpretation is reasonable and does not contradict the rule's plain language. *Railroad Comm'n v. Texas Citizens for a Safe Future & Clean Water*, 336 S.W.3d 619, 624 (Tex. 2011).

DISCUSSION

The parties do not dispute that Magnolia has a valid lease to drill on any of the tracts contacted by the wellbore. The issue is whether the record supports granting a permit for a PSA well under relevant and proper rules. Appellants contend that the trial court should have affirmed the Commission's order because Magnolia proved its entitlement to the permit granted. The Commission contends that its order issuing the permit based on a good-faith claim to drill

and operate the Well was supported by substantial evidence. The Commission also contends that, because it complied with notice-and-comment rulemaking to adopt rules and forms, it was not required to also promulgate by rulemaking the policy for issuing a permit to drill and operate a horizontal well. Magnolia similarly contends that the APA did not require the Commission to conduct formal rulemaking before issuing permits for unpooled multi-tract horizontal wells given its broad statutory authority, regulations, and discretion to exercise its expertise. Magnolia also contends that the trial court erred by holding that the Commission is required to evaluate whether an operator has both a valid lease and pooling authority when drilling a horizontal well across multiple tracts. Magnolia further contends that the trial court required the Commission to exceed its jurisdiction by holding that the Commission must adjudicate disputes between private parties over the authority to drill horizontal allocation wells as part of its good-faith evaluation of an application for a drilling permit. We will evaluate these overlapping issues together in the context of the trial court's judgment and the Commission's order.

1. Applicable statutes, rules, and decisional law background

The Legislature gave the Commission jurisdiction over all oil and gas wells in Texas. Tex. Nat. Res. Code § 81.051(a)(2). Conservation and development of all natural resources of this state is among the public rights and duties described in the Texas Constitution. Tex. Const. art. XVI, § 59(a). The Legislature empowered the Commission to "make and enforce rules and orders for the conservation of oil and gas and prevention of waste of oil and gas." Tex. Nat. Res. Code § 85.201. Commission rules require application for a permit to drill an oil well. 16 Tex. Admin. Code § 3.5(a). The application for the permit must be filed "on a form approved by the Commission," *id*., which implies the Commission has the power to approve forms. The Texas Supreme Court has held that, to show entitlement to a permit, an

operator must make a reasonably satisfactory showing of a good-faith claim to operate the proposed well. *Magnolia Petroleum Co. v. Railroad Comm'n*, 170 S.W.2d 189, 191 (Tex. 1943). The applicant can make a reasonably satisfactory showing of a good-faith claim of ownership even if another in good faith disputes title. *Id.* The Commission's rule defines "good-faith claim" as a "factually supported claim based on a recognized legal theory to a continuing possessory right in a mineral estate, such as evidence of a currently valid oil and gas lease or a recorded deed conveying a fee interest in the mineral estate." 16 Tex. Admin. Code § 3.15(a)(5) (regulations for surface-equipment removal requirements and inactive wells); *see also* Tex. Nat. Res. Code § 89.002(11) (using same definition in context of abandoned wells statute); *see also Roland Oil Co. v. Railroad Comm'n*, No. 03-12-00247-CV, 2015 WL 870232 at *2 (Tex. App.—Austin Feb. 27, 2015, pet. denied) (mem. op.).

In the 1943 *Magnolia* case, the Texas Supreme Court held that the Commission does not undertake to adjudicate questions of title or rights of possession when it grants a drilling permit. 170 S.W.2d at 191. The Commission's role in granting permits is to administer the conservation laws of Texas and to determine whether they bar drilling the well. *Id*. Title questions are a matter of common law that must be settled in the courts. *Id.* The trial court in *Magnolia* canceled a drilling permit granted by the Commission to E.A. Landman because the trial court found there was a bona fide controversy regarding whether Landman or Magnolia had proper title to the leasehold. *Id.* at 190. The court of appeals reversed the judgment canceling the permit but suspended it pending determination of the title suit in the county where the land was. *Id.* In reversing both the trial and appellate courts, the Texas Supreme Court wrote that granting a permit "merely removes the conservation laws and regulations as a bar to drilling the well . . . . Where there is a dispute as to those rights, it must be settled in court." *Id.* at 191. The

court concluded, "If the applicant makes a reasonably satisfactory showing of a good-faith claim of ownership in the property, the mere fact that another in good faith disputes his title is not alone sufficient to defeat his right to the permit; neither is it ground for suspending the permit or abating the statutory appeal pending settlement of the title controversy." *Id*.

