IN THE SUPREME COURT OF THE STATE OF MONTANA
No. DA 23-0289

PHOENIX CAPITAL GROUP HOLDINGS, LLC, a Delaware limited liability company,

Plaintiff/Appellant/Cross-Appellee,

vs.

BOARD OF OIL AND GAS CONSERVATION OF THE STATE OF MONTANA,

Defendant/Appellee/Cross-Appellant,

and

KRAKEN OIL AND GAS, LLC,

Intervenor-Defendant/Appellee/Cross-Appellant.

COMBINED RESPONSE BRIEF AND OPENING BRIEF OF THE BOARD OF OIL AND GAS CONSERVATION OF THE STATE OF MONTANA

On Appeal from the Montana Thirteenth Judicial District Court,
Yellowstone County, The Honorable Colette B. Davies, Presiding

APPEARANCES:

MONTANA DEPARTMENT OF JUSTICE
Liz Leman, Agency Legal Counsel
Montana Bar No. 58640632
Agency Legal Services Bureau
1712 Ninth Avenue
P.O. Box 201440
Helena, MT 59620-1440
Telephone: (406) 444-7375
Elizabeth.Leman@mt.gov

Attorney for Montana Board of Oil and Gas Conservation

Jeffrey J. Oven (Bar #5005)
Brett L. Kvasnicka (Bar #50403076)
CROWLEY FLECK PLLP
P.O. Box 2529 59103
490 N. 31st Street, Suite 500
Billings, MT 59101-1267
Telephone: (406) 252-3441
joven@crowleyfleck.com
bkvasnicka@crowleyfleck.com

Attorneys for Kraken Oil and Gas, LLC

Adrian A. Miller
Michelle M. Sullivan
Sullivan Miller Law PLLC
2812 1st Avenue North, Suite 225
Billings, MT 59101
Telephone: (406) 403-7066
Fax: (406) 294-5702
Adrian.Miller@sullivanmiller.com
MichelleSullivan@sullivanmiller.com

Attorneys for Phoenix Capital Group Holdings, LLC

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INTRODUCTION

In February 2021, Appellant Phoenix Capital Group Holdings, LLC ("Phoenix") purchased mineral interests from the Solis family. Phoenix soon regretted its purchase when it discovered the Solises had for years repeatedly and consistently refused to participate in the drilling project of Appellee Kraken Oil and Gas, LLC ("Kraken"). Phoenix regretted its purchase even more when Appellee the Board of Oil and Gas Conservation of the State of Montana (the "Board") determined Kraken had complied with the statutory requirements for forced pooling and an award of risk penalties and granted Kraken's request for both. The fact that Phoenix failed to do its due diligence before purchasing the Solises' interest does not change the correct interpretation of Mont. Code Ann. § 82-11-202, and the district court (and the Board) should be affirmed on the merits.

The correctness of the district court's order on summary judgment is reinforced, ironically, by the evidence it improperly excluded. At the hearing before the Board, Kraken offered testimony that Katherine Solis affirmatively stated that she did not wish to participate in the drilling project. The hearing testimony was uncontradicted and no objection was made, although Phoenix was present with counsel. When Phoenix later objected to the evidence before the district court, the district court erred in excluding it, because Phoenix had failed to

preserve its objection at the lower level. Furthermore, the district court erred in finding that the evidence was hearsay because it constitutes an "operative fact" under the verbal act doctrine.

ISSUES PRESENTED

1. Whether the district court correctly affirmed the Board's order granting Kraken's request to force pool all mineral interests in the spacing unit and to authorize recovery of risk penalties against the interest owned by Phoenix?

2. Whether the district court correctly excluded statements to which no objection was made at the administrative level, and whether it correctly found that the statements were hearsay?

STATEMENT OF THE CASE

The Board agrees with Phoenix's statement of the procedural history of this case.

STATEMENT OF THE FACTS

Phoenix is the current owner of an undivided 1.4653 percent mineral interest located in Sections 6 and 8 in Township 25N, Range 59E in Richland County, Montana. *See* D.C. Doc. 25, Ex. 5. Phoenix purchased its interest on February 24, 2021, from Katherine Solis (via Steven Solis Sr., who received and re-transferred the interest the same day). *See* D.C. Doc. 25, Exs. 5, 6. With Board approval, Kraken has drilled the four oil wells at issue in this case in Sections 6 and 7: the

RKT Carda 7-6 #1H, RKT Carda 7-6 #2H, RKT Carda 7-6 #3H, and RKT Carda 7-6 #4H (hereinafter, "#1H Well" and "Latter Wells," respectively).

On October 4, 2018, the Board issued Order No. 52-2018, designating all of Sections 6 and 7, Township 25N, Range 59E as a permanent spacing unit for the production of oil and gas from the #1H Well, the first well drilled in the project. *See* D.C. Doc. 23, Ex. A. On the same day, the Board issued Order No. 53-2018, force pooling the interests in the same area and authorizing Kraken to recover non-consent (or risk) penalties related to the #1H Well. *See* D.C. Doc. 30, Ex. A-1.

On January 3, 2020, the Board approved Kraken's applications for permits to drill the Latter Wells in the same spacing unit. *See* D.C. Doc. 28, Exs. 23–25. On January 13, 2020, Kraken sent Ms. Solis election packets regarding each of the Latter Wells by certified mail to her address of record (hereinafter, "January 2020 Letters"). *See* D.C. Doc. 25, Exs. 11–13; D.C. Doc. 27, Ex. F. Each letter explained that Kraken planned to drill a new well and stated the details of the well, including its location, planned depth, expected cost, and anticipated spud date. *See id.* Each letter sought Ms. Solis's acceptance or rejection of the proposal within thirty days and explained that she could participate by paying a share of the costs or by leasing her mineral interest to Kraken. *See id.* Each letter warned that risk penalties may be imposed if she did not respond. *See id.* If she had questions, each letter provided a phone number and email address where she could reach a Kraken

representative. *See id.* Ms. Solis never responded in any way or paid any share of the costs of drilling. *See* D.C. Doc. 27, Ex. B at ¶ 6. Between January 21 and February 6, 2020, Kraken spudded (began drilling) the Latter Wells.

