



RAILROAD COMMISSION OF TEXAS

OFFICE OF GENERAL COUNSEL

OIL & GAS DOCKET NO. 7B-0267313

COMMISSION CALLED HEARING TO PROVIDE DIAMOND S MASADA LLC AN OPPORTUNITY TO SHOW CAUSE WHY IT IS NOT LEGALLY RESPONSIBLE FOR PLUGGING THE ISENHOWER (18479) LEASE, WELL NOS. 3, 6, 8, 9, 10, 11, 12, 13, 17, 19, 21, 25, 26, 27, 28, 34, 35A, AND 41, CALLAHAN COUNTY REGULAR FIELD, CALLAHAN COUNTY, TEXAS

APPEARANCES:

FOR RESPONDENT:

Pete Lippincott

RESPONDENT:

Diamond S Masada LLC

PROPOSAL FOR DECISION

PROCEDURAL HISTORY

DATE OF REQUEST FOR HEARING:	August 30, 2010
DATE OF NOTICE OF HEARING:	September 8, 2010
DATE OF HEARING:	October 25, 2010
HEARD BY:	James M. Doherty, Hearings Examiner
DATE PFD CIRCULATED:	December 3, 2010

STATEMENT OF THE CASE

This hearing was called at the request of Diamond S Masada LLC ("Masada") to provide Masada with an opportunity to show cause why it is not legally responsible for plugging the Isenhower (18479) Lease ("subject lease"), Well Nos. 3, 6, 8, 9, 10, 11, 12, 13, 17, 19, 21, 25, 26, 27, 28, 34, 35A and 41 ("subject wells"), Callahan County Regular Field, Callahan County, Texas. The Notice of Hearing provided Masada notice that the Commission would also consider why the Statewide Rule 14(b)(2) plugging extensions for the wells should not be canceled and why Masada should not be ordered to plug the wells. A hearing was held on October 24, 2010. Masada appeared at the hearing through its member, Pete Lippincott, and presented evidence.

BACKGROUND

On June 15, 2010, a mineral owner in the property where the subject wells are located filed a complaint with the Commission alleging, among other things, that the oil and gas lease that

formerly covered this property had terminated based on a cessation of production. The complainant objected to approval of plugging extensions for the subject wells and asserted that the operator had no right other than to plug the wells and restore the land to good condition. A September 2, 1981, Oil, Gas and Mineral Lease submitted with the complaint had a term consisting of a primary term of one year and then so long thereafter as oil, gas or other mineral was produced from the leased premises. This Lease also contained a 60-day cessation of operations clause. The mineral owner complaint was assigned Hearings Section Complaint File No. 2010-086.

On July 6, 2010, the Hearings Section sent Masada a letter providing notice of the filing of the mineral owner complaint and requiring that Masada provide the Commission with evidence that it had a continuing right to operate the subject wells. No reply to this letter was filed by Masada. Accordingly, on August 3, 2010, the Hearings Section notified Masada that the Statewide Rule 14(b)(2) plugging extensions for the subject wells were cancelled and Masada was required to place the wells into compliance or plug them within 30 days or request a hearing on the matter. On August 30, 2010, Masada requested this hearing.

MATTERS OFFICIALLY NOTICED

The examiner has officially noticed the contents of Complaint File No. 2010-086 to provide the background leading up to the call of this hearing. The examiner has also officially noticed Commission records as follows: (1) P-5 Master Inquiry database relating to Masada; (2) P-5 Financial Assurance Inquiry database relating to Masada; (3) Officer/Agent Inquiry Selection database relating to Masada; (4) On Schedule Leases, Wells, Wellbores By Operator database relating to Masada; (5) Wells Subject to Rule 14(b)(2) database for Masada; (6) P-4 Current Fields/Leases By Current Operator and P-4 Current Fields/Leases By Historical Operator Name databases for Masada; (7) Production Data Inquiry database relating to Masada; (8) P-4 Inquiry database for the subject lease; (9) P-4 Certificate of Compliance Certified Letter/Cancellation/Reissue Inquiry database for the subject lease; (9) Oil Proration Schedule database for the subject lease; and (10) Oil Lease Ledger Status Inquiry for the subject lease.