While the Legislature has enacted statutes governing pooling of lands for oil and gas production, it has not done so for PSAs for horizontally drilled wells. The Legislature has considered bills amending the Natural Resources Code to expressly authorize—if not expressly prohibited by a lease, deed, or other contract and if granted a permit by the Commission—drilling and producing oil or gas from wells that traverse multiple tracts to prevent waste, promote conservation, or protect correlative rights. *See, e.g.,* Tex. H.B. 1552, 84th Leg., R.S. (2015); *see also* Tex. S.B. 367, 87th Leg., R.S. (2021). Bills to establish a statutory structure for unitization of separate tracts and involve the Commission in determining whether the unitization plan is fair, reasonable, and equitable for all interests have also been introduced but not passed. *See* Tex. S.B. 177, 85th Leg., R.S. (2017); Tex. H.B. 100, 83rd Leg., R.S. (2013).

Similarly, the Commission has not adopted Administrative Code rules specific to PSAs, though it has requested information about PSAs through its forms[5] and has granted permits for wells that were the subject of PSAs. The Commission has both rulemaking and adjudicatory powers with which to regulate oil and gas production. *Railroad Comm'n v. Lone Star Gas Co.*,

[5] *See, e.g.*, 16 Tex. Admin. Code §§ 3.40(g) (Assignment of Acreage to Pooled Development and Proration Units), 3.86(g)(4) (Horizontal Drainhole Wells) (requiring filing of Texas R.R. Comm'n 2022 Form P-16 for Acreage Designation, *available at* https://www.rrc.texas.gov/media/tppn4axe/p-16.pdf (filer must state that "[a]ll tracts listed will actually be traversed by the wellbore or the filer has pooling authority or other contractual authority, such as a production sharing agreement, authorizing inclusion of the non-drill site tract in the acreage assigned to the well.")).

844 S.W.2d 679, 688 (Tex. 1992). The Commission may exercise "informed discretion" whether to use rulemaking or adjudication, but should choose rulemaking except in cases when there is a danger that rulemaking would frustrate the effective accomplishment of the Commission's functions. *Id.* at 689. The Commission's adjudicatory decisions do not necessarily bind it in future adjudications, but an agency must explain its reasoning when it appears to depart from its policy or there is an apparent inconsistency in its decisions. *Texas State Bd. of Pharmacy v. Witcher*, 447 S.W.3d 520, 534 (Tex. App.—Austin 2014, pet. denied). In 2008, two of the three Commissioners voted to approve a permit application pursuant to a PSA and directed staff that permit applications for PSA wells "should be approved when the usual criteria are met and the operator certifies that at least 65% of the working and royalty interest owners in each component tract have signed the production sharing agreement." Texas R.R. Comm'n, Formal Comm'n Actions, Hearings Div., p. 3, Status #665639 (Sept. 9, 2008) (available at https://web.archive.org/web/20161222204413/https://www.rrc.texas.gov/media/9027/090908.pdf).[6]

2. The Commission's power to issue permits for multi-tract horizontal wells without pooling

The trial court held that the Commission erred by failing to consider the pooling clause of the lease covered by the Well in deciding that Magnolia has a good-faith claim to operate the Well. The Opielas' lease provides:

> Nothing contained herein shall authorize Lessee *in any manner whatever* to pool said land or any part of the same for oil, and for the production of oil from said land under this lease, and in the event oil is discovered on and under said land Lessor shall receive as his royalty the full one-eighth of all the oil produced and

[6] All sites listed by URL in this opinion were last visited June 26, 2023.

> saved from said entire tract of land leased hereunder, as herein in Paragraph 3 provided.

(Emphasis added.) The Opielas have not consented to pooling or signed a PSA and contend that the PSA well is "pooling by another name" and, as such, is prohibited by the lease; thus, they argue, the Commission cannot correctly find that Magnolia has a good-faith claim to the right to drill a horizontal well into the tract. The requirement that an applicant file a Form P-16 for a permit for a horizontal well appears in Rule 40, entitled the Assignment of Acreage to Pooled Development and Proration Units. 16 Tex. Admin. Code § 3.40(g). We must examine the relationship of pooling and PSAs to determine whether the assertion of right to drill under a PSA triggers and infringes on an anti-pooling clause in a lease.

