

**STATE OF NEW MEXICO
ENERGY, MINERALS AND NATURAL RESOURCES DEPARTMENT
OIL CONSERVATION DIVISION**

**APPLICATIONS OF CIMAREX ENERGY CO.
FOR A HORIZONTAL SPACING UNIT AND COMPULSORY
POOLING, LEA COUNTY, NEW MEXICO**

Case Nos. 23448 – 23455

**APPLICATIONS OF CIMAREX ENERGY CO.
FOR COMPULSORY POOLING,
LEA COUNTY, NEW MEXICO**

Case Nos. 23594 – 23601

**APPLICATIONS OF READ & STEVENS, INC.
FOR COMPULSORY POOLING,
LEA COUNTY, NEW MEXICO**

Case Nos. 23508 – 23523

**CIMAREX ENERGY CO.'S CLOSING STATEMENT
WITH FINDINGS OF FACT AND CONCLUSIONS OF LAW**

Cimarex Energy Co. (“Cimarex”), through its undersigned attorneys, submits to the New Mexico Oil Conservation Division (“Division”) its Findings of Fact and Conclusions of Law that sets forth the facts established at the contested hearing of the above-referenced cases held August 9-11, 2023, between competing applicants Cimarex and Read & Stevens, Inc. (“Read & Stevens”) along with Read & Stevens’ designated operator, Permian Resources Operating, LLC (“Permian Resources”) (collectively referred to as “Permian Resources”) and then applies the relevant statutes, regulations, and Division and Oil Conservation Commission (“Commission”) precedent to those facts. The facts and the law establish that Cimarex’s development plan is superior to the plan proposed by Permian Resources and that it is the only plan that satisfies the Division’s statutory mandate to prevent waste, protect correlative rights, and avoid the costs and risks associated with drilling numerous unnecessary wells.

FINDINGS OF FACT

A. General Overview of the Competing Development Plans

1. Both parties are proposing to develop Sections 5 and 8, Township 20 South, Range 34 East. Cimarex's plan for these lands is named "Mighty Pheasant," while Permian Resources plan for these lands are named "Joker." Both parties are also proposing to develop Sections 4 and 9, Township 20 South, Range 34 East. Cimarex's plan for these lands is named "Loosey Goosey", while Permian Resources plan for these lands is named "Bane." These lands are collectively referred to as the "Subject Lands."

B. Cimarex's Development Plan

2. Cimarex has filed applications with the Division to drill four wells in the Bone Spring formation and one well in the 2nd Sand as part of its Mighty Pheasant plan and to drill the same number of wells with the same targets as part of its Loosey Goosey plan. However, Cimarex's development plan contemplates a total of four 1st Sand Bone Spring wells, three wells in the Upper 2nd Sand (contingent on data acquired from the 3rd Sand wells), four wells in the 2nd Sand, and four wells in the 3rd Bone Spring Sand for its Mighty Pheasant plan and the same number of wells with the same target zones for its Loosey Goosey plan.

3. Cimarex has made application for permits for the wells as early as February and March 2022. *See* Cimarex's Exhibit B, ¶ 7, Hearing Packet I; see also Exhibit B-2, Hearing Packet I. Cimarex has already conducted an onsite inspection with the BLM to confirm approval for its locations. *See* Tr. (DD 8-9-23) 227: 20-21; 228: 1.

4. Cimarex will develop the Subject Lands with only 33.9 acres of disturbance to the surface, consisting of 2.33 acres of roads, 25.24 acres for 4 drill pads and 6.31 acres for a

single battery, thus substantially minimizing the environmental impact of Cimarex's development plan. *See* Cimarex's Exhibit C, ¶ 9, Hearing Packet I (Self-affirmed Statement of Facility Engineer). Cimarex is keeping operations on-pad and using on-pad extensions for a more efficient connection to the flow lines. *See* Tr. (DD 8-9-23) 220: 10-18; 221: 5-9.

5. Cimarex's total costs for its 30 proposed wells is \$283,253,951.43. *See* Cimarex's Exhibit A-10, Hearing Packet I; Cimarex's Exhibit A, ¶ 33, Hearing Packet I; Cimarex's Exhibit A-3, Hearing Packet I. "Cimarex's proposal will deliver a top performer" as compared to all the co-development plans shown in Cimarex's Exhibit D-13, where both the Bone Spring and Wolfcamp formations were developed, thus providing "a greater return on investment and in terms of EUR."). *See also*: Cimarex's Exhibit D at ¶ 43, Hearing Packet I. Tr. (DD 8-10-23) 25: 17-25; 26: 1-2 (Cimarex's engineer explaining why only a single landing in the Third Bone Spring is needed to develop the reserves).

C. Cimarex's History of Development in the Area

6. Cimarex's development plan for the Subject Lands is part of a larger comprehensive plan for the area that Cimarex initiated and has been working on since before 2018. *See* Cimarex's Exhibit A-7, slides 1-4, in Hearing Packet I, for full outline of the Area of Interest that includes the Subject Lands; *see also* Cimarex's Exhibit A, ¶ 26, in Hearing Packet I (describing that the Area of Interest in 20 South, 34 East covers the Subject Lands (Sections 5 & 8 and 4 & 9), as well as Sections 6, 7, 17-20, and 29-33, all representing sections in which Cimarex has acquired 60 percent working interest ("WI") representing Cimarex's past and future plans for development of this general area). *See also*: Cimarex's Exhibit D-1, Hearing Packet I; Cimarex's Exhibit D, ¶ 10.

7. Cimarex has spud 104 wells in Lea County, including 79 wells with two-mile laterals when the available length allowed for 2-mile laterals and 25 one-mile wells when the lateral length was restricted. *See* Cimarex's Exhibit A-7, Slide 3, Hearing Packet I. In the Area of Interest, which includes the Subject Lands, Cimarex has drilled 35 wells in the Third Bone Spring Sand, starting in 2010 through 2022. *See* Cimarex's Exhibit B, ¶ 5, Hearing Packet; *see* also Cimarex's Exhibit D, ¶ 18, Hearing Packet I (Reservoir Engineer stating Cimarex has executed 15% of all well in the Area of Interest and whose results helped drive significant lateral investment in the Area).