The examiner has also officially noticed (1) Desist and Refrain Order issued by the California Department of Corporations to Pete Lippincott and Michael P. Johnstone on July 17, 2007; (2) Form P-4 transferring Isenhower (18479) Lease to Masada; (3) Forms P-4 transferring current and former leases to Masada; (4) Forms P-5 for Masada for the years 2006-2010; (5) Articles of Organization filed with Texas Secretary of State by Masada; and (6) Texas Franchise Tax Public Information Reports filed by Masada for the years 2007-2010.

Commission records officially noticed by the examiner show that Masada is a Texas limited liability company, and its Form P-5 organization report is currently active. The most recent Form P-5 filed for Masada lists Pete Lippincott as Manager of the company. Masada has approved financial assurance on file in the form of a \$50,000 letter of credit.

The Commission's On Schedule Leases, Wells, Wellbores by Operator database as of the date of the hearing showed that Masada was the designated operator of 61 wellbores having total depth of 57,333 feet. The Commission's Wells Subject to Rule 14(b)(2) database as of the date of the hearing showed that 54 of Masada's wells were subject to Rule 14(b)(2). Plugging extensions had been approved for 32 of these wells and denied for 22 of the wells. Twenty-five of Masada's wells subject to Rule 14(b)(2) had been inactive for 36 months or more. The Commission's Production Data Inquiry database shows that for the period January 2009 through August 2010, Masada reported total production for all leases and wells of 10 barrels of oil and that no production has been reported for any of Masada's wells since April 2009.

The Commission's P-4 Inquiry database shows that Masada was designated the operator of the Isenhower (18479) Lease by filing a Form P-4 approved on January 4, 2007, effective February 1, 2006. The Oil Proration Schedule database shows that this lease has a total of 22 wells, all of which were shut in at the time of the hearing. The P-4 Certificate of Compliance Certified Letter/Cancellation/Reissue Inquiry database shows that the certificate of compliance for the lease has been cancelled since October 1, 2007, by reason of the failure of Masada to pay required reconnect fees. and the lease was severed most recently on June 3, 2010, for H-15 delinquency, a problem that had not been resolved as of the date of the hearing. The Oil Lease Ledger Status Inquiry database shows that there has been no reported production for the lease since June 2005.¹

DISCUSSION OF THE EVIDENCE

Pete Lippincott, who listed himself as Masada's "CEO" on his appearance form, appeared at the hearing and presented testimony. According to Lippincott, Masada never had an oil and gas lease covering the property where the Isenhower (18479) Lease wells are located. This regulatory lease was assigned to Masada by Mahaffey Investments. According to Lippincott, the Isenhower (18479) Lease wells were transferred into Masada's name by a Form P-4 signed for Masada by Bobby Fellers, without Lippincott's knowledge or consent. Until October 2009, Masada's P-5 address was an address in Abilene, Texas, which was also Fellers' business address. Lippincott made the claim that he was unaware that the Isenhower (18479) Lease wells had been transferred into Masada's name until six or eight months ago, after he had changed Masada's P-5 address to Lippincott's own address in Houston and when he started to receive Commission correspondence about problems on the lease. Lippincott stated that Fellers had never been an employee of Masada

¹ Other relevant facts disclosed by the documents officially noticed by the examiner are discussed in the Examiner's Opinion section of this proposal for decision.

and that his relationship with Fellers was an arrangement pursuant to which Fellers would file production reports for Masada leases in Callahan County. However, he also claimed that Fellers was to “head-up” Masada, and Lippincott was to be the “bondholder.”²

Lippincott does not believe that Masada should be deemed legally responsible for the plugging of the Isenhower (18479) Lease wells and suggests that the Commission look to Bobby Fellers or Mahaffey Investments for this responsibility.