Pooling is the subject of a chapter of the Natural Resources Code and other statutes in that code, in contrast to the silence regarding PSAs. *See* Tex. Nat. Res. Code ch. 102; *see also, e.g., id.* §§ 71.051-.057, 101.011-.013. Pooling is often done to allow smaller tracts to combine to meet requirements for spacing or density of wells. *See Browning Oil Co. v. Luecke*, 38 S.W.3d 625, 634 (Tex. App.—Austin 2000, pet. denied). Mineral operations anywhere in the combined tracts, or unit, are treated as if occurring on all tracts in the unit. *Id*. Pooling links properties such that the owners of the pooled tracts own joint undivided interests in the royalty earned from production under any of the tracts pooled. *Id.* Proceeds from production from one of the pooled tracts are shared by all owners of the tracts in proportion to the individual tract's proportion of the pooled acreage. *Id.*; *see also Hooks*, 457 S.W.3d at 62-63. A lessee has no power to pool absent express authority in its leases. *Luecke*, 38 S.W.3d at 634.

Pooling of tracts is not expressly required by Texas statutes or regulations for horizontal drilling of a wellbore that crosses property lines. Commentators have noted that, as of

the start of 2022, no statute or regulation yet addressed either PSA or allocation well permits. 2 E. Smith & J. Weaver, Tex. Law of Oil & Gas § 9.9(B), at 9-167-68 (2d Ed. 2020). Though stating that PSAs could form "super-pooled units"—a term not found in Texas statutes or rules—that combine pooled acreage into larger pools, the commentators describe PSAs as beginning with private contractual agreements among the owners and operators of pooled or unpooled tracts that will be traversed by a horizontal well. *Id.* at 9-169. A horizontal well is initially drilled vertically, then turns horizontal and can extend for hundreds of feet across multiple tracts. 38 S.W.3d at 634. Each tract traversed by the horizontal wellbore is a drillsite tract, and each production point on the wellbore is a drillsite. *Id.* Importantly, lessors in *Luecke* were not entitled to production from other lessors' tracts unless there had been a cross-conveyance of property interests; without valid pooling, the division of royalties was based on what production could be attributed to the lessors' tracts with reasonable probability. *Id.* at 646. By contrast, under a PSA, the interest owners on the various tracts agree how production from a well will be shared. 2 E. Smith & J. Weaver, Tex. Law of Oil & Gas § 9.9(B), at 9-170.

Before the hearings examiners in this case, James Clark, qualified as an expert witness on the Commission's procedures for permitting and other regulatory matters, testified that the PSA in this case divided production based on the effective lateral length on each tract.[7] Clark testified that "if it were a pooled unit, it would be neither a PSA nor an allocation," but that a lessee who had pooling authority perhaps could choose whether to pool or use a PSA. We conclude that production through a PSA well is not the same as pooling under Texas law.

[7] A similar method is used to apportion production for an allocation well. *See Springer Ranch, Ltd. v. Jones*, 421 S.W.3d 273, 286 (Tex. App.—San Antonio 2013, no pet.).

Consistent with our conclusion, the record indicates that the Commission simply ignored the anti-pooling clause as irrelevant to the Well permit. In rejecting the Opielas' complaint about the permit, the Commission cited its decisions upholding permits for allocation wells despite the absence of pooling authority in leases. In *Klotzman*, the Commission rejected its hearing examiners' recommendation that the permit be denied because of the lack of pooling authority under the leases being combined to form the developmental unit for the horizontal well. Texas R.R. Comm'n, *Application of EOG Resources, Inc. for its Klotzman Lease (Allocation), Well No. 1H(Status No. 744730), Eagleville (Eagleford-2) Field, Dewitt County, as an Allocation Well Drilled on Acreage Assigned from Two Leases*, Oil and Gas Docket No. 02-0278952 (Final Order issued Sept. 24, 2013) (*Klotzman*) at 1. The Commission concluded that the lessee had a good-faith claim to drill the Well essentially because an exception to spacing rules could be granted because the lessee had all of the working interest to the leases affected by the Well. *Id.* at 1-2. The Commission dismissed a similar challenge to another allocation well in *Monroe*, concluding that the issue was decided in *Klotzman*. Texas R.R. Comm'n, *Complaint of Monroe Properties, Inc., et al. that Devon Energy Production Co, L.P. Does Not Have a Good Faith Claim to Operate the N I Helped 120 (Allot) Lease, Well No. 6H, Phantom (Wolfcamp) Field, Ward County, Texas*, Oil and Gas Docket No. 08-0305330 (Order of Dismissal issued Dec. 18, 2017). The Commission's reliance on *Klotzman* indicates that it did not necessarily fail to consider the lease's pooling clause but that it found that the anti-pooling clause did not prevent Magnolia from showing a good-faith claim of the right to operate and drill the Well. Further, a lack of pooling authority alone does not prohibit drilling under a PSA.