8. Cimarex's reputation as a prudent operator is well-earned: for its 81 wells in Lea County during the period of 2018-2022, for the first 12 months of operations, Cimarex averaged 50,749 BOE per 1,000 ft of laterals (81 wells) and averaged 34,633 barrels of oil per 1,000 feet of laterals (81 wells), which ranked Cimarex in the top two operators. *See* Cimarex's Exhibits D-1 and D-2, Hearing Packet I. Permian Resources results were substantially below those of Cimarex. *Id.*

D. Permian Resource's Development Plan

9. Permian Resources has filed applications with the Division to drill a total of 48 wells: four wells in the Bone Spring formation, four wells in the Upper 2nd Sand, four wells in the 2nd Sand, eight Wells in the 3rd Bone Spring Sand, and four wells in the Upper Wolfcamp in its Bane plan and the same number of wells with the same target zones in its Joker plan. Permian Resources has not yet applied for permits for the wells it has proposed in its plan. *See* Tr. (DD 8-11-23) 25: 19-22. However, Permian Resources may not drill the eight Upper Wolfcamp wells based on the results that it is in the process of collecting from the Batman wells. Tr. (DD 8-10-23) 170: 5 to 172: 16. As of the date of the August 2023 hearing, Permian Resources had

only collected 60 days of production data from the Batman wells. *Id.* at 170: 5-19.

10. Permian Resources' total costs for its 48 wells is a slightly more than \$539 Million. Permian Resources' Exhibit C-10.

11. Permian Resources' proposed Upper Wolfcamp will not result in a significant increase in the overall production of hydrocarbons. Tr. (DD 8-10-23) 25: 17-25; 26: 1-2 (Cimarex's engineer explaining why only a single landing in the Third Bone Spring is needed to develop the reserves); Cimarex Exhibit D (Behm Direct Testimony) at ¶¶ 8, 37, 35, 48, 54, and 67 and Cimarex Exhibits D-9, D-11, D-16, D-18 through D-23. Permian Resources proposes to drill eight unnecessary wells in the Upper Wolfcamp that increase the costs of the plan by slightly more \$95 Million, *see* Cimarex Exhibit D-18, Hearing Packet I, without any significant increase to production or EUR. Cimarex Exhibit D (Behm Direct Testimony) at ¶¶ 8, 37, 35, 48, 54, and 67 and Cimarex Exhibits D-9, D-11, D-16, D-18 through D-23, Hearing Packet I.

12. Under Cimarex's plan for Option I, parties that own a greater interest in the Wolfcamp formation than the Bone Spring would nonetheless receive a greater return on their investment than what they would receive under Permian Resources' plan. *See* Cimarex Exhibit D (Behm Testimony) at ¶¶ 54-58 and Exhibits D-19 and D-20. Conversely, under Permian Resources' plan, owners who own in both the Bone Spring and Wolfcamp formations would receive a much lesser share of the total proceeds from production even if they owned a greater interest in the Wolfcamp formation than in the Bone Spring. *Id.* and Cimarex Exhibit D at ¶¶ 59-62 and Exhibits D-21 and D-22. For example, Sections 5 and 8 (Mighty Pheasant/Joker) MRC Permian, which has the largest ratio of ownership in Wolfcamp to Bone Spring, 3.0088, meaning that it owns 3 times more interest in the Wolfcamp than the Bone Spring, would still receive approximately \$20,044 more per acre PV10 under Cimarex's plan when compared to what it

would receive under Permian Resources' plan. Cimarex Exhibit D at ¶¶ 59-60 and Exhibit D-21. And HOG Partnership which owns more in the Wolfcamp than the Bone Spring by a factor 1.37, receives \$30,343 more PV10 per acre under Cimarex's plan for Option I than what it receives under Permian Resources' plan. Cimarex Exhibit D at ¶¶ 61-62 and Exhibit D-22. Permian Resources' development plan is uneconomical. Cimarex Exhibit D at ¶¶ 54-58; 67 and Cimarex Exhibits D-19 and D-20.

13. Permian proposes to drill ten unnecessary wells in the Bone Spring formation, consisting of two wells in the Upper 2nd Sand and eight wells in the 3rd Bone Spring, at a cost of slightly more than \$114 Million. Cimarex Exhibit D-18. In sum, between the cost of these additional 18 unnecessary wells and the higher AFEs proposed for its remaining 30 wells (eight wells in the First Sand, six in the Upper Second Sand, eight in the 2nd Sand, and eight in the 3rd Sand), the total cost of Permian Resources development plan is \$270 Million greater than Cimarex's (\$539 Million minus \$269 Million). Cimarex Exhibit D-18, Hearing Packet I.

14. Permian Resources plan is predicated on the false premise that its Third Bone Spring wellbores will produce only the Third Bone Spring pool and its Upper Wolfcamp wells will produce only the Upper Wolfcamp pool, a premise that is in no way supported by the actual geology. Cimarex's Exhibit B, Para. 30, Hearing Packet I; Tr. (DD 8-9-23) 154: 18-21; 155: 1-4. However, Permian Resources knew that there would be communication and mixing of hydrocarbons between the two formations. *See* Tr. (DD 8-10-23) 181: 2-4 (Permian Resources' Reservoir Engineer acknowledging that there will be communication and mixing of hydrocarbons between the two formations).

E. Permian Resources' History of Development in the Area

15. Permian Resources, designated as the operator in the competing applications, has presented Read & Stevens to the Division as the actual applicant in all the pooling applications submitted for its proposed development of the Subject Lands. *See* Pooling Applications filed by Read & Stevens in Case Nos. 23508 – 23523. Read & Stevens has had a long history of engaging in bad faith negotiations with Cimarex resulting in delays and disruptions of Cimarex's plans and progress for developing this area. *See* Cimarex Exhibit A, ¶ 29, Hearing Packet I. Cimarex would have developed the Subject Lands much earlier in time but for Read & Stevens unjustified claim that Magnum Hunter Production, Inc. ("Magnum Hunter"), a subsidiary of Cimarex, had no right to be the operator under an existing Operating Agreement dated August 1, 1979 ("1979 OA"). This bad faith tactic was successful since it tied Cimarex up in court with costs and time -- *See id.*; *see also* Cimarex's Exhibit A-8 in Hearing Packet I.