EXAMINER’S OPINION

Pursuant to Statewide Rule 14(b)(2)(B) in effect at the time of cancellation of plugging extensions for the Isenhower (18479) Lease wells, the wells were entitled to a plugging extension only if Masada had, and upon request provided evidence of, a good faith claim to a continuing right to operate the wells. This same requirement now appears in Statewide Rule 15(e)(3), which was effective September 1, 2010. Because Mr. Lippincott confirmed at the hearing that Masada has never had an oil and gas lease covering the property where the Isenhower (18479) Lease wells are located, the August 3, 2010, cancellation of the plugging extensions for these wells was clearly correct. Masada does not dispute this.

The Isenhower (18479) Lease wells have been inactive since June 2005. The wells do not have plugging extensions and have not been plugged. The certificate of compliance for the lease has been cancelled since October 1, 2007, and the lease was most recently severed on June 3, 2010, for failure of Masada to perform required fluid level or hydraulic pressure tests. In addition, Masada does not have a right to operate the wells. The wells are thus in violation of Statewide Rule 14(b)(2) which requires that plugging operations on each dry or inactive well be commenced within a period of one year after drilling or operations cease unless the Commission has approved a plugging extension for the well. Masada does not dispute this either.

The only remaining question is whether Masada or someone else has the legal responsibility for plugging the wells. Pursuant to §89.011 of the Texas Natural Resources Code, the operator of a well is required to plug the well when required and in accordance with Commission rules that are in effect at the time of the plugging. “Operator” is defined in §89.002 of the Code as a person who assumes responsibility for the physical operation and control of a well as shown by a form the person files with the Commission and the Commission approves. Statewide Rule 79 defines “operator” as a person, acting for himself or as an agent for others, and designated to the Commission as the one who has the primary responsibility for complying with its rules and regulations in any and all acts subject to the jurisdiction of the Commission. Pursuant to Statewide Rule 58, Form P-4 establishes the operator of an oil lease, gas well, or other well and certifies responsibility for regulatory compliance, including plugging of wells. Statewide Rule 58 provides also that an approved Form P-4 shall bind an operator until another operator files a subsequent Form P-4 and the Commission

² Lippincott confirmed that his testimony at the hearing was the first time he had ever made the claim to the Railroad Commission that the Isenhower (18479) Lease wells had wrongfully been placed into Masada’s name by Fellers.

has approved the subsequent Form P-4 and transferred the property on Commission records to the subsequent operator.

Masada designated itself the operator of the Isenhower (18479) Lease wells by filing a Form P-4 which was approved on January 4, 2007, effective February 1, 2006. This Form P-4 was signed for Masada by Bobby Fellers, Manager. No subsequent Form P-4 has been filed or approved to transfer the lease to any other operator.

Mr. Lippincott testified at the hearing that Fellers executed and filed the Form P-4 that designated Masada the operator of the Isenhower (18479) Lease wells without authority and without Lippincott's knowledge. For reasons discussed below, the examiner has concluded that Lippincott's testimony is not credible.

Bobby Fellers was no stranger to Masada at the time the Form P-4 was filed that designated Masada the operator of the Isenhower (18479) Lease wells. The Articles of Organization filed with the Texas Secretary of State on October 19, 2005, to organize Diamond S Masada LLC as a Texas limited liability company showed Fellers as the organizer, stated that the company would be managed by managers, and listed both Fellers and Lippincott as managers of the company. Texas Franchise Tax Public Information Reports filed for Masada with the State Comptroller for the years 2007 and 2008 listed both Fellers and Lippincott as Managers and Fellers as registered agent. The 2009 Texas Franchise Tax Public Information Report filed for Masada listed Fellers and Lippincott as Managers and Lippincott as the registered agent. Only as of 2010 was Fellers' name omitted from the Masada Texas Franchise Tax Public Information Report. In the 2010 Report, Edward S. Lippincott was listed as both Manager and registered agent. Furthermore, Form P-5 organization reports filed with the Commission for Masada for the years 2005 through 2008 were signed by Fellers and listed both Fellers and Lippincott as Managers. On March 29, 2009, Fellers signed a Form P-5 filed for the purpose of removing his name as a Manager and listing only Lippincott as Manager. A Form P-5 renewal for Masada filed with the Commission on November 4, 2009, was signed by Lippincott, listed Lippincott as the only Manager, and changed Masada's P-5 address to Lippincott's address in Houston. The 2010 Form P-5 renewal filing for Masada made on October 13, 2010, was also signed by Lippincott and named Lippincott as Masada's Manager.