The trial court erred by concluding that the Commission erred by failing to consider the lease's pooling clause in assessing the good faith of Magnolia's claim of a right to drill on the property.[8]

3. The Commission's authority to adjudicate the validity of leases

Magnolia contends that the trial court erred by holding that the "Commission erred in concluding it has no authority to review whether an applicant seeking a well permit has authority under a lease or other relevant title documents to drill the well." The PFD stated:

> The Commission does not adjudicate questions of title or right to possession, which are questions for the court system. A showing of a good faith claim does not require an applicant to prove title or a right of possession. It is sufficient for an applicant to make a reasonably satisfactory showing of a good faith claim.

(Footnotes omitted.) In their findings of fact and conclusions of law, the Commission found a good-faith claim of right to operate despite the possibility of a bona-fide lease dispute and found that lease disputes are beyond the jurisdiction of the Commission. This conforms to the Texas Supreme Court's holding that "[w]hen [the Commission] grants a permit to drill a well it does not undertake to adjudicate questions of title or rights of possession. These questions must be settled in the courts." *Magnolia*, 170 S.W.2d at 191. The Commission has no power to determine property rights. *Jones v. Killingsworth*, 403 S.W.2d 325, 328 (Tex. 1965). The Commission is similarly limited from adjudicating the validity of contractual agreements such as pooling agreements. *See Railroad Comm'n v. Rau*, 45 S.W.2d 413, 416 (Tex. Civ. App.—

[8] We note that whether Magnolia has breached the Opielas' lease, improperly taken their oil, or violated laws or regulations when producing oil from the Tract are questions separate from Magnolia's good-faith claim to operate the Well and may be properly the subject of a judicial suit like the one filed by the Opielas and currently pending in Karnes County. *See Opiela v. EnerVest Operating LLC*, No. 18-06-00153-CVK (81st Dist. Ct., Karnes County, Tex.).

Austin 1931, writ dism'd) (cited by *Kawasaki Motors Corp. USA v. Texas Motor Vehicle Comm'n*, 855 S.W.2d 792, 799 (Tex. App.—Austin 1993, no writ)). The Commission did not err by concluding that it had no power to adjudicate the applicant's rights under a lease or other relevant title documents, and the trial court erred to the extent it determined otherwise.

The Opielas assert that the Commission found in Findings 15-19 "that contractual authority is irrelevant to evaluating a good-faith claim and that the Commission has no jurisdiction to consider the contents of the lease." We do not find such a sweeping assertion of irrelevancy and lack of jurisdiction to "consider" the contents of the lease by the Commission in the cited findings, which are set out below; considering the contents of the lease is not the same as adjudicating rights under it. But even if the Commission entirely refused to look at the lease, the Opielas have not shown prejudice to their substantial rights. The Opielas' complaint that the Commission failed to consider the lease terms focuses on the anti-pooling clause. As we have concluded that the permit for horizontal drilling under a PSA is not pooling under Texas law, the anti-pooling clause was not implicated, and any refusal by the Commission to review that clause or the lease as a whole during its review of the good faith of Magnolia's claim of right to operate and drill did not prejudice the Opielas' substantial rights. The trial court erred by concluding otherwise.

4. The Commission's adoption of rules

The trial court held that the Commission erred in adopting rules for allocation and PSA wells without complying with the requirements of the APA and in applying those rules to issue a permit for the Well. The trial court did not specify which rules were erroneously

adopted. The parties narrowed the field somewhat in their briefing,[9] then narrowed the list further at oral argument to focus on rules not adopted through the APA, including forms.[10] The Opielas also complain of the adoption of the standard that an operator can obtain a permit for a PSA well by getting 65% of the interest holders to sign the PSA.

---

[9] In their briefing, the Opielas discussed Rules 5, 26, 40, 80, and 86. *See* 16 Tex. Admin. Code §§ 3.5, .26, .40, .80 .86. There is no dispute that any relevant version of these rules was adopted and amended pursuant to APA procedures and, more critically, that the two-year period for challenging the rulemaking process has passed. *See* Tex. Gov't Code § 2001.035(b). To the extent that the trial court's judgment addressed noncompliance with APA rulemaking procedures in the adoption of Rules 5, 26, 40, 80, and 86, it exceeded the scope of this permit complaint and was erroneous.