16. After Cimarex prevailed in court and was elected under the 1979 OA to operate the Subject Lands, Read & Stevens continued to reject the order of the court and refused to acknowledge the legitimacy of Cimarex's right to operate under the 1979 OA. Instead, Read & Stevens began spudding unauthorized wells, without submitting well proposals to Cimarex, and set casing for each of their wells in parts of the Subject Lands now under review; specifically in Section 9, Read & Stevens spudded the North Lea 9 Federal 2H (API No. 30-025-4375) in the 3rd Bone Spring and the North Lea 4 Fed Com 2H (API No. 30-025-43504) also in the Bone Spring formation. *See* Cimarex Exhibit A, ¶¶ 28-39, Hearing Packet I. Read & Stevens bad faith antics over the years has consumed an inordinate amount of time and resources and has caused substantial delay in Cimarex's development of the Subject Lands. *See id.* at ¶¶ 30 – 32. *See* Cimarex's Exhibit A at ¶¶ 28-30.

17. Permian Resources claims that these bad faith negotiations, which it does not

deny and are part of the history of development, occurred prior to its recent acquisition of Read & Stevens and therefore should not be considered in the Division's review for operatorship. *See* Tr. (DD 8-11-23) 34:18-25; 35: 1-9 (Permian Resources' landman acknowledging the strife between Read & Stevens and Cimarex and stating he was not personally acquainted with the history). Cimarex would have been able to develop the Subject Lands much earlier, prior to Permian Resources' acquiring the interests and submitting competing application "but for" Read & Stevens improper behavior. *See id.* at ¶¶ 30 – 32; *see also* Tr. (DD 8-9-23) 31: 8-25; 32: 1-25; 120: 15-21; 121: 1-11.

18. Read & Stevens acquired and owned interest in the Subject Lands with the intent to develop them. Over the years, Read & Stevens engaged in bad faith actions and negotiations that delayed and prevented Cimarex from developing the lands, including failed and unjustified attempts to sue Cimarex in court, illegitimately spudding and casing wells, without the consent of members to the 1979 OA, and disregarding terms of the governing 1979 OA. Findings of Fact at ¶ X,

19. Permian Resources entered into New Mexico as a new operator and has been active in the area only over the past several years and during that time has drilled only five wells in this Area of Interest. *See* Permian Resources' Exhibit C, ¶ 31; Tr. (8-11-23) 18: 5-10; 19: 2-8.

F. Geological Features of the Subject Lands

20. The controlling feature of the geology underlying the Subject Lands, as recognized by both parties' geologists, is that the Third Bone Spring formation and the Upper Wolfcamp formation lack frac baffles between the two formations. *See* Tr. (DD 8-9-23) 153: 13-15; *see also* Tr. (DD 8-10-23) 206: 16-19 (Mr. Bradford, Permian Resources' geologist

agreeing with Cimarex's geologist that there are no frac baffles between the Third Bone Spring and Upper Wolfcamp).

21. Because of the lack frac baffles between the two formations, the Third Bone Spring formation and the Upper Wolfcamp formation are essentially "one continuous reservoir interval" with substantial communication of hydrocarbons between the formations. *See* Cimarex's Exhibit B at ¶ 30; Tr. (DD 8-9-23) 154: 18-21; 155: 1-4 (Cimarex's geologist explaining there are two formations but one continuous reservoir between the two); *see also* Tr. (DD 8-10-23) 206: 11-15 (Permian Resources' geologist agreeing with Cimarex's geologist that there is substantial communication of hydrocarbons between the Third Bone Spring and Upper Wolfcamp); Tr. (DD 8-10-23) 181: 2-4 (Permian Resources' Reservoir Engineer acknowledging that there will be communication of hydrocarbons between the two formations).

22. The vast majority of units in this Area of Interest have been developed in the Third Bone Spring formation. *See* Cimarex's Exhibit D-1, Hearing Packet I. Operators are aware that, in this specific area, if the Bone Spring formation is developed and produced, then it becomes uneconomical to co-develop the Wolfcamp formation, an awareness that is reflected in the pattern of development in this area. *Id.*

23. The primary concentration of reserves in the single common source of supply resides in the Third Bone Spring. *See* Cimarex Exhibit B, ¶ 30, Hearing Packet I (Cimarex geologist testifying that "Cimarex's proposed 3rd Bone Spring single landing is the optimal proposal based on the geology of the target area"). Based on an assessment of PhiH porosity which can show a certain type of measurement of percentages of production that would come from the Third Bone Spring, currently estimated, based on Cimarex's plan for Option II, at 72.8%, while it is currently estimated that 27.2% of production would come from the Upper

Wolfcamp. *See* Cimarex's Exhibit B at ¶ 15; *see also* Cimarex's Exhibit B-10; Tr. (DD 8-10-23) (Permian Resources' geologist stating that PhiH is "a very good way to show where the reservoir tank is in a geologic formation").

24. Fracs from wells drilled in the Upper Wolfcamp would extend into and produce the Third Bone Spring. Tr. (8-10-23) 56: 3-13. Permian Resources' Reservoir Engineer admitted that Permian Resources' Bone Springs wells will produce hydrocarbons from the Upper Wolfcamp and its Upper Wolfcamp wells will produce hydrocarbons from the Third Bone Spring formation. *See* Tr. (DD 8-10-23) 181: 2-4. Permian Resources' Upper Wolfcamp wells will produce primarily from the Third Bone Spring Sand, production that could permanently damage the Third Bone Spring formation by reducing the amount of reserves recoverable from the Third Bone Spring by subsequent development. *See* Cimarex's Exhibit B at ¶ 30.