The examiner concludes that as a Manager of Masada listed as such on Masada's Form P-5 organization report and Texas Franchise Tax Public Information Report during 2007 when the Form P-4 designating Masada as operator of the Isenhower (18479) Lease wells was filed and approved and during 2006 when the Form P-4 approval was made effective, Bobby Fellers had all the authority he needed to sign Forms P-4 to transfer the wells to Masada and make Masada legally responsible for compliance with Commission rules with respect to the wells.

Contrary to the implication of Lippincott's testimony at the hearing, the fact that Fellers signed for Masada on the Form P-4 that transferred the Isenhower (18479) Lease wells to Masada was not out of the ordinary. The examiner has officially noticed all the Forms P-4 that transferred all of Masada's current leases to Masada, including the Forms P-4 relating to the Gressett Oil Unit (18834) Lease, the Nelson, Ben Et Al. (23496) Lease, and the GAU Unit (25081) Lease in District 03 and the Williams, R. D. "A" (00478) Lease, the Alvey Estate (17206) Lease, and the Isenhower

(18479) Lease in District 7B. Four of the six Forms P-4 transferring these leases to Masada were signed for Masada by Fellers and two were signed by Lippincott. There are three leases formerly operated by Masada listed in the P-4 Current Fields/Leases by Historical Operator Name database; the Jewell R. Shirley (00381) Lease, the Adams, Roy (01470) Lease and the Isenhower, W. Est. (20700) Lease, all in District 7B. All three of the Forms P-4 that transferred these leases into Masada's name were signed by Fellers.

Assuming that Fellers had authority to sign for Masada on the Form P-4 that transferred the Isenhower (18479) Lease wells to Masada, which he clearly did, it really would make no difference that Lippincott personally may have been unaware of the transfer at the time it was made. Even so, it is simply not credible that Lippincott, as a Manager of Masada since the inception of the company, first learned of the January 2007 transfer of the lease to Masada in 2009. Lippincott raised no question with the Railroad Commission about Masada's legal responsibility for the wells until the hearing in this docket in October 2010.

The examiner has officially noticed a Desist and Refrain Order issued by the California Department of Corporations to Pete Lippincott and Michael P. Johnstone on July 17, 2007, that recited that commencing in 2006 Johnstone placed advertisements in newspapers and on the internet advertising investments in oil and gas projects, and California residents responding to the contact information in the advertisements were offered investments in oil and gas projects by Johnstone and Lippincott. The Order further recited that one of the oil and gas projects offered by Johnstone, Lippincott and Diamond S Oil, Inc. was for a "Fractional Undivided Working Interest Participation" in a project referred to as the "Eisenhower (sic)/William Shallow Development" prospect located in Callahan County, Texas. The Order further recited that the project was claimed to be owned and operated by Diamond S Oil, Inc. and Diamond S Masada, Inc. The examiner has further officially noticed from the Commission's P-4 Current Fields/Leases by Operator Name database that Diamond S Masada, LLC. is the operator of the Isenhower (18479) Lease and the Williams, R. D. "A" (00478) Lease, both in Callahan County, Texas. Recitations in the Desist and Refrain Order suggest that Lippincott was aware much earlier than 2009 that Masada was the operator of the Isenhower (18479) Lease.

The examiner concludes that Masada is legally responsible for the plugging of the Isenhower (18479) Lease wells, and Masada should be ordered to plug the wells. Furthermore, since Pete Lippincott was a person in a position of ownership and control of Masada at the time the plugging extensions for the Isenhower (18479) Lease wells were cancelled and the wells became non-compliant with Statewide Rule 14(b)(2), the examiner recommends an order finding and concluding that Lippincott is subject to the restrictions of Texas Natural Resources Code §91.114(a)(2). The examiner recommends adoption of the following Findings of Fact and Conclusions of Law.

