

## Court Decision Raises New Questions for Allocation and PSA Wells

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After years of questions, legislative wrangling and arguments on both sides of the issue, the validity of permits for allocation and production sharing agreement (“PSA”) wells in Texas (following the drilling and completion of thousands upon thousands of allocation and PSA wells) has recently been called into question by a Texas trial court. The question of the legality of such wells and related Railroad Commission of Texas (“RRC”) permitting practices has bubbled to the surface a few times in recent years with administrative fights in front of the RRC itself and multiple lawsuits that all ultimately fizzled out through settlement prior to any ruling on the issue.

That changed on May 12, 2021 when the 53rd District Court in Travis County issued a final judgment in *Opiela v. Railroad Commission of Texas*, Cause No. D-1-GN-20-000099, providing the first judicial ruling on allocation and PSA wells in Texas. That case originated with the grant of a permit to a producer to drill a PSA well through Opiela’s mineral estate. While Opiela’s mineral estate was subject to an oil and gas lease, that lease did not contain a pooling clause, and Opiela declined to join a PSA. As such, when a producer sought a permit to drill first an allocation well and then a PSA well that produced from Opiela’s tract, Opiela challenged the RRC’s authority to issue the permit. The RRC dismissed Opiela’s challenge and Opiela pursued the contest in state court litigation.

In its ruling, the district court found that the RRC’s issuance of the permit for the well traversing Opiela’s mineral interest was improper in the following ways:

- The RRC erred in adopting allocation and PSA well policies and issuing the pertinent permit without formally enacting administrative rules in compliance with the Texas Government Code (including after a public comment period).
- The RRC erred in failing to investigate and confirm whether the producer seeking the permit had authority to drill the pertinent well under the necessary leases and pooling clauses within those leases.
- The RRC erred in finding the producer had a good faith claim of right to drill the well subject to the permit.

In light of this decision, the *Opiela* court remanded the challenge to the RRC’s administrative process for further proceedings.

While the court’s decision will likely be appealed, the case presents several important considerations for producers that have drilled or plan to drill allocation or PSA wells. An obvious one is how will the RRC treat the permitting process after the *Opiela* court’s judgment? Will it be “business as usual” for producers seeking permits or will the RRC show reticence in reaction to this final judgment?

Another consideration is the decision's potential effect upon existing permits for allocation and PSA wells, which currently cover several thousand producing oil and gas wells in Texas. A parallel proceeding to *Opiela* in Karnes County, Texas focuses on claims between Opiela and producers that, once determined, could shed light on the issue. Regardless of future developments in that case, producers and interest owners might expect increased challenges and complaints from lessors and landowners in the near term, particularly those who otherwise sought to challenge the permissibility of allocation wells and PSA wells.

While the RRC has consistently taken the position that it has the authority to grant permits for allocation and PSA wells, a position receiving broad support from TIPRO, TXOGA and other oil and gas interest groups, this judicial rebuke creates uncertainty for producers and mineral interest holders. The likely appeal of the *Opiela* final judgment and future allocation well suits will reveal whether Opiela marks a turning point for the validity of allocation and PSA wells under Texas law. To date, the RRC's permitting process has worked in concert with other factors to facilitate the rapid growth of onshore U.S. oil and gas production, the importance of which should not be underestimated.