25. Thus, under these particular geological conditions, the most efficient way to produce the reservoir is by drilling only the Third Bone Spring and not the Upper Wolfcamp; completing horizontal wells in the Upper Wolfcamp would constitute a wasteful expenditure of capital that would add significant risk without adding to the overall production of hydrocarbons. *See* Cimarex's Exhibit B at ¶ 30 in Hearing Packet I (geologist testifying that "Cimarex's proposed 3rd Bone Spring single landing is the optimal proposal based on the geology of the target area"); *see also* Cimarex's Exhibit D-19 in Hearing Packet I (showing that Permian Resources plan is wastefully over drilled while capturing negligible additional reserves); Cimarex's Exhibit D at ¶ 43 in Hearing Packet I (Cimarex's Reservoir Engineer testifying that "Cimarex's proposal will deliver a top performer" as compared to all the co-development plans shown in Cimarex's Exhibit D-13 thus providing "a greater return on investment and in terms of

EUR.”)

26. The written direct testimony of Ira Bradford, Permian Resources’ geologist, fails to acknowledge the lack of frac baffles. *See* Permian Resources’ Exhibit E. Although he fails to acknowledge the lack of frac baffles between the two formations in his written testimony, his exhibits illustrate the undisputable fact that there is an absence of frac baffles between the formations that necessarily will result in a significant amount of communication of hydrocarbons between the formations. *See* Tr. (DD 8-9-23) 154:1-6 (Ms. Mueller explaining that Mr. Bradfords Exhibit E5 shows a lack of frac baffles). Furthermore, under cross examination, Mr. Bradford not only acknowledged the absences of frac baffles but also agreed that their absence means that there will be communication of hydrocarbons between the formations. *See* Tr. (DD 8-10-23) 206: 11-15.

G. Controlling Ownership of the Subject Lands

27. Cimarex has the majority and controlling percentage of WI in the Subject Lands, both in the Bone Spring and Wolfcamp. *See* Permian Resources’ Supplemental Exhibit I; *see also* Tr. (8-11-23) 37:1-25; 38: 1-9 (Permian Resources’ landman confirming that Cimarex has the majority and controlling interest in both the Bone Spring and Wolfcamp). In the Bone Spring formation where the single common source of supply primarily resides, Permian Resources acknowledges that Cimarex, with the support of its committed owners, controls a majority of 50.23% of the WI in the four sections of the Subject Lands (1287.03 acres out of 2162.77 acres) , while Permian Resources controls only 34.18% of the WI in the Subject Lands (875.74 acres). *See* Permian Resources’ Supplemental Exhibit I at p. 2. With respect to the Wolfcamp formation, Permian Resources acknowledges that Cimarex, with the support of its committed owners, controls 41.80% of the WI (1070.97 acres out of 2162.77 acres, while

Permian Resources controls 39.48% of the WI (1011.59 acres). *Id.*

28. CLM Production and Warren Associations (collectively referred to herein as “Warren”) own a very small percentages (0.00125%) in the Upper Wolfcamp but own no interest in the Bone Spring.

CONCLUSIONS OF LAW

- 1. Permian Resources’ applications to develop the Subject Lands are fatally and incurably flawed because when Permian Resources did not possess the requisite intent to develop the Subject Lands as set forth in those applications.**

When Permian Resources filed its competing applications, its plan to develop the Subject Lands was inchoate because it was contingent on accumulating additional data from its Batman wells to justify the drilling of the eight (8) Upper Wolfcamp Wells. Findings of Fact at ¶ 9. However, as of the August hearing dates, Permian Resources had only collected 60 days of production from the Batman wells. *Id.* Thus, when Permian Resources filed its applications for the eight Upper Wolfcamp Wells on April 13, 2023, it did not have any data from the Batman wells on which it will base its decision to actually drill the Wolfcamp wells.

Because Permian Resources’ development plan has been subject to change from the time it filed its applications, and remains in a state of flux, the Division cannot apply the comparative criteria in any meaningful way to determine whether Permian Resources’ development is superior to Cimarex’s. This fatal flaw is not curable at this stage of the proceedings because the time for filing competing applications against Cimarex’ development plan has long passed.

Thus, the Division must dismiss Permian Resources’ applications with prejudice and limit its inquiry to the question of whether Cimarex’s development plan meets the criteria set forth in the Oil and Gas Act, NMSA 1978, § 70-2-1, *et seq.*

2. Cimarex's development plan is superior to Permian Resources' plan.

When faced with competing development plans, the Division bases its determination of which plan best satisfies the Division's statutory obligation to ensure that proposed oil and gas operations prevent waste, protect correlative rights, and to avoid of the costs and risks associated with drilling numerous unnecessary wells through the application of the following seven (7) factors ¹:

- a. *A comparison of geologic evidence presented by each party as it relates to the proposed well location and the potential of each proposed prospect to efficiently recover the oil and gas reserves underlying the property.*

Cimarex is the only operator in these proceedings that has closely analyzed and evaluated the dispositive characteristics and nature of the geology under the Subject Lands and that has utilized its analysis in a good faith manner to locate and position its wells in order to achieve optimal production without excessive and unnecessary costs and without the drilling of numerous unnecessary wells.

The controlling feature of the geology underlying the Subject Lands, as recognized by both parties' geologists, is that the Third Bone Spring formation and the Upper Wolfcamp formation lack frac baffles between the two formations. Findings of Fact at ¶ 20. Because of the lack of frac baffles between the two formations, the Third Bone Spring formation and the Upper Wolfcamp formation are essentially "one continuous reservoir interval" with substantial communication of hydrocarbons between the formations. *Id.* at ¶ 21. Thus, under these particular geological conditions, the most efficient way to produce the reservoir is by drilling only the Third Bone Spring and not the Upper Wolfcamp. *Id.* at ¶¶ 5 and 21. Completing

¹ See, e.g., OCD Order No. R-21834 (The OCD evaluated the parties' development plans based on these seven factors); OCC Order No. R-21416-A (The OCC evaluated competing plans on the same seven factors as the OCD).

horizontal wells in the Upper Wolfcamp would constitute a wasteful expenditure of capital that would add significant risk without adding to the overall production of hydrocarbons. *Id.* at ¶ 11.