FINDINGS OF FACT

1. At least ten (10) days notice of this hearing was provided to Diamond S Masada, Inc. ("Masada") by mailing the notice to Masada's Form P-5 organization report address. Masada appeared at the hearing through its Manager, Pete Lippincott, and presented evidence.
2. On August 3, 2010, an examiner in the Hearings Section of the Commission's Office of General Counsel notified Masada that the Statewide Rule 14(b)(2) plugging extensions for wells on the Isenhower (18479) Lease were cancelled and Masada was required to place the wells into compliance or plug them within 30 days or request a hearing on the matter. The cancellation of the plugging extensions was based on Masada's failure, upon request, to provide evidence that it had a good faith claim of right to operate the lease.
3. This hearing was called at the request of Masada to provide Masada with an opportunity to show cause why it is not legally responsible for plugging the Isenhower (18479) Lease wells, why the Statewide Rule 14(b)(2) plugging extensions for the wells should not be cancelled, and why Masada should not be ordered to plug the wells.
4. Masada is a Texas limited liability company. The Articles of Organization for the company were filed with the Texas Secretary of State on October 19, 2005. The Articles of Organization stated that Bobby Fellers was the organizer, and Fellers and Pete Lippincott were named in the Articles as Managers of the company.
5. Texas Franchise Tax Public Information Reports filed for Masada with the State Comptroller for the years 2007 and 2008 listed both Fellers and Lippincott as Managers and Fellers as registered agent. The 2009 Texas Franchise Tax Public Information Report filed for Masada listed Fellers and Lippincott as Managers and Lippincott as the registered agent. As of 2010 Fellers' name was omitted from the Masada Texas Franchise Tax Public Information Report. In the 2010 Report, Edward S. Lippincott was listed as both Manager and registered agent.
6. Form P-5 organization reports filed with the Railroad Commission for Masada for the years 2005 through 2008 were signed by Fellers and listed both Fellers and Lippincott as Managers. On March 29, 2009, Fellers signed a Form P-5 filed for the purpose of removing his name as a Manager and listing only Lippincott as Manager. A Form P-5 renewal for Masada filed with the Commission on November 4, 2009, was signed by Lippincott, listed Lippincott as the only Manager, and changed Masada's P-5 address to Lippincott's address in Houston. The 2010 Form P-5 renewal filing for Masada made on October 13, 2010, was also signed by Lippincott and named Lippincott as Masada's Manager.

7. The Commission's P-4 Current Fields/Leases by Current Operator Name database lists six regulatory leases currently operated by Masada: the Gressett Oil Unit (18834) Lease, the Nelson, Ben Et Al. (23496) Lease, and the GAU Unit (25081) Lease in District 03 and the Williams, R. D. "A" (00478) Lease, the Alvey Estate (17206) Lease, and the Isenhower (18479) Lease in District 7B. Four of the six Forms P-4 transferring these leases to Masada were signed for Masada by Fellers and two were signed by Lippincott.
8. The Commission's P-4 Current Fields/Leases by Historical Operator Name database lists three additional leases formerly operated by Masada: the Jewell R. Shirley (00381) Lease, the Adams, Roy (01470) Lease and the Isenhower, W. Est. (20700) Lease, all in District 7B. All three of the Forms P-4 that transferred these leases into Masada's name were signed by Fellers.
9. Masada was designated the operator of the Isenhower (18479) Lease by filing a Form P-4 approved on January 4, 2007, effective February 1, 2006. This Form P-4 was signed for Masada by Bobby Fellers.
10. As a Manager of Masada, Bobby Fellers had authority to sign and file the Form P-4 that designated Masada the operator of the Isenhower (18479) Lease.
11. As a Manager of Masada at the time the Statewide Rule 14(b)(2) plugging extensions for the Isenhower (18479) Lease wells were cancelled and the wells became non-compliant with Statewide Rule 14(b)(2), Pete Lippincott was a person in a position of ownership or control of Masada.
12. A violation of Statewide Rule 14(b)(2) is a violation of a rule related to safety and the prevention or control of pollution.
13. Well Nos. 2, 3, 6, 8, 9, 10, 11, 12, 13, 17, 19, 21, 25, 26, 27, 28, 29, 30, 32, 34, 35A, and 41 are carried on the Oil Proration Schedule for the Isenhower (18479) Lease in District 7B. All of these wells are shown on the Oil Proration Schedule to be shut in.
14. The certificate of compliance for the Isenhower (18479) Lease has been cancelled since October 1, 2007, by reason of the failure of Masada to pay required reconnect fees. The lease was severed most recently on June 3, 2010, for H-15 delinquency, a problem that had not been resolved as of the date of the hearing.
15. There has been no production reported to the Commission for the Isenhower (18479) Lease since June 2005.
16. The wells on the Isenhower (18479) Lease have been inactive for more than one year, do not have plugging extensions, and have not been plugged.