More than a year later in February 2021, Phoenix purchased Ms. Solis's mineral interest. Immediately following the conveyance, Phoenix sent an email to Kraken regarding its purchase of the Solises' mineral interests. *See* D.C. Doc. 25, Ex. 15; D.C. Doc. 27, Ex. G. In its email, Phoenix stated it wished to participate in several wells, including the #1H Well and Latter Wells. On March 18, 2021, Kraken responded that the Solis interest had been deemed non-consent and the Board had authorized non-consent penalties (for the #1H Well) pursuant to Mont. Code Ann. § 82-11-202(2). *See* D.C. Doc. 25, Ex. 17; D.C. Doc. 27, Ex. H.

On August 18, 2021, Kraken completed the Latter Wells. *See* JA-2 at 65:24–66:2. On August 26, 2021, Kraken applied to the Board for a pooling order and imposition of non-consent penalties. *See* D.C. Doc. 23, Ex. C. The Board held a hearing on the application on October 14, 2021, at which both Kraken and Phoenix appeared with their counsel. *See* D.C. Doc. 27, Ex. C.

In support of its application, Kraken presented testimony from a contracted landman, Lindsey Meszaros, regarding her attempts on Kraken's behalf to obtain Ms. Solis's participation in the drilling project. *See* D.C. Doc. 23, Ex. D at 8:1–9:17. Ms. Meszaros testified that she attempted to contact Ms. Solis by phone

"eight or nine times" beginning in June 2017, before any wells were drilled. Each time Ms. Meszaros said who she was and why she was calling, Ms. Solis would end the phone call. *See* D.C. Doc. 23, Ex. D at 8:6–20. Similarly, every packet mailed to Ms. Solis was returned as "unclaimed" (not "undeliverable"). *See* D.C. Doc. 23, Ex. D at 9:6–8, 9:12–13. Ms. Meszaros contacted Ms. Solis's sister, Ella Lennox, who had leased her mineral interest to Kraken. Ms. Lennox confirmed her sister's contact information and said Ms. Solis was not interested in a lease because she feared it would jeopardize her husband's subsidized medical care. *See* D.C. Doc. 23, Ex. D at 8:22–35. In late September 2017, Ms. Meszaros was finally able to speak with Ms. Solis, who confirmed that she did not want to lease her mineral interest, did not want to sell her interest, and did not want to participate in the drilling project in any capacity. *See* D.C. Doc. 23, Ex. D at 8:37–40. Ms. Solis further asked Ms. Meszaros not to contact her anymore. *See* D.C. Doc. 23, Ex. D at 9:8–13. At that point, Ms. Meszaros felt she had exhausted every reasonable method to obtain Ms. Solis's voluntary participation in the drilling project. *See* D.C. Doc. 23, Ex. D at 10:10–26.

In response, Phoenix argued that because Ms. Solis had not refused in writing to participate in the drilling project, and because the letters to notify her that the Latter Wells would be drilled were not sent 30 days prior to the spud date, Kraken could not rely on a presumption of non-participation under Mont. Code

Ann. § 82-11-202(3)(a). *See* D.C. Doc. 23, Ex. D at 13:26–14:10. On questioning by the Board's attorney, Phoenix conceded that neither a letter sent 30 days prior to the spud date nor written waiver of rights was required for a pooling order and risk penalties to issue. *See* D.C. Doc. 23, Ex. D at 17:32–20:12. Kraken clarified that it was not relying on the presumption of non-participation in Mont. Code Ann. § 82-11-202(3)(a) in making its application, but on Ms. Solis's actual statements, and argued that even if the Board did reach the presumption, Ms. Solis had acknowledged receipt of Kraken's letters by refusing to accept them. *See* D.C. Doc. 23, Ex. D at 20:19–31. Phoenix did not object to any of the testimony offered by Ms. Meszaros.

Following the hearing, the Board issued Order No. 74-2021, granting Kraken's request to force pool the mineral interests in Sections 6 and 7, Township 25N, Range 59E and authorizing Kraken to recover non-consent penalties with respect to the Latter Wells. *See* D.C. Doc. 23, Ex. B. In doing so, the Board did not reach the presumption in Mont. Code Ann. § 82-11-202(3)(a). Instead, it found that "Kraken Oil & Gas LLC has made an unsuccessful, good faith attempt to acquire voluntary pooling of interests in the spacing unit as required by § 82-11-202(1)(b), Mont. Code Ann." but that "[Ms.] Solis failed or refused to pay her share of the costs of development or other operations after written demand under § 82-11-202(2)(b), Mont. Code Ann." It further found that "Phoenix Capital is bound by

this decision as the successor to her interest." D.C. Doc. 23, Ex. B at BOGC 00050.

Phoenix applied for rehearing of Order No. 74-2021 on the grounds that it was not provided actual notice of the October 14, 2021 hearing, did not have the opportunity to conduct discovery, and the Board could rely on neither the presumption in Mont. Code Ann. § 82-11-202(3)(a) nor hearsay evidence. *See* D.C. Doc. 23, Ex. E. On December 1, 2021, the Board issued Administrative Order No. 11-A-2021, denying Phoenix's Application for Rehearing on the grounds that it had demonstrated no error in the Board's original decision, and to the extent it alleged procedural errors, it had waived them by failing to raise them at hearing. *See* D.C. Doc. 23, Ex. F.

Phoenix filed suit. All parties later agreed there were no disputes of fact, and the matter could be resolved on summary judgment. Each party filed a motion for summary judgment. At the hearing on November 22, 2022, the district court excluded as hearsay the portion of Ms. Meszaros's testimony before the Board where she recited what Ms. Solis had said to her on the phone. Nevertheless, on April 17, 2023, the Court granted summary judgment to the Board and to Kraken and denied Phoenix's request for summary judgment. Phoenix timely appealed, and Kraken and the Board timely cross-appealed.

STANDARDS OF REVIEW

A. Summary Judgment

The Montana Supreme Court reviews a district court's summary judgment ruling "de novo, applying the same summary judgment standards, based on Rule 56, M.R.Civ.P., as the District Court." *Thornton v. Alpine Home Ctr.*, 2001 MT 310, ¶ 10, 307 Mont. 529, 38 P.3d 855. Summary judgment should be granted where the evidence shows "that there is no genuine issue as to any material fact and that the movant is entitled to judgment as a matter of law." Mont. R. Civ. P. 56(c)(3).