The written direct testimony of Ira Bradford, Permian Resources' geologist, fails to acknowledge the lack of frac baffles. *Id.* at ¶ 26. Mr. Bradford ignores this critical and dispositive geological feature because it undercuts Permian Resources' proposed drilling and development of the Third Bone Spring and Upper Wolfcamp that is premised on the misguided and incorrect assumption that the two formations represent two separate reservoirs. *Id.* Although he fails to acknowledge the lack of frac baffles between the two formations in his written testimony, his exhibits illustrate the undisputable fact that there is an absence of frac baffles between the formations that necessarily will result in a significant amount of communication of hydrocarbons between the formations. *Id.* Furthermore, under cross examination, Mr. Bradford not only acknowledged the absences of frac baffles but also agreed that their absence means that there will be communication of hydrocarbons between the formations. *Id.*

In sum, Cimarex has designed its development plan to account for the lack of frac baffles, a dispositive feature of the geology. As a result, Cimarex's plan prevents waste, protects correlative rights, and proposes the optimal location of its wells which, under the specific geologic features found in the Subject Lands, is in the Third Bone Spring and not the Upper Wolfcamp.

In stark contrast, Permian Resources, while aware of the lack of frac baffles, fails in its plan to account for this geological feature that should be the driving factor underlying any development plan proposed for the Subject Lands. As a result of its willful failure to recognize and embrace the specific geological features of the Subject Lands, Permian Resources has

proposed a plan that creates substantial waste by proposing an excessive number of unnecessary wells to be drilled into the Upper Wolfcamp that will not result in an increase in the overall production of hydrocarbons. *Id.* at ¶ 11. Moreover, Permian Resources' plan undermines correlative rights because it places a significant economic burden on the owners of working interests and violates 19.15.12.9 NMAC without any means for remediating its violation, as described below.

b. A comparison of the risk associated with the parties' respective proposal for the exploration and development of the property.

Avoiding the drilling of unnecessary wells is listed in the pooling statute as the first of the three reasons for pooling interests in a unit. *See* NMSA 1978, § 17-2-17(C). The Division is required under the Act and its statutes to avoid the drilling of unnecessary wells in order to minimize the increase and "augmentation of risks arising from the drilling of an excessive number of wells." *Id.* at § 70-2-17(B).

Permian Resources proposes to drill a total of 48 wells to develop the hydrocarbons underling the subject lands. Finding of Facts at ¶ 9. Eight of these wells are unnecessary because they are proposed in the Upper Wolfcamp formation and will not result in any meaningful increase in the overall production of hydrocarbons. *Id.* at ¶ 11. In comparison, Cimarex's plan will efficiently develop the hydrocarbons underlying the Subject Lands with only 30 well, 18 less than Permian Resources. *Id.* at ¶ 5. Thus, Cimarex's plan significantly reduces both the overall costs and the increased risks of drilling an additional 18 wells, which will not add to overall production in any meaningful sense.

Therefore, Cimarex's plan is the better plan under the Act because it is the only development plan that avoids over drilling and the significant costs and risks inherent to drilling numerous unnecessary wells.

- c. *A review of the negotiations between the competing parties prior to the applications to force pool to determine if there was a “good faith” effort.*

Cimarex’s development plan for the Subject Lands is part of a larger comprehensive plan for the area that Cimarex initiated and has been working on since before 2018. Findings of Fact at ¶¶ 6-7.

Permian Resources, designated as the operator in the competing applications, has presented Read & Stevens to the Division as the actual applicant in all the pooling applications submitted for its proposed development of the Subject Lands. *Id.* at ¶ 15. Read & Stevens has had a long history of engaging in bad faith negotiations with Cimarex resulting in delays and disruptions of Cimarex’s plans and progress for developing this area. *Id.* Cimarex would have developed the Subject Lands much earlier in time but for Read & Stevens’ unjustified claim that Magnum Hunter Production, Inc. (“Magnum Hunter”), a subsidiary of Cimarex, had no right to be the operator under an existing Operating Agreement dated August 1, 1979 (“1979 OA”). This bad faith tactic was successful since it tied Cimarex up in court with costs and time. *Id.*

After Cimarex prevailed in court and was elected under the 1979 OA to operate the Subject Lands, Read & Stevens continued to reject the order of the court and refused to acknowledge the legitimacy of Cimarex’s right to operate under the 1979 OA. *Id.* at ¶ 16. Instead, Read & Stevens began spudding unauthorized wells, without submitting well proposals to Cimarex, and set casing for each of their wells in parts of the Subject Lands now under review; specifically in Section 9, Read & Stevens spudded the North Lea 9 Federal 2H (API No. 30-025-4375) in the 3rd Bone Spring and the North Lea 4 Fed Com 2H (API No. 30-025-43504) also in the Bone Spring formation. *Id.* Read & Stevens bad faith antics over the years has consumed an inordinate amount of time and resources and has caused substantial delay in Cimarex’s development of the Subject Lands. *Id.*

Permian Resources claims that these bad faith negotiations, which it does not deny and are part of the history of development, occurred prior to its recent acquisition of Read & Stevens and therefore should not be considered in the Division's review for operatorship. *Id.* at ¶ 17. However, Permian Resources' attempt to whitewash away Read & Stevens' history of bad faith should not be countenanced because "but for" the history of Read & Stevens' bad faith actions over the years, Cimarex would have been able to develop the Subject Lands much earlier, prior to Permian Resources' acquiring the interests and submitting competing application. *Id.*

Furthermore, under New Mexico law, if a corporation acquires another company or entity, it also acquires that transferor's "dirty laundry" if acquiring company continues the business of the acquired entity. *Garcia v. Coe Mfg. Co.*, 1997 NMSC 13, ¶ 12, 933 P.2d 243, 247. Thus, when Permian Resources acquired Read & Stevens and continued Read & Stevens' business, it also acquired Read & Stevens' history of unseemly and unsavory business practices. *TVSLR LLC v. NM Taxation Revenue Dept.* No. A-1-CA-37587, ¶ 19 (NM App 2021) (the transfer of the corporation to another entity is a mere continuation of the transferor's business if it is the same business); *EEOC v. Roark-Whitten Hosp* 28 F.4th 136, 146-47 (10th Cir.) (purchasing corporation subject to selling corporation's liabilities where the purchasing corporation is merely a continuation of the selling corporation).