17. Masada does not have an oil and gas lease covering the property where the Isenhower (18479) Lease wells are located and has no good faith claim to a right to operate these wells.

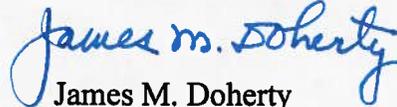
CONCLUSIONS OF LAW

1. Proper and timely notice of this hearing was provided to all interested persons.
2. All things have occurred and been accomplished to give the Commission jurisdiction to decide this matter.
3. Pursuant to §89.011 and §89.002 of the Texas Natural Resources Code and Statewide Rules 58 and 79 [16 TEX. ADMIN. CODE §3.58 and §3.79] Diamond S Masada, LLC is the operator with the responsibility for compliance with Commission rules, including rules relating to the plugging of inactive wells, with respect to the Isenhower (18479) Lease, Well Nos. 2, 3, 6, 8, 9, 10, 11, 12, 13, 17, 19, 21, 25, 26, 27, 28, 29, 30, 32, 34, 35A, and 41, Callahan County Regular Field, Callahan County, Texas.
4. Plugging extensions for the Isenhower (18479) Lease wells were properly cancelled on August 3, 2010, for failure of Diamond S Masada, LLC to file, upon request, evidence that Diamond S Masada, LLC has a good faith claim to a continuing right to operate the wells pursuant to Statewide Rule 14(b)(2)(C)(I) [16 TEX. ADMIN. CODE §3.14(b)(2)(C)(I)], now Statewide Rule 15(h) [16 TEX. ADMIN. CODE §3.15(h)].
5. Diamond S Masada, LLC violated Statewide Rule 14(b)(2) by failing to plug the Isenhower (18479) Lease, Well Nos. 2, 3, 6, 8, 9, 10, 11, 12, 13, 17, 19, 21, 25, 26, 27, 28, 29, 30, 32, 34, 35A, and 41, Callahan County Regular Field, Callahan County, Texas, within a period of one year after drilling or operations ceased and by failing to obtain approved plugging extensions for these wells.
6. As a person in a position of ownership or control of Diamond S Masada, LLC at the time the violations of Statewide Rule 14(b)(2) were committed with respect to the Isenhower (18479) Lease, Well Nos. 2, 3, 6, 8, 9, 10, 11, 12, 13, 17, 19, 21, 25, 26, 27, 28, 29, 30, 32, 34, 35A, and 41, Callahan County Regular Field, Callahan County, Texas, Pete Lippincott is subject to the restrictions of §91.114(a)(2) of the Texas Natural Resources Code.
7. Diamond S Masada, LLC should be ordered to plug the Isenhower (18479) Lease, Well Nos. 2, 3, 6, 8, 9, 10, 11, 12, 13, 17, 19, 21, 25, 26, 27, 28, 29, 30, 32, 34, 35A, and 41, Callahan County Regular Field, Callahan County, Texas.

RECOMMENDATION

The examiner recommends that the Commission adopt the attached final order affirming the August 3, 2010, cancellation of plugging extensions for the Isenhower (18479) Lease wells and ordering Diamond S Masada, LLC to plug these wells.

Respectfully submitted,



James M. Doherty
Hearings Examiner