[10] The Opielas contend that, although Rule 80 was amended under the APA, forms adopted under its provisions are void because the Commission uses Rule 80 to amend forms without going through APA rulemaking procedures. *See* Tex. Gov't Code § 2001.035(a) (rule is voidable unless agency adopts it in substantial compliance with APA procedures). Amended Rule 80 provides: "Notice of any new or amended forms shall be issued by the Commission." 16 Tex. Admin. Code § 3.80(a) (effective in 2014 (39 Tex. Reg. 5148 (July 7, 2014)). When adopting the amendment to Rule 80, the Commission stated:

> The policy requires the Commission to promulgate, abolish or amend forms only upon the approval of a majority of Commissioners at a public meeting. . . . Where required by Texas law to promulgate, abolish, or amend a certain form through rulemaking procedures conducted under the Texas Administrative Procedure Act, the Commission will continue to do so. Otherwise, the Commission will consider staff's recommended form revisions in an open meeting. Staff will place the proposed form revisions on the Commission's website for public review and comment for a period of time proportionate to the subject and degree of change.

39 Tex. Reg. 5148. Appellants contend that the Commission's adoption of forms under the Rule 80(a) process substantially complies with the APA procedures. An amicus argues, however, that the amended Rule 80(a) is void because it purports to amend the APA itself by modifying rulemaking processes for forms and, among other arguments, that forms purporting to amend or replace a form created under APA rulemaking are void because the definition of rule "includes the amendment or repeal of a prior rule." *See* Tex. Gov't Code § 2001.003(6)(B).

Because resolution of these issues regarding Rule 80 would not alter our resolution of the appeal, we need not address them.

The parties extensively argued these rulemaking-related issues. But because resolution of these issues would not alter our resolution in the next section of the core issue in this case—whether Magnolia made a reasonable showing of a good-faith claim of the right to drill the horizontal PSA well into the Tract and was entitled to the permit—resolving them is not necessary to final disposition of the appeal. *See* Tex. R. App. P. 47.1.

5. The finding that Magnolia made a reasonably satisfactory showing of a good faith claim to operate the Well

The trial court held that the Commission erred in finding that Magnolia showed a good-faith claim of right to drill the Well. Appellants contend that the Commission correctly granted the permit because Magnolia met the 65% threshold for agreement of the mineral and working interest holders on each tract. The Commission's findings of fact included the following:

> 7. For a PSA, the operator certifies to the Commission that at least 65% of the mineral and working interest owners from each tract have signed an agreement as to how proceeds will be divided.
>
> 8. Regarding the Person Tract, 65.625% of the mineral interest owners signed either a PSA, consent to pool or ratification of unit, all setting forth a method of dividing proceeds.
>
> . . . .
>
> 12. According to the instructions for Form P-16 *Acreage Designation*, which is a form filed when applying for a drilling permit, the term PSA is defined as follows:
>
> > **PSA (PRODUCTION SHARING AGREEMENT WELLBORE):** For purposes of this document, a horizontal wellbore crossing two or more tracts/leases and for which the operator certifies that at least 65% of the MINERAL and WORKING interest owners from each tract within the developmental unit have signed an agreement as to how proceeds will be divided. The wellbore need not be perforated within each tract of the developmental unit.

13. All of the written agreements relied on by Magnolia as PSAs contain an agreement as to how proceeds will be divided.

14. Magnolia has PSAs with at least 65% of all mineral interest owners and working interest owners for each of the tracts traversed by the Well.

15. The Commission has previously determined that written oil and gas leases covering the tracts the well traverses are a reasonably satisfactory showing of a good faith claim to operate an allocation well. It follows that written agreements with 65% of all mineral interest owners and all working interest owners for each tract the well produces from is sufficient to get a permit to operate a well, in this case a PSA well.

16. Magnolia has a good faith claim to operate the Well.

17. Complainants claim that their contractual lease covering the Person Tract does not contain pooling authority and Complainants have not signed a PSA such that Magnolia does not have a right to drill the Well. Complainant also claims that some of the documents relied on by Magnolia are not PSAs and some of the mineral interest owners of the Person Tract who did sign agreements did not have authority.

18. While Complainants may have a bona fide lease dispute as to whether Magnolia has a right to operate, that is insufficient to defeat Magnolia's good faith claim.

19. While the Complainants may have a bona fide lease dispute with Magnolia, the determination of whether there has been a breach and the appropriate remedy is outside the jurisdiction of the Commission.

PFD at 16-17. The Commission also adopted the conclusion of law that "Respondent provided a reasonably satisfactory showing of a good faith claim to operate the Well." *See* Tex. Admin. Code § 3.15(a)(5).

The Commission's conclusion that Magnolia made the requisite showing of a good-faith claim plainly rests on satisfaction of the 65% threshold of agreement to the PSA that is not found in the Texas Administrative Code. If, as the Opielas contend, the 65% threshold is an improperly adopted rule, then the Order is founded on an error of law and must be reversed.

If, as Appellants contend, the 65% threshold as articulated by the Commission in 2008 is a properly created standard, we conclude that the Order is not supported by substantial evidence.