This Court "need not defer to the judgments and decisions of the district court," including with respect to "evidentiary rulings in the summary judgment context." *PPL Mont., LLC v. State*, 2010 MT 64, ¶ 85, 355 Mont. 402, 229 P.3d 421. Rather, the Court "review[s] evidentiary rulings going directly towards the propriety of summary judgment de novo, in order to determine whether the evidentiary requirements for summary judgment have been satisfied." *Id.*

B. Board Orders

"When reviewing an agency decision," this Court applies "the same standard as the district court." *Mont. Power Co. v. Mont. PSC*, 2001 MT 102, ¶ 18, 305 Mont. 260, 26 P.3d 91. An order of the Board is reviewed under Mont. Code Ann. § 82-11-144, and not under the Montana Administrative Procedure Act

(MAPA). *See Ostby v. Bd. of Oil & Gas Conserv.,* 2014 MT 105, ¶ 11, 374 Mont. 472, 324 P.3d 1155.

On review, the "statute, rule, order, or decision involved in the suit shall be prima facie valid," Mont. Code Ann. § 82-11-144, meaning that it is presumed to be correct "until contradicted and overcome by other evidence." Mont. Code Ann. § 26-1-102(6). The Court's role "is not to say whether the Court would have granted the permits" or issued a particular decision, but whether the Board "was sufficiently thorough and discerning in its decision-making process" to satisfy the applicable legal requirements. *Mont. Wildlife Fed'n Mont. Bd. Of Oil & Gas Conserv.*, 2012 MT 128, ¶ 51, 365 Mont. 232, 280 P.3d 877; *see also Park Cty. Envtl. Council v. Mont. Dep't of Envtl. Quality*, 2020 MT 303, ¶ 18, 402 Mont. 168, 477 P.3d 288 ("The Court's focus is on the administrative decision-making process rather than the decision itself.").

The suit "shall be tried de novo and disposed of as an ordinary civil suit and not upon the record of any hearing before the board." Mont. Code Ann. § 82-11-144. That means that the Board's findings of fact "in support of the rule, order, or decision involved in the suit [are] not binding on the court though supported by evidence introduced at a hearing before the board" and that the Court "shall decide all relevant questions of law…." Mont. Code Ann. § 82-11-144. Because the Board's order is prima facie valid, the initial burden is on the challenger to produce

evidence sufficient to overcome the presumption that the order is correct; the court's role is to review the evidence de novo to determine whether it is sufficient.

SUMMARY OF THE ARGUMENT

At the center of this case is Phoenix's buyer's remorse, by which it attempts to upend the plain and established meaning of Mont. Code Ann. § 82-11-202. Phoenix argues principally that (1) good faith required Kraken to accept Phoenix's belated attempts to participate in the Latter Wells, rendering forced pooling inappropriate, and (2) Kraken's January 2020 Letters to Ms. Solis do not entitle it to receive risk penalties because they did not comply with the requirements of Mont. Code Ann. § 82-11-202(3).

The first argument fails because Kraken had already made an "unsuccessful, good faith attempt" to voluntarily pool Ms. Solis's interest. The terms of that offer expired long before Phoenix tried to accept it, and Kraken's entitlement to forced pooling (and therefore risk penalties) had already attached.

The second argument fails because the January 2020 Letters were not sent pursuant to Mont. Code Ann. § 82-11-202(3), and neither Kraken nor the Board relied on the statutory presumption of refusal. Subsection (2)(b) does not set a deadline for the owner's response to an offer to participate; the operator's offer does. Because Ms. Solis actually received Kraken's offer, and subsequently "failed" *and* "refused" to participate, no presumption is needed.

In the event this Court deems the evidence that Ms. Solis "failed" to participate in the Latter Wells insufficient, it should overturn the district court's exclusion of evidence showing that she "refused" to participate. Phoenix failed to preserve its hearsay objection for review by the district court. Furthermore, the evidence was not properly deemed hearsay, because it falls within the exception described by the verbal act doctrine.

RESPONSIVE ARGUMENT

Phoenix's appeal revolves around the interpretation of Mont. Code Ann. § 82-11-202. In interpreting a statute, the Court's purpose is "to ascertain and declare" what the statute says, and "not to insert what has been omitted or to omit what has been inserted." Mont. Code Ann. § 1-2-101. In other words, the Court is tasked to "implement the objectives the legislature sought to achieve." *Pennell v. Nationstar Mortg., LLC*, 2022 MT 235, ¶ 10, 410 Mont. 526, 520 P.3d 796 (quoting *Mont. Vending, Inc. v. Coca-Cola Bottling Co.*, 2003 MT 282, ¶ 21, 318 Mont. 1, 78 P.3d 499). "If the intent of the legislature can be determined from the plain meaning of the words used in the statute, the plain meaning controls, and this Court need go no further nor apply any other means of interpretation." *Mont. Vending*, ¶ 21 (citation omitted).

If, on the other hand, a statute's meaning cannot be determined from its plain language, the Court turns to a determination of the legislature's intent.

See Mont. Vending, ¶ 21. The statutory scheme should be read as a whole and construed "so as to forward the purpose of that scheme." *Wright v. Ace Am. Ins. Co.*, 2011 MT 43, ¶ 24, 359 Mont. 332, 249 P.3d 485. The Court's interpretation "cannot divest the authority of other provisions, or render other provisions, superfluous." *City of Missoula v. Fox*, 2019 MT 250, ¶ 22, 397 Mont. 388, 450 P.3d 898. Furthermore, "[s]tatutory construction should not lead to absurd results if a reasonable interpretation can avoid it." *Mont. Sports Shooting Ass'n v. State*, 2008 MT 190, ¶ 11, 344 Mont. 1, 185 P.3d.

For administrative review cases in particular, "it is a well-accepted rule of statutory construction that the long and continued contemporaneous and practical interpretation of a statute by the executive officers charged with its administration and enforcement constitutes an 'invaluable aid in determining the meaning of a doubtful statute.'" *Mont. Power Co.*, ¶ 24 (quoting *Bartels v. Miles City*, 145 Mont. 116, 122, 399 P.2d 768, 771 (1965)). This is particularly the case where the agency has "technical and scientific expertise beyond the grasp of the Court." *Mont. Envtl. Ctr. v. Mont. Dep't of Envtl. Quality*, 2019 MT 213, ¶ 20, 397 Mont. 161, 451 P.3d 493. Thus, this Court generally accords "great deference" to the agency's interpretation, absent "compelling indications that the construction is wrong." *Mont. Power Co.*, ¶ 23 (quoting *D'Ewart v. Neibauer*, 228 Mont. 335, 340, 742 P.2d 1015, 1018 (1987)). This deference is "most appropriate when the agency

interpretation has stood unchallenged for a considerable length of time, thereby creating reliance in the public." *Mont. Trout Unlimited v. Mont. Dep't of Nat. Res. & Conservation*, 2006 MT 72, ¶ 37, 331 Mont. 483, 133 P.3d 224.