Read & Stevens acquired and owned interest in the Subject Lands with the intent to develop them. Over the years, Read & Stevens engaged in bad faith actions and negotiations that delayed and prevented Cimarex from developing the lands, including failed and unjustified attempts to sue Cimarex in court, illegitimately spudding and casing wells, without the consent of members to the 1979 OA, and disregarding terms of the governing 1979 OA. Findings of Fact at ¶ 16. Permian Resources, after acquiring its interests in the Subject Lands, continues Read &

Stevens efforts to develop the Subject Lands by making Read & Stevens itself the applicant for its pooling applications, thereby directly benefiting from Read & Stevens' bad faith actions and efforts that have provided Permian Resources with the ill-gotten opportunity to compete for operatorship.

Thus, in order to fulfill the Division's policy of not awarding bad faith negotiations, it should not allow Permian Resources to obtain any benefit related to Read & Stevens' bad faith actions and negotiations in these matters.

d. A comparison of the ability of each party to prudently operate the property and, thereby, prevent waste.

Cimarex has a long history and track record as a prudent operator in Lea County, as evidenced by the fact that it has been drilling wells and developing lands in Lea County and the Area of Interest, that includes the Subject Lands, since before 2018, and is one of the leading developers and producers in the Area of Interest. *Id.* at ¶¶ 6-8.

Cimarex has spud 104 wells in Lea County, including 79 wells with two-mile laterals when the available length allowed for 2-mile laterals and 25 one-mile wells when the lateral length was restricted. *Id.* at ¶ 7. In the Area of Interest, which includes the Subject Lands, Cimarex has drilled 35 wells in the Third Bone Spring Sand, starting in 2010 through 2022, which is 15% of all wells in the Area of Interest and whose results helped drive significant lateral investment in the Area. *Id.*

Cimarex's reputation as a prudent operator is well-earned: for its 81 wells in Lea County during the period of 2018-2022, for the first 12 months of operations, Cimarex averaged 50,749 BOE per 1,000 ft of laterals (81 wells) and averaged 34,633 barrels of oil per 1,000 feet of laterals (81 wells), which ranked Cimarex in the top two operators. *Id.* at ¶ 8. Cimarex's proven history of superior performance, coupled with its development plan that takes into account the

lack of frac baffles in the Subject Lands probably explains the fact that the majority of WI owners in the Subject Lands support Cimarex's development plan. *Id.* at ¶ 27.

Furthermore, for the wells Cimarex has proposed in the present cases, it has made application for permits for the wells as early as February and March 2022 and has already conducted an onsite inspection with the BLM to confirm approval for its locations. *Id.* at ¶ 3.

In contrast, Permian Resources entered into New Mexico as a new operator and has been active in the area only over the past 2 to 3 years during which time it has drilled 5 wells in this Area of Interest. *Id.* at ¶ 19.

The history of each party's development in the Area of Interest and in Lea County, coupled with the fact that Permian Resources' plan costs a quarter of a billion dollars more than Cimarex's plan - representing a grossly excessive and unnecessary economic waste - establish that Cimarex is the party that has shown more initiative and has been more prudent in its preparations for its proposed wells.

e. A comparison of the differences in well cost estimates (AFE's) and other operational costs presented by each party for their respective proposals.

In most cases, when the Division is presented with competing development plans for the same lands, the difference in cost estimates is minor or only vary by 15% to 20% at the most. However, the price tags of the two competing development plans for the Subject Lands in the present cases vary by more than 50%, with Cimarex at a reasonable approximate cost of \$283,253,951.43 to drill and operate its 30 wells and Permian Resources' costs at approximately a quarter of a billion dollars more than Cimarex's costs for the drilling and operation of its 48 wells. Findings of Fact at ¶¶ 5 and 10. To characterize this difference as substantial is an understatement. The difference in capital expenditures between the two plans boldly emphasizes the fact that Cimarex accounts for the actual geology of the Subject Lands that results in it being

able to provide a significantly more efficient and economical development plan than that proposed by Permian Resources. The development plan that Permian Resources champions would result in the drilling of an excessive number of unnecessary wells at enormous costs, a waste of resources caused by its willful disregard of the actual geology.

f. An evaluation of the mineral interest ownership held by each party at the time the application was heard.

Cimarex has the majority and controlling percentage of WI in the Subject Lands, both in the Bone Spring and Wolfcamp. *Id.* at ¶ 27. In the Bone Spring formation where the single common source of supply primarily resides, Permian Resources acknowledges that Cimarex, with the support of its committed owners, controls a majority of 50.23% of the WI in the four sections of the Subject Lands (1287.03 acres out of 2162.40 acres), while Permian Resources controls only 34.18% of the WI in the Subject Lands (875.74 acres). *Id.* With respect to the Wolfcamp formation, Permian Resources acknowledges that Cimarex, with the support of its committed owners, controls 41.80% of the WI (1070.97 acres out of 2162.40 acres), while Permian Resources controls 39.48% of the WI (1011.59 acres). *Id.*

Cimarex also owns contractual interests based on the pre-existing 1979 OA that favors Cimarex. Permian Resources suggests that the Division by statute prefers leasehold WI interest over contractual WI interest, but there is no basis for this suggestion. Under the Act, an “owner” of a working interest is defined as “the person who has the right to drill into and produce from any pool and to appropriate production either for the person or for the person and another.” NMSA 1978, §70-2-33(E). Both a person with a leasehold WI interest not subject to any contractual rights and a person with contractual WI satisfies this definition as both owners have the right to drill into and produce from any pool and appropriate production. Furthermore, both

forms of WI must be pooled under the pooling statute. *See* §70-2-17(C) (shall pool all or any part of such lands or interests or both) (emphasis added).