The Commission did not in its Order, including the findings and conclusions, cite a source for the origin of the 65% threshold to demonstrate a good-faith claim to operate the Well and entitlement to a permit to operate the Well.[11] In their briefing, the parties trace the formalization of that authority to the 2008 minute entry in which two of the three Commissioners approved a permit while "directing staff that wells that are permitted based on a production sharing agreement should be approved when the usual criteria are met and the operator certifies that at least 65% of the working and royalty interest owners in each component tract have signed *the production sharing agreement*."[12] (Emphasis added.) The Commission's 2008 pronouncement did not assert that multiple different PSAs could be signed or that other documents could be the equivalent of a PSA for purposes of reaching the 65% threshold. Here, the Commission found that Magnolia represented that at least 65% of mineral interest owners had signed "an agreement as to how proceeds will be divided," which on the Tract included "*either* a PSA, consent to pool, or ratification of unit." The evidence shows that only 15.625% of the interest owners on the Tract signed a PSA; the remaining nearly 50% signed some other document. Substantial evidence does not support a finding that 65% of the interest owners "signed the production sharing agreement."

---

[11] As discussed below in greater depth, the definition cited in Finding 12 tracks the instructions to Form P-16 as revised in February 2019 and finalized in June 2019—after the application, permit, complaint, and hearing in this case. *See* PFD at 5 n.7, 16.

[12] Texas R.R. Comm'n, Formal Comm'n Actions, Hearings Div., p. 3, Status #665639 (Sept. 9, 2008) (available at https://web.archive.org/web/20161222204413/https://www.rrc.texas.gov/media/9027/090908.pdf).

Recognizing that a PSA and other documents could be functional equivalents, we will examine further. The Commission's Findings 7 and 15 describe a broader scope of agreements as demonstrating that a PSA exists to include "an agreement" or a "written agreement." The Commission found that 65.625% of the interest owners had signed "written agreements" with Magnolia, including consents to pool. An exhibit in the administrative record details that, of the interest owners on the Tract, 15.625% signed a PSA, 0.563% signed a ratification of designation of unit, and 49.437% signed a consent to pool. But the Commission does not require pooling to permit a PSA well and, as we have concluded, PSAs are not the same as pooling because the property interests involved and production divisions are not the same. Consequently, even while granting due deference to the Commission's expertise in regulating this complex industry, *see SWEPI L.P.*, 103 S.W.3d at 587, we are not persuaded that signing a consent to pool can substitute for signing a PSA absent a good-faith showing that the consents to pool and the PSA call for the same sharing of production for the horizontal well across tracts that are not pooled. Magnolia did not certify and the Commission did not make such a finding in this record, nor is there any indication in the application that pooling of the three tracts occurred.[13] Even if we

[13] Examining the terms of the agreements could expand the scope of the Commission's inquiry into reviewing the parties' agreements and, therefore, could exceed the normal scope of inquiry in which the Commission engages at the permitting stage. Indeed, Clark testified that he does not "think that the Commission ever sees a sharing agreement or a pooling unless it's represented to be a pooled unit."

We note, however, that the consents to pool for persons listed as owners of the Tract do not all call for the same division of production as the PSAs. For example, the consent to pool signed by William J. O'Brien III states:

> The production on which Owners'[] royalty is calculated shall be that proportion of the total unit production which the net acreage of the Property included in the unit bears to the total surface acreage in the unit, but only to the extent such proportion of unit production is sold by Lessee.

By contrast, a PSA signed for Peggy Person states:

consider the 65% threshold from the Commission's 2008 directive a properly adopted rule or decisional precedent, the record does not contain substantial evidence that Magnolia satisfied that rule by certifying that 65% of the interest owners have signed the PSA, undermining Finding 14.[14]

The Commission's Finding 12 quotes the definition of a PSA from Form P-16 as allowing proof of a PSA to include certification that 65% of interest owners have signed "an agreement as to how proceeds will be divided." But this quotation tracks the 2019 instructions for Form P-16, while the permit contested here was granted based on applications filed in May and August 2018—applications that predate use of the definition of PSA in the Form P-16 instructions as revised in February 2019 and June 2019 or Form P-16 as revised in June 2019.[15] The hearing

---

> The proportionate share of production allocated to each Sharing Well Property will be calculated by a fraction which has as its denominator the Completed Lateral Length of the Sharing Well and which has as its numerator the distance (in feet) that the Completed Lateral Length lies within the Sharing Well Property.

[14] As noted above, if the 65% threshold is not a properly adopted rule, the Commission's Order would fail to satisfy the substantial-evidence standard because the Order would be founded on an error of law and arbitrary. *See* Tex. Gov't Code § 2001.174(2).