I. The Board correctly decided that Kraken is entitled to forced pooling.

A. Forced pooling is appropriate where the operator has made an "unsuccessful, good faith attempt" to voluntarily pool mineral interests.

Oil and gas development in Montana is governed by Montana's Oil and Gas Conservation Act (the "Act"), enacted in 1953 and based on model legislation published by the Interstate Oil Compact Commission (IOCC). *See U.V. Indus. v. Danielson*, 184 Mont. 203, 213, 602 P.2d 571, 578 (1979). The purpose of Montana's Act is generally understood to be "[t]he prevention of physical waste, the prevention of economic waste, and the protection of correlative rights." *Pattie v. Oil & Gas Conservation Comm'n*, 145 Mont. 531, 540, 402 P.2d 596, 601 (1965). "Correlative rights" means "those rights of each landowner, lessee, or operator in the common source of petroleum. The rights are limited by corresponding duties to the neighboring operator." *Id.* at 536, 402 P.2d at 599.

To control wellhead densities and locations, the Board is (among other things) authorized to establish spacing units on surface land upon the application of an "interested person" (typically an operator). *See* Mont. Code Ann. § 82-11-201. A spacing unit is defined as "the area that can be efficiently drained by one well,"

Mont. Admin. R. 36.22.302(69), although the Board may approve additional wells in a spacing unit where necessary to accomplish the purposes of the Act. *See* Mont. Code Ann. § 82-11-201(6). A temporary spacing unit is first established where underground resources are "unproven." *See* Mont. Code Ann. § 82-11-201(2). This allows for exploratory drilling, and an order establishing a temporary spacing unit typically requires the operator to begin drilling within one year. If the area proves promising, the operator may apply to establish a permanent spacing unit after the well is completed. *See* Mont. Code Ann. § 82-11-201(1)(b).

Once a permanent spacing unit is established, the operator begins to seek voluntary pooling of the mineral interests owned within the unit. Pooling recognizes that each mineral interest owner within the spacing unit owns a proportionate share of the underground resource, and that the surface location of the well does not determine ownership of the extracted resource. *See* Mont. Code Ann. § 82-11-202(1)(b) (both operations on and production from the unit is considered to have taken place on each individual tract within the spacing unit). Voluntary pooling may mean that mineral interest owners agree to pay for a proportionate share of the costs incurred in drilling and producing the well, or it may mean that they lease their interest to the developer in exchange for flat and/or royalty payments.

If an owner cannot be found or does not wish to participate, the operator may apply to the Board for forced pooling. *See* Mont. Code Ann. § 82-11-202(1)(b). The purpose of forced pooling is to prevent waste of economic resources and to protect other owners' correlative right to be paid from the production. *See* D.C. Doc. 25, Ex. 1 at 48. The application must go to a hearing before the Board. *See* Mont. Code Ann. § 82-11-202(1)(b). Thus, although the statute allows operators to apply for forced pooling either before or after a well is drilled, *see* Mont. Code Ann. § 82-11-202(2), operators often wait until a well is completed to know whether it will be profitable, and whether the potentially costly application process will be worthwhile. *See* JA-2 at 52:22–53:12, 53:21–54:1. The Board has discretion to issue a forced pooling order upon a finding that the operator "has made an unsuccessful, good faith attempt to voluntarily pool the interests within the permanent spacing unit." Mont. Code Ann. § 82-11-202(1)(b).

Even though forced pooling may not be ordered for some time, the operator's right to obtain forced pooling (and therefore risk penalties, *see infra*) "attaches" to the interest of a non-consenting owner once the operator has made its "unsuccessful, good faith attempt" to pool voluntarily. The operator's "attempt" is essentially an offer for the mineral interest owner to enter a contractual relationship with the operator. Offers to contract may be revoked or expire by their own terms.

See Sunburst Oil & Gas Co. v. Neville, 79 Mont. 550, 563, 565, 257 P. 1016, 1019–20 (1927) (offer may be revoked until accepted).

A ruling by the Industrial Commission of the State of North Dakota (ICND), the Board's equivalent in that state, is instructive as to the policy reasons for immediate attachment. North Dakota has also adopted the IOCC's model legislation, and its governing statutes are substantially similar to Montana's. *See* D.C. Doc. 25, Ex. 3 at 15–16, 19; N.D. Cent. Code § 38-08-08(1) and (3)(c) (forced pooling may be ordered "after notice and hearing" and risk penalties may be ordered after "an unsuccessful, good faith attempt to have the unleased nonparticipating owner execute a lease…."). Many operators work in both Montana and North Dakota. In considering an application for forced pooling and risk penalties where a new owner acquired the mineral interest at issue after the operator had unsuccessfully sought voluntary pooling from the prior owner, the ICND held:

> Once operators fulfill all the substantive and procedural requirements, they should not be left wondering whether the penalty is secure or whether a third party will enter the picture. Operators are entitled to some certainty. The arrival of a third party—an arrival of which the operator is likely unaware—should not be allowed to disrupt reasonable expectations. Once the response period set forth in a proper invitation to lease has expired without a reply from the mineral owner, the risk penalty "attaches." Although the Commission must ultimately approve the penalty, if there is opposition, operators can have some confidence that the Commission is likely to impose the penalty if their invitation to lease satisfies the statutes and rule. Further, a party like [the new owner] is better able to control its uncertainty than is an operator…. [The new

> owner] can protect itself by managing its relationship with the mineral owner…. Lastly, the risk penalty is designed to benefit companies willing to take the risk in exploring for and developing oil and gas.

D.C. Doc. 30, Ex. B at ¶ 23; *see also* JA-2 at 74:24–75:15. The same principles apply in Montana. Once the operator's reasonable, good faith offer to participate expires, the operator is entitled to rely on the owner's non-response and is not bound by future attempts to accept.

B. Kraken made an "unsuccessful, good faith attempt" to voluntarily pool the mineral interest.

Between June and September or October of 2017, Kraken contacted Ms. Solis multiple times by both phone and mail. It double checked that it had the correct contact information, gave her different options to participate, and warned her about the consequences of non-participation. In January 2020, Kraken again contacted Ms. Solis by certified mail regarding participation specifically in the Latter Wells. Kraken gave her 30 days to voluntarily participate in the project. Consistent with her prior conduct, she never responded to the letters.