Cimarex continues to make efforts to acquire interest to increase and fortify its controlling percentages.

- g. A comparison of the ability of the applicants to timely locate well sites and to operate on the surface ("surface factor").*

As noted above, Cimarex has already received its drilling permits granting permission to spud its wells, while Permian Resources has not. Furthermore, Cimarex will develop the Subject Lands with only 33.9 acres of disturbance to the surface, consisting of 2.33 acres of roads, 25.24 acres for 4 drill pads and 6.31 acres for a single battery, thus substantially minimizing the environmental impact Cimarex's development plan. Findings of Fact at ¶ 4. Cimarex is able to use a single tank battery for both its Options I and II because it has accounted for allocation and segregation of production from the formations, as described in Section 4, below.

Permian Resources also intends to use a single tank battery, but as described below in Section 3, Permian cannot obtain approval for commingling under Rule 19.15.12.9(C) and therefore would not be able to utilize a single tank battery.

Furthermore, Cimarex has already conducted an onsite inspection with the BLM to confirm approval for its locations. *Id.* at ¶ 3. In addition, Cimarex is keeping operations on-pad and using on-pad extensions for a more efficient connection to the flow lines. *Id.* at ¶ 4.

Based on the foregoing, Cimarex respectfully submits that it prevails over Permian Resources in all seven factors, (a) through (g).

3. Permian Resources plan irremediably violates 19.15.12.9 NMAC

At the conclusion of the contested hearing, Examiner Garcia requested that the parties address the applicability of 19.15.12.9 NMAC to this contested proceeding. *See* Tr. (DD 8-11-

23) 82: 12-25. For the reasons set forth below, Cimarex's plan, in both its Option I and II modes, conforms to the requirements of Rule 19.15.12.9, while Permian Resources' plan not only violates the Rule but cannot be brought into compliance with the Rule.

As a starting point, both parties agree that there is a lack of frac baffles between the Third Bone Spring formation and the Wolfcamp formation. Findings of Fact at ¶ 20. As a result of this geologic feature, the parties acknowledge that there will be substantial communication of hydrocarbons between the formations. *Id.* at ¶ 21. Cimarex estimates that production from its Third Bone Spring could consist of up 27.2% of hydrocarbons from the Upper Wolfcamp. *Id.* at ¶ 23. Permian Resources' Upper Wolfcamp wells will produce primarily from the Third Bone Spring Sand, production that could permanently damage the Third Bone Spring formation by reducing the amount of reserves recoverable from the Third Bone Spring by subsequent development. *Id.* at ¶ 24.

Rule 19.15.12.9(A) requires an operator to "produce each pool as a single common source of supply and complete, case, and maintain and operate wells in the pool as to prevent communication within the wellbore with other pools." In this case, because there will be communication between the Third Bone Spring pool and the Upper Wolfcamp pool, the only way to meet the requirements of Rule 19.15.12.9 is to obtain the Division's approval for an exception to the segregation requirement of Rule 19.15.12.9(A). Exceptions are only available if an operator can satisfy the requirements for approval for either surface commingling or downhole commingling. *See* 19.15.12.9(C) NMAC; *see also* 19.15.12.10 NMAC and 19.15.12.11 NMAC.

Under its development plan, Permian Resources will drill both the Third Bone Spring formation and the Upper Wolfcamp formation of the Subject Lands, with a set of wells drilled

into the Third Bone Spring in close proximity with a set of wells drilled into the Upper Wolfcamp. Because Permian Resources will force pool and drill into both formations as separate pools, they will be producing directly both formations, not producing just one formation with incidental drainage from the adjacent formation.² Once an operator spaces and pools a formation, the extraction of hydrocarbons from that formation shifts under the Act from drainage to production. *See* §70-2-17(C); *see also* Cimarex's Brief at p. 8.

Since Permian Resources will produce from two adjacent formations that lack frac baffles and thus experience communication and commingling of hydrocarbons, it is impossible for Permian Resources to "produce each pool as a single common source of supply," and thus, it is impossible for it to "complete, case, maintain, and operate [its] wells in [each] pool so as to prevent communication within the well bore with other pools." *See* 19.15.12.9(A) NMAC. Once Permian Resources completes its wells in the Third Bone Spring and Upper Wolfcamp formations and starts producing from both formations, Permian Resources' Third Bone Spring wells will not only produce a physically unmeasurable and therefore unknown amount of hydrocarbons from the Third Bone Spring, the Third Bone Spring wells will also commingle and produce a physically unmeasurable and therefore unknown amount of hydrocarbons from the Upper Wolfcamp formation. Likewise, Permian Resources' Upper Wolfcamp will produce and commingle unmeasurable and therefore unknown amounts from both the Third Bone Spring and Upper Wolfcamp formations. Thus, Permian Resources will not be able to segregate the oil or gas produced from each pool, and consequently, will be in direct violation of Rule

² *See* Cimarex Energy Co.'s Brief Providing the Basis for Evaluating a Single Reservoir Situated in the Third Sand of the Bone Spring Formation in an Area that Lacks a Baffle Separating it from the Underlying Wolfcamp Formation ("Brief"), pp. 6 – 10 (discussing how the Pooling Statutes under the Act distinguishes between "production" and "producing," on the one hand, and "drainage," on the other, as two different and precisely defined categories).

19.15.12.9. Basically, by drilling, fracing, and producing both the Third Bone Spring and Upper Wolfcamp in such close proximity, Permian Resources will be creating one giant blender that mixes and commingles production without any possibility for distinguishing or measuring the production from each formation and pool, as Permian Resources plan is premised on the assumption, fully contradicted by the actual geology of the Subject Lands, that there are two pools because there are two formations.