[15] This definition appears in the instructions for the 2019 version of Form P-16. *See* PFD at 4 n.5; *see also See* Texas R.R. Comm'n 2019 Form P-16 Instructions (available at https://static1.squarespace.com/static/60a1390c3f87204622d78356/t/60a44ce659676b700c0e40b3/1621380326686/p-16-instructions-drilling-permits.pdf); 2019 Form P-16 (available at https://static1.squarespace.com/static/60a1390c3f87204622d78356/t/60a44cc8c37bbe66f9284b6d/1621380296941/p-16p-final.pdf) (revised 6/2019).

In Magnolia's reply in support of its motion to dismiss the Opielas' complaint about the permit, filed December 7, 2018, Magnolia states that Form P-16 was "last revised January 2016." Neither the 2016 version of Form P-16 nor its instructions defined a PSA well. *See* Texas R.R. Comm'n 2016 Form P-16 for Acreage Designation (available at https://web.archive.org/web/20160804030249/http://www.rrc.texas.gov/media/31924/p-16p-final.pdf); see *also* Texas R.R. Comm'n 2016 Form P-16 Instructions (available at https://web.archive.org/web/20160804030249/http://www.rrc.texas.gov/media/31920/p-16-instructions-final.pdf).

on the complaint about the permit concluded in January 2019. Even assuming that the 2019 revisions to the instructions for Form P-16 were properly adopted, they do not control review of the application and permit at issue here. Regardless of whether the 2016 version of Form P-16 was properly adopted, neither that form nor the instructions used to complete the applications here contained the expanded definition of the agreements that would meet the 65% threshold. Substantial evidence does not support a finding or conclusion that Magnolia showed a good-faith claim to operate a PSA well based on a certification that at least 65% of the working and royalty interest owners in each component tract have signed the PSA as required by the 2008 Commission directive. The trial court did not err by finding the Commission erred by concluding otherwise.

6. Allocation well alternative

Magnolia invites us in the alternative to render judgment granting the permit as an allocation well. Though witness Clark opined at the hearing that Magnolia would have been entitled to an allocation-well permit, we do not find reverting to the previously obtained and challenged permit and rendering judgment that the allocation-well permit be issued to be among the dispositions available because the Order before us does not pertain to an allocation well permit. *See* Tex. Gov't Code § 2001.174. In the alternative, Magnolia requests that we remand

---

Without determining whether the forms and instructions are rules, we note that a substantive rule will be applied only prospectively unless it appears by fair implication from the language used that it was the intent of the legislature (or agency) to make it applicable to both past and future transactions. *Pantera Energy Co. v. Railroad Comm'n*, 150 S.W.3d 466, 473–74 (Tex. App.—Austin 2004, no pet.). Because the permit at issue in this case was granted and the Opielas' complaint about it denied based on an application completed in 2018, the 2019 revisions of the forms and their status as any sort of rule do not control our review of the Commission's 2019 decision and we need not consider whether the 2019 (or later) revisions to Form P-16 and related instructions are improperly adopted rules. *See* Tex. R. App. P. 47.1.

to the Commission to consider whether the Well may be permitted as an allocation well. We will remand for further proceedings, the content and nature of which will be determined by the parties, the Commission, and the relevant law and rules.

CONCLUSION

We reverse the parts of the trial court's judgment in which it determined (1) that the Commission erred in concluding it has no authority to review whether an applicant seeking a well permit has authority under a lease or other relevant title documents to drill the Well, and (2) that the Commission erred in failing to consider the pooling clause of the lease covered by the Well in deciding that Magnolia has a good-faith claim to operate the Well. We affirm the parts of the trial court's judgment in which it determined that the Commission erred in finding that Magnolia showed a good-faith claim of right to drill the Well and that this cause should be remanded.

We reverse the Commission's Order and remand this cause to the Commission for further proceedings.

Darlene Byrne, Chief Justice

Before Chief Justice Byrne, Justices Kelly and Smith
Dissenting Opinion by Justice Kelly

Affirmed in Part, Reversed in Part and Remanded

Filed: June 30, 2023

APPENDIX 5

Court of Appeals Dissenting Opinion

TEXAS COURT OF APPEALS, THIRD DISTRICT, AT AUSTIN

NO. 03-21-00258-CV

Railroad Commission of Texas and Magnolia Oil & Gas Operating LLC, Appellants

v.