Clearly, Kraken's multiple attempts were "unsuccessful" within the meaning of Mont. Code Ann. § 82-11-202(1)(b). However, Phoenix argues Kraken's efforts were not in "good faith" because "'good faith' did require Kraken to accept Phoenix's offers to voluntarily pool the Minerals in the months before Kraken's Application." Appellant's Opening Brief (Br.) at 18 (emphasis in original). The problem is that Phoenix's "offers"—which in fact were attempts to accept

Kraken's offer—came too late. Kraken's offers had expired by their own terms, 30 days after they were delivered to Ms. Solis and more than a year before Phoenix attempted to accept. By that time, the offers were simply no longer on the table, and the acceptance was ineffective. As her successor in interest, Phoenix was bound by Ms. Solis's refusal to participate. As an operator that complied with its statutory duties, Kraken was entitled to rely on Ms. Solis's non-response in the planning of its legal and financial affairs. This is particularly the case because Phoenix was the party in the better position to "manage its relationship" with Ms. Solis and determine that she had given up the opportunity to participate. *See* D.C. Doc. 30, Ex. B at ¶ 23.

Phoenix argues that the district court's acceptance of "industry practices" as to the typical timing of an application for forced pooling is "expressly contradicted" by Mont. Code Ann. § 82-11-202(1)(b) and infers that Kraken acted in bad faith because it waited to make its application. Br. at 20–22. But as Phoenix itself says, Mont. Code Ann. § 82-11-202(1)(b) allows operators to "seek a pooling order at any time" after a permanent spacing unit is created. Br. at 21 (emphasis in original). The district court merely accepted that the "industry practice" is to wait until a well is completed to ensure that it is worth the expense of applying for forced pooling. *See* JA-1 at 9; JA-2 at 52:22-53:10. Because an operator can seek forced pooling "at any time" after the spacing unit is created, there is no "express

contradiction." And because Kraken relied on this common practice when it applied for forced pooling eight days after the Latter Wells were completed, Phoenix's speculative inference of neglect or bad faith, *see* Br. at 21–22, 34–35, is unwarranted and unfounded.

What Phoenix does not argue—because it could not—is that Ms. Solis never received Kraken's offers, or that she was misled about or misunderstood the offers in some way. Rather, the evidence shows that Kraken made every reasonable effort to involve Ms. Solis in the project, that Ms. Solis knew of the offer, and that she wanted no part of it. "Good faith" does not require Kraken to continue asking when it knows the answer, nor does it require Kraken to upend its own plans to accommodate Phoenix's late arrival.

Kraken made the "unsuccessful, good faith attempt" to voluntarily pool Ms. Solis's interest that is required by statute. Phoenix is bound by Ms. Solis's failure to participate. The Board correctly ordered forced pooling, and the district court correctly affirmed. This Court should affirm the district court's decision.

II. The Board correctly decided that Kraken is entitled to risk penalties.

A. Risk penalties are required where "an owner, after written demand, has failed or refused to pay" its share of costs.

Upon issuance of a forced pooling order where (as in this case) a well was drilled before the hearing, the Board "must" also authorize recovery of risk

penalties if the "owner, after written demand, has failed or refused to pay the owner's share of the costs of development or other operations[.]" Mont. Code Ann. § 82-11-202(2)(b). The penalty allows operators to recover the "costs of development or other operations" out of a non-participating owner's share of the production. *See* Mont. Code Ann. § 82-11-202(2)(a). It is intended to "encourage landowners to (1) voluntarily enter oil and gas agreements, (2) promote natural resource production, and (3) protect other landowners' correlative rights." D.C. Doc. 25, Ex. 1 at *64. Thus, risk penalties include up to 200 percent of certain categories of expenses. *See* Mont. Code Ann. § 82-11-202(2)(b)(i)-(ii). Until the penalty is recovered, the non-consenting mineral owner receives a "landowner royalty equal to one-eighth of the owner's proportionate share of production from the well." Mont. Code Ann. § 82-11-202(2)(c).

By the plain meaning of Mont. Code Ann. § 82-11-202(2)(b), if it finds that an operator is entitled to forced pooling, the Board "must" order risk penalties. The statute requires no second step of analysis step by the Board. *See* D.C. Doc. 25, Ex. 3 at 7 n.39 ("The forced pooling statute leaves no discretion to be exercised by the Board in the imposition of the non-joinder 'penalty' amounts.")

At most, subsection (2)(b) adds to subsection (1)(b) the requirement of a writing. The word "demand" cannot be read both literally and consistently with the statute. A "demand" is the "assertion of a legal or procedural right," BLACK'S LAW

DICTIONARY (9th ed. 2009), and under the Act, no operator has an absolute right to payment from an interest owner. This is evident from the statute itself: it does not entitle operators to owners' participation but prescribes a remedy where an owner does not participate. In other words, the operator has the right to *either* an interest owner's participation *or* the assessment of risk penalties, at the interest owner's election. Accordingly, to the extent a "written demand" is ambiguous in the context of subsection (2)(b), it is best understood as the operator's obligation to notify interest owners of the project, offer them one or more options to participate—including sufficient information for them to make an informed decision—and to give the owner adequate time to decide. At the hearing required for all such applications, *see* Mont. Code Ann. § 82-11-202(1)(b), Board members receive evidence, question witnesses, and use their industry expertise to assess the sufficiency of the attempt to voluntarily pool.

The other requirements of (2)(b) are functionally equivalent to the requirements of (1)(b): by definition, if the operator has made a sufficient "attempt" to voluntarily pool, it has made a "demand" (offer) for the purpose of risk penalties. Likewise, if the operator has been "unsuccessful" at obtaining voluntary pooling, the owner has "failed or refused to pay" for the purpose of risk penalties. To the extent that (2)(b) is ambiguous, a written offer is the only novel requirement.

B. Ms. Solis, upon written demand, failed or refused to pay her share of the costs of the Latter Wells.

1. Kraken sent a "written demand."

The January 2020 Letters constitute "written demands" to Ms. Solis to pay her share of the costs of the Latter Wells. As discussed above, *see supra*, Kraken could not literally "demand" payment, but it did describe the Latter Wells, offered Ms. Solis two different ways to participate, requested her response within 30 days by means of an enclosed election form, and warned her of the consequences of non-participation. In short, the January 2020 Letters are "written demands," as that phrase is best understood in this context.

Phoenix contends that the January 2020 Letters were not "written demands … to pay the owner's share of the costs" because they do not request immediate payment of a specific amount. *See* Br. at 30–31. This reading of subsection (2)(b) is flawed for two reasons. First, many interest owners elect to lease their interest, in which case they are not required to make any payment. The January 2020 Letters offered this option to Ms. Solis. *See* D.C. Doc. 25, Exs. 11–13 at ¶ 8. If Ms. Solis had accepted the offer to lease her interest, there would be no purpose served by including Kraken's exact costs, but she still would have been deemed a participating owner.

Second, Phoenix's reading undermines the purposes of the Act and leads to absurdity. Before a well is drilled—that is, at the time operators seek voluntary

pooling—operators do not yet have exact costs. Only estimates are available because the work has not yet been completed. But the purpose of risk penalties is to encourage voluntary pooling and reward those who undertake the risks of development. *See* D.C. Doc. 25, Ex. 1 at 6–7; D.C. Doc. 30, Ex. B at ¶ 23. If operators had to wait until an exact accounting was available before seeking owners' participation, the undertaking would no longer be risky—and there would be no need for forced pooling or risk penalties at all. *But see City of Missoula*, ¶ 22 (interpretation of one statute cannot invalidate others).

The more reasonable, consistent reading of (2)(b) is the operator must seek an owner's *agreement* to pay (or lease), rather than seeking immediate payment. This reading gives effect to all parts of the statutory scheme and gives appropriate deference to the Board's longstanding interpretation. *See Mont. Trout Unlimited*, ¶ 37; *see also* JA-2 at 58:3-5. Applications for forced pooling and risk penalties are very routine—"a huge part of [the Board's] docket," JA-2 at 26:15-17—and the language at issue has been part of subsection (2)(b) since 1993. Even so, no case challenging the Board's interpretation of a "written demand" has previously been filed. Accordingly, operators in Montana rely on the Board's interpretation when sending thousands of election packets per year to interest owners. Phoenix's reading is not only unsupported, but it would also throw oil and gas development in Montana into chaos. To the extent that subsection (2)(b)'s requirement of a

"written demand" for payment is ambiguous, the Board's reading is the simplest, most reasonable, and most consistent with the Act as a whole, and it is relied upon by operators throughout Montana.

2. Ms. Solis actually "failed or refused to pay" her share of costs, and no presumption is required.

There is no dispute that Ms. Solis did not participate in the drilling project: she "failed or refused" to pay her share of costs within the 30 days allotted in Kraken's January 2020 Letters. However, Phoenix argues that Kraken must comply with the requirements for a presumption of refusal stated in Mont. Code Ann. § 82-11-202(3), even though both Kraken's application for risk penalties and the Board's Order No. 74-2021 explicitly did not rely on the presumption. *See* D.C. Doc. 27, Ex. C at 15:28–31, 20:19–20, 23:38, 24:23–28; D.C. Doc. 27, Ex. J at BOGC 00050.

Subsection (3) was added to Mont. Code Ann. § 82-11-202 in 1993, not to create new substantive requirements of operators, but for the purpose of "clarifying when an owner is presumed to have refused to pay costs." Compiler's Comments, Mont. Code Ann. § 82-11-202; D.C. Doc. 23, Ex. D at 14:30–34. Locating mineral interest owners is often difficult, because over the years, many owners move without changing their address of record with the clerk and recorder where they own their interest. In some instances, the interests within the unit are held by hundreds of owners located all around the world. *See* Mont. Code Ann. § 82-11-

202(1)(a); JA-2 at 47:20–24, 63:24–64:5. This puts operators in the position of trying to contact interest owners with no way of knowing whether the owner has received their letter. In those instances, a statutory presumption becomes essential. It provides that:

> An owner is presumed to have refused to pay the owner's share of costs if prior to the spud date of the well, the owner fails to pay or agree in writing to promptly pay the share of the costs after notice by the well operator either:
> (i) acknowledged in writing by the owner as received; or
> (ii) sent at least 30 days prior to the spud date of the well to the owner by certified mail, addressed to the owner's address of record in the office of the clerk and recorder of the county where the well is to be drilled or to the owner's address on file with the board.

Mont. Code Ann. § 82-11-202(3)(a).

Phoenix's contentions, *see, i.e.,* Br. at 23–27, stem from its fundamental refusal to accept that the January 2020 Letters were not sent pursuant to Mont. Code Ann. § 82-11-202(3). It is true that the time frame for response stated in the Letters happens to be the same number of days after which the statutory presumption applies. Each letter gave Ms. Solis "thirty (30) days from the receipt of this letter to accept or reject [the] well proposal." *See* D.C. Doc. 25, Exs. 11–13 at ¶ 4. It is also true that the January 2020 Letters "contain the exact information required by subsection (3)." Br. at 26, 30. However, Phoenix ignores or disregards that 30 days is a standard response time in many situations, and that the information required by subsection (3) is basic descriptive information that any

investor would want to know. *See* Mont. Code Ann. § 82-11-202(3) (notices sent for purpose of the presumption must state "the location of the well, the projected depth and target formations, the anticipated costs of drilling and completing the well, and the anticipated spud date of the well"). None of the Letters cite subsection (3) or invoke the presumption. In this case, Kraken knew that it had the correct contact information for Ms. Solis, and it knew she had received (if not opened) its letters. It had no need to rely on the presumption in subsection (3).

Moreover, and contrary to Phoenix's insistence, nothing in Kraken's January 2020 Letters required Ms. Solis to respond before the wells were spudded. *But see* Br. at 25–27 ("while Kraken claims that it did not have to send the Notices 30 days prior to the spud date of the Wells, Solis only had until the spud date to pay or agree to pay under the statutory presumption in subsection (3)" (emphasis in original)). Kraken acknowledged as much at hearing before the district court: that it would have accepted Ms. Solis's response, had it come after the spud date for a particular well but before the 30-day period was up. *See* JA-2 at 72:10–17. Because Kraken did not rely on the presumption, the spud dates of the Latter Wells were irrelevant to the deadline set in the January 2020 Letters.

Absent the timeframe stated in Mont. Code Ann. § 82-11-202(3), Phoenix wonders, "when exactly was the mineral owner required to pay?" Br. at 28. The answer is simple: within the deadline set by the January 2020 Letters. Phoenix's

confusion does not warrant importing the text of subsection (3) into subsection (2)(b). If Phoenix desires a hard-and-fast rule within subsection (2)(b), it should petition the legislature. Until then, operators will continue to request owners' participation within a timeframe they set, and the Board will continue to use its industry expertise and experience to determine whether the opportunity to participate was sufficient.