Elsie Opiela and Adrian Opiela, Jr., Appellees

FROM THE 53RD DISTRICT COURT OF TRAVIS COUNTY
NO. D-1-GN-20-000099, THE HONORABLE KARIN CRUMP, JUDGE PRESIDING

D I S S E N T I N G O P I N I O N

The majority concludes that there was not substantial evidence supporting the Commission's finding that Magnolia "has PSAs with at least 65% of all mineral interest owners and working interest owners for each of the tracts traversed by the Well" and, in turn, the Commission's conclusion that "Magnolia has a good faith claim to operate the Well." In doing so, the majority assumes that the 65% threshold standard applied by the Commission is not an improperly adopted rule, as the Opielas contend. Because I disagree that the evidence is insufficient to support the Commission's finding that Magnolia has satisfied the 65% threshold, I respectfully dissent from that portion of the opinion.

The majority's decision rests on the distinction between an agreement to share production and an agreement to allow pooling. In essence, the majority concludes that pooling agreements would not be applicable to the proposed multi-tract horizontal well and thus there is no evidence of a production sharing agreement as to interest owners who signed pooling agreements.

I do not disagree that formally pooling leases into a pooled unit is different than an agreement between interest owners as to how production is shared from a horizontal well. That does not mean, however, that an interest owner who agrees that his lease may be "pooled," such that production from one tract is treated as production from all tracts, has not agreed as to how to share production from a horizontal well.[1]

I would conclude that an operator's certification that at least 65% of the mineral and working interest owners from each tract have agreed as to how production will be shared from a horizontal well, when supported by signed agreements in the record, is sufficient to show a good-faith claim to operate the proposed well. Because royalty calculations are specific to each lease and subject to negotiation, the exact shares or method for dividing proceeds from production (such as by surface acreage or in proportion to the length of the well that traverses the land) under any particular agreement is immaterial. Agreeing to share production differently with some interest owners simply means the operator may end up paying a larger royalty share than if the agreements had been uniform. In addition, this approach—considering only whether an agreement to share production exists, without regard to its specific terms—is consistent with Texas Supreme Court directive that the Commission should not be in the business of interpreting lease rights. *See Magnolia Petroleum Co. v. Railroad Comm'n*, 170 S.W.2d 189, 191 (Tex. 1943).

Here, the Commission found that "65.625% of the mineral interest owners signed either a PSA, consent to pool or ratification of unit, all setting forth a method of dividing proceeds" and that "[a]ll of the written agreements relied on by Magnolia as PSAs, contain an agreement as

[1] I note that one ground raised by the Opielas to challenge the permit is that their lease lacks a pooling agreement.

to how proceeds will be divided." I would conclude that these unchallenged findings are sufficient to support the Commission's conclusion as to Magnolia's good faith claim to drill the well. I would then resolve the issue of whether the Commission's 65% threshold standard complies with the APA. Because the majority does neither, I dissent.

_____

Chari L. Kelly, Justice

Before Chief Justice Byrne, Justices Kelly and Smith

Filed: June 30, 2023

APPENDIX 6
Court of Appeals Judgment

TEXAS COURT OF APPEALS, THIRD DISTRICT, AT AUSTIN

JUDGMENT RENDERED JUNE 30, 2023

NO. 03-21-00258-CV

Railroad Commission of Texas and Magnolia Oil & Gas Operating LLC, Appellants

v.

Elsie Opiela and Adrian Opiela, Jr., Appellees

APPEAL FROM THE 53RD DISTRICT COURT OF TRAVIS COUNTY
BEFORE CHIEF JUSTICE BYRNE, JUSTICES KELLY AND SMITH
AFFIRMED IN PART, REVERSED IN PART AND REMANDED –
OPINION BY CHIEF JUSTICE BYRNE
DISSENTING OPINION BY JUSTICE KELLY

This is an appeal from the judgment signed by the trial court on May 12, 2021. Having reviewed the record and the parties' arguments, the Court holds that there was reversible error in the trial court's judgment. We reverse the parts of the trial court's judgment in which it determined (1) that the Railroad Commission of Texas erred in concluding it has no authority to review whether an applicant seeking a well permit has authority under a lease or other relevant title documents to drill the Audioslave A 102H Well (the Well), and (2) that the Commission erred in failing to consider the pooling clause of the lease covered by the Well in deciding that Magnolia Oil & Gas Operating LLC has a good-faith claim to operate the Well. We affirm the parts of the trial court's judgment in which it determined that the Commission erred in finding that Magnolia showed a good-faith claim of right to drill the Well and that this cause should

be remanded. We reverse the Commission's Order and remand this cause to the Commission for further proceedings.

It is further order that appellants pay half of the costs of this appeal and that appellees pay the remaining half of those costs.