Kraken made a "written demand," and Ms. Solis "failed or refused" to participate in the project. She actually "refused" to participate on the phone with Lindsey Meszaros, and she also "failed" to respond to the January 2020 Letters before the deadline they set. Phoenix is bound by that refusal and that failure. Importantly, there is no indication that Ms. Solis did not receive the letters; Kraken knew that it had the correct address. Therefore, neither the Board nor the district court needed to rely on any presumption to find that Ms. Solis chose not to participate. The Board correctly ordered risk penalties pursuant to Mont. Code Ann. § 82-11-202(2)(b), and the district court correctly affirmed. This Court should affirm the district court's decision.

OPENING ARGUMENT

III. The district court erred in excluding evidence of Ms. Solis's statements.

This Court does not reverse an erroneous evidentiary ruling unless a substantial right of the party is affected. Mont. R. Evid. 103(a). Therefore, if this

Court finds that Ms. Solis's failure to agree to participate within 30 days of receiving the January 2020 Letters is sufficient to find that she "failed or refused to pay" within the meaning of Mont. Code Ann. § 82-11-202(2)(b), then it need not reach this evidentiary issue. If, however, it cannot find that she "failed" to pay, then it must address whether evidence that she "refused" to pay is admissible.

The district court excluded Ms. Meszaros's testimony as hearsay but did not further explain its reasoning. *See* JA-2 at 90:25–91:4; JA-1 at 3. It appears to have relied on Phoenix's argument that "the definition of de novo" is that "[t]he Court gets to accept new evidence, new objections." JA-2 at 15:2–4; *but see* JA-2 at 56:5–16 (citing Mont. R. Evid. 103(a)(1)). This ruling was erroneous for two reasons. First, it applies an incorrect definition of "de novo": the issue was not preserved for appeal, and the court should not have considered it at all. Second, under the verbal act doctrine, the statement should have been ruled non-hearsay.

A. The objection was not preserved for appeal and plain error review is inappropriate.

"The rule is well established that this Court will not address an issue raised for the first time on appeal." *Stevens v. Novartis Pharms. Corp.*, 2010 MT 282, ¶ 78, 358 Mont. 474, 247 P.3d 244 (citations omitted). In other words, error cannot be predicated on the admission of evidence unless a "timely objection or motion to strike appears of record." Mont. R. Evid. 103(a)(1). An objection is timely if it is "made as soon as the grounds for the objection become apparent." *Kizer v.*

Semitool, 251 Mont. 199, 207, 824 P.2d 229, 234 (1991) (citing *McCormick on Evidence*, § 53 at 126 (3rd ed. 1984)). "Failure to make a timely and specific objection constitutes a waiver of the right to claim error on appeal and results in the evidence being treated the same as any other admissible evidence." *Hunt v. K-Mart Corp.*, 1999 MT 125, ¶ 10, 294 Mont. 444, 981 P.2d 275. "To hold otherwise would not only put the trial court in error on an issue which had not been presented to it for ruling, but would permit a litigant" to re-try its case. *Reno v. Erickstein*, 209 Mont. 36, 41, 679 P.2d 1204, 1207 (1984) (quoting *Rasmussen v. Sibert*, 153 Mont. 286, 295, 456 P.2d 835, 840 (1969)).

This rule applies even where the standard of review is de novo. *See Nat'l Cas. Co. v. Am/ Bankers Ins. Co.*, 2001 MT 28, ¶ 25, 304 Mont. 163, 19 P.3d 223; *State v. Akers*, 2017 MT 311, ¶ 10, 389 Mont. 531, 408 P.3d 142. "De novo judicial review" is "[a] court's nondeferential review of an administrative decision, [usually] through a review of the administrative record plus any additional evidence the parties present." BLACK'S LAW DICTIONARY (9th ed. 2009). Thus, while de novo review contemplates "new evidence," it does not contemplate "new objections" to evidence already admitted.

There is an exception for plain error review, under which a court may decide to take notice of errors "affecting substantial rights although they were not brought

to the attention of the [lower] court." Mont. R. Evid. 103(d). Under plain error review, a

> reviewing court may discretionarily review a claimed error not previously raised below which affects fundamental constitutional rights where failing to review it may result in a manifest miscarriage of justice, leave unsettled the question of the fundamental fairness of the proceedings, or compromise the integrity of the judicial process. A court's inherent power of plain error review should be used sparingly and only in exceptional cases meeting one of the criteria.

In re Transfer Terr. from Poplar Elem. Sch. Dist. No. 9 to Froid Elem. Sch. Dist. No. 65, 2015 MT 278, ¶ 18, 381 Mont. 145, 364 P.3d 1222 (citing *Paulson v. Flathead Conservation Dist.*, 2004 MT 136, ¶ 40, 321 Mont. 364, 91 P.3d 569). Therefore, before it decides an issue that was not properly preserved below, the court must first determine that plain error review is appropriate. *See In re Transfer*, ¶ 19.

Phoenix did not object to any portion of Ms. Meszaros's testimony before the Board. Therefore, it did not preserve the issue for review by the district court. The district court's review of the hearsay objection was "fundamentally unfair" to the Board, which acted as the "lower court" in this case and did not have the opportunity to consider the objection. *See In re Transfer*, ¶ 13; *see also Reno*, 209 Mont. at 41, 679 P.2d at 1207 *and Stevens*, ¶ 78. Before addressing the hearsay question, the district court should have addressed whether plain error review was appropriate in the circumstances. This alone is error sufficient to warrant reversal.

Furthermore, the district court could not have found that plain error review was appropriate. To the extent it has any, none of Phoenix's "substantial rights" of constitutional magnitude were at issue—only money. *Cf. Reno*, 209 Mont. at 42, 679 P.2d at 1207–08 ("Courts have typically confined the scope of the plain error doctrine to criminal cases, because the right to life and liberty is unquestionably substantial or fundamental."). There is no question about the fundamental fairness of these proceedings or the integrity of the judicial process in this case. Phoenix has had every opportunity to present its case. Simply put, this is not the "exceptional case" meriting plain error review. *See In re Transfer*, ¶ 18.

Phoenix waived the right to claim error on this issue, and Ms. Meszaros's testimony should have been treated as admissible. *See Hunt*, ¶ 10.

B. The verbal act doctrine applies, and the testimony is not hearsay.

Additionally, the district court erred in ruling that Ms. Meszaros's testimony was hearsay. If the court were going to consider the hearsay objection, it should have overruled the objection under the verbal act doctrine. *See* D.C. Doc. 36 at 8–10.

"Where the issue is the existence of a statement, not the truth of the matter asserted, Montana recognizes the verbal act doctrine." *In re Estate of Mead*, 2014 MT 264, ¶ 23, 376 Mont. 386, 336 P.3d 362. "It is applied, when … the utterance is an *operative fact* which gives rise to legal consequences." *Phillip R.*

Morrow, Inc. v. FBS Ins. Montana-Hoiness Labar, Inc., 236 Mont. 394, 398, 770 P.2d 859, 861 (1989) (emphasis in original). An "operative fact" is one "that affects an existing legal relation, [especially] a legal claim" or one "that constitutes the transaction or event on which a claim or defense is based." BLACK'S LAW DICTIONARY (9th ed. 2009). Therefore, "[u]nder the verbal act doctrine in Montana, statements may be admitted 'for the purpose of establishing the fact that the words had been said by defendant.'" *Phillip R. Morrow*, 236 Mont. at 399, 770 P.2d at 862 (quoting *State v. Collins*, 178 Mont. 36, 44, 582 P.2d 1179, 1183 (1978)). Statements admitted under the verbal act doctrine are non-hearsay evidence under Mont. R. Evid. 801(c). *See Phillip R. Morrow*, 236 Mont. at 400, 770 P.2d at 862.

For example, the Montana Supreme Court in *Phillip R. Morrow* adopted the reasoning of the Tenth Circuit, which deemed as non-hearsay the testimony offered by an insurance agent that a policyholder who caused a car accident had requested cancellation of his policy. 236 Mont. at 398–99, 770 P.2d at 861–62. "The *presence* or *absence* of such words and statements of themselves are part of the issues in the case. This use does not require a reliance by the jury or the judge upon the competency of the person who originally made the statements for the truth of their content." *Id.* (emphasis in original; quoting *Creaghe v. Iowa Home Mutual Casualty Co.*, 323 F.2d 981 (10th Cir. 1963)). In its own analysis, the *Phillip R.*

Morrow Court found that statements "characterized as 'Dan Fisher told me Kip Vanderverter told him, 'don't do business with Morrow,'" were not hearsay. 236 Mont. at 398–99, 770 P.2d at 861–62. The statements were "admissible to prove the existence of acts by Vanderverter to pressure Dan Fisher …, not for the truth of the matters asserted within them." *Id.* at 399–400, 770 P.2d at 862 (citing 6 J. Wigmore, *Wigmore on Evidence* § 1774 (Chadbourn Rev. 1976)). Finally, this Court found that the decedent's statement, "[N]o, that's my shaky handwriting" was admissible to acknowledge his signature on his will. *Estate of Mead*, ¶¶ 20, 24. "The statement's status as an acknowledgement is an operative fact because legal consequences flow from the fact's existence." *Id.* ¶ 24.

Ms. Solis's statement that she did not wish to participate in the drilling project is an operative fact from which legal consequences flow. Because Mont. Code Ann. § 82-11-202(1)(b) requires Kraken to make a "good faith attempt to voluntarily pool," and Mont. Code Ann. § 82-11-202(2)(b) imposes risk penalties when an owner "has failed or refused" to pay, Ms. Solis's statement to Ms. Meszaros had a legal effect. Her statement is not offered to prove some other fact, and her competence and true intention or meaning is irrelevant. The relevant fact is that the statement was made. Therefore, the district court erred in excluding Ms. Meszaros's testimony as hearsay.

CONCLUSION

Phoenix failed to do its due diligence before purchasing Ms. Solis's mineral interest in Richland County. If it had, it would have learned that beginning in 2017, Kraken made several "unsuccessful, good faith attempts" by phone and by mail to voluntarily pool Ms. Solis's interest. It would have learned that in January 2020, Kraken made specific "written demands" that explained the Latter Wells and offered multiple ways for Ms. Solis to participate in their drilling and production. And it would have learned that Ms. Solis steadfastly refused all of Kraken's advances, and that risk penalties had already attached to its new interest. Because Phoenix did not do its due diligence, it attempts to subvert the plain and established meaning of Mont. Code Ann. § 82-11-202 through misdirection, mischaracterization, and misplaced outrage. Its arguments should be rejected and the district court affirmed on the merits.

In the event this Court cannot find that Ms. Solis "failed" to participate in the Latter Wells for the purposes of Mont. Code Ann. § 82-11-202(2)(b), it should find evidence that she affirmatively "refused" to participate admissible. Phoenix's hearsay objection was not properly preserved for the district court's review, and moreover the evidence is not hearsay under the verbal act doctrine. The district court should be reversed on this limited evidentiary issue.

Respectfully submitted this 16th day of October, 2023.

AGENCY LEGAL SERVICES BUREAU

/s/ Liz Leman
LIZ LEMAN
Agency Legal Counsel

CERTIFICATE OF COMPLIANCE

Pursuant to Rule 11 of the Montana Rules of Appellate Procedure, I certify that this principal brief is printed with a proportionately spaced Times New Roman text typeface of 14 points; is double-spaced except for footnotes and for quoted and indented material; and the word count calculated by Microsoft Word for Windows is 8,547 words, excluding certificate of service and certificate of compliance.

/s/ Liz Leman
LIZ LEMAN
Agency Legal Counsel

CERTIFICATE OF SERVICE

I, Elizabeth Ann Leman, hereby certify that I have served true and accurate copies of the foregoing Brief - Appellee and Cross to the following on 10-16-2023:

Jeffery James Oven (Attorney)
490 N. 31st Street, Ste 500
Billings MT 59101
Representing: Kraken Oil and Gas LLC
Service Method: eService

Adrian Ann Miller (Attorney)
2812 1st Ave. N., Suite 225
Suite 225
Billings MT 59101
Representing: Phoenix Capital Group Holdings, LLC
Service Method: eService

Michelle Sullivan (Attorney)
PO Box 534
180 N. 9th Avenue
Forsyth MT 59327
Representing: Phoenix Capital Group Holdings, LLC
Service Method: eService

Brett L. Kvasnicka (Attorney)
P.O. Box 2529
490 N. 31st Street, Ste. 500
Billings MT 59103-2529
Representing: Kraken Oil and Gas LLC
Service Method: eService

Electronically signed by Rochell Standish on behalf of Elizabeth Ann Leman
Dated: 10-16-2023