This is the fatal, irremediable flaw of Permian Resources plan -- by completing Third Bone Spring and Upper Wolfcamp wells in close proximity that will be commingling production by simultaneously capturing hydrocarbons from both formations -- there is no means of allocating hydrocarbons between the two formations. Permian Resources' geologist was aware of the lack of frac baffles. Findings of Fact at ¶¶ 20 and 21. However, Permian Resources did not request approval for or mention commingling in its pooling applications. *See* Permian Resources' Exhibit A.

Even if Permian Resources had requested approval to commingle in its applications, such a request would have been futile. In order to qualify for surface commingling, an operator must provide the Division with some acceptable and measurable means of allocating the production to the various pools to be commingled. *See* 19.15.12.10(A)(1) NMAC. Because Permian Resources is drilling both the Third Bone Spring and Upper Wolfcamp, penetrating what is essentially a single common source of supply, the wellbores will produce a commingled mixture of hydrocarbons from both formations in amounts that are impossible to measure or determine under the Rules. The Division makes it clear that where there is diversity of ownership between two pools, which there is in the present cases:

the Division will only permit surface commingling of production from the pools if the operator accurately meters production from each of such pools or determines

the production by other methods the division has specifically approved prior to commingling.

19.15.12.10(C)(1) NMAC. Permian Resource can do neither and therefore surface commingling cannot be approved.

The three accepted methods of allocation for surface commingling – the well test method, the metering method, and the subtraction method – cannot be applied to Permian Resources' wells because under these methods there is no way to meter or measure the commingled amounts produced from each pool, and Permian Resources has not provided the Division with any "alternative methods" because it has either recklessly or intentionally assumed that the two formations reflect the existence of two distinct pools instead of one single reservoir, thereby ignoring the geology and need to account for commingling under 19.15.12.10(B)(1)(a). Findings of Fact at ¶¶ 20-21; 23-24.

An operator who seeks Division approval of its proposed plan must make every effort to inform and disclose all the relevant data and information regarding the geology and characteristics of the land that would affect waste and correlative rights and assist the Division with selecting the best plan for preventing waste, protecting correlative rights, and avoiding the drilling of unnecessary wells. By disregarding the unique geology of the Subject Lands and the implications resulting therefrom, Permian Resources failed to provide such necessary disclosures.

Because Permian Resources' plan is wrongly predicated on the premise that the two formations, Third Bone Spring and the Upper Wolfcamp, represent two distinct pools segregated by baffling instead of being a single reservoir without baffles as shown by the actual geology, Permian Resources did not request approval for downhole commingling despite the fact that, given the geology and lack of frac baffles, it is impossible to maintain segregation of

hydrocarbons between the two formations being produced from its Third Bone Spring and Upper Wolfcamp wells.

Furthermore, even if Permian Resources had requested approval for downhole commingling, it could not implement downhole commingling without a serious violation of correlative rights; therefore, Permian Resources' plan cannot not qualify for this exception. *See* 19.15.12.11(A)(8) NMAC (downhole commingling will not be approved unless correlative rights will not be violated). The primary concentration of reserves in the single common source of supply resides in the Third Bone Spring. Findings of Fact at ¶ 23. As a result, given the open communication between the Third Bone Spring formation and the Upper Wolfcamp formation, production from Permian Resources' wells drilled in the Upper Wolfcamp will capture the majority of their production from the Third Bone Spring, thus giving a major, unwarranted windfall to owners' Wolfcamp interest, particularly to those who own exclusively in the Upper Wolfcamp and not in Third Bone Spring, such as CLM Production and Warren Associates. The imbalance in production would distort and undermine the owners' ability to receive their just and equitable share of production.³ Given the magnitude of financial burden that Permian Resources imposes upon the owners for the excessive costs of its plan, Permian Resources' plan undermines any operative definition of correlative rights.

4. Cimarex's plan is the only plan presented to the Division that can meet the mandates of 19.15.12.9 NMAC.

In contrast to Permian Resources plan, Cimarex's plan, both its Option I and its Option II modes, meets the mandates of 19.15.12.9 NMAC. First, under Option I, Cimarex would drill

³ Permian Resources argues that the correlative rights of CLM Production and Warren Associates would be violated because they do not own in the Third Bone Spring, but these parties, who are closely associated and allied with Permian Resources, would receive a substantial windfall and unjust enrichment from Permian Resources Upper Wolfcamp wells that goes far beyond their just and equitable share of production at the expense of Third Bone Spring owners.

its Third Bone Spring wells and produce the Third Bone Spring formation, in a manner consistent with the Division's approval of other Bone Spring only units which are the vast majority of units in this Area of Interest. Findings of Fact at ¶ 22. Operators are aware that, in this specific area, if the Bone Spring formation is developed and produced, then it becomes uneconomical to co-develop the Wolfcamp formation, an awareness that is reflected in the pattern of development in this area. *Id.* at ¶¶ 7 and 22.

Accordingly, in its Option I, Cimarex would drill and produce only the Bone Spring unit, based on the precise definition and usage of "producing" and "production" as used under the Act and the Act's distinction between "drainage" and "production." *See* Cimarex's Brief, pp. 6-10. Thus, under Option I, only the Bone Spring would be produced, which has the primary concentration of product, and any hydrocarbons drained from the Upper Wolfcamp would not be considered or defined as "production" under the Act but would be defined as incidental "drainage." *Id.*

If the Division -- which has currently designated the Bone Spring and Wolfcamp as separate formations and therefore separate pools under the Rules (*see* §70-2-33(B)) -- decides to maintain its current designation of the Bone Spring and Wolfcamp as separate pools, then Cimarex's Option I would allow for the spacing, pooling, and production from the Third Bone Spring formation pursuant to the Act without violating correlative rights or causing waste, as the Division has done for the vast majority of units in this area, which are exclusively Bone Spring units and not co-developed units. Under this scenario, Cimarex would be able to satisfy the requirement for segregation of production from different pools as required by 19.15.12.9 NMAC, in the same manner that the majority of operators in this area who pool and produce

only the Bone Spring satisfy the segregation requirement, by producing the Third Bone Spring and allowing any incidental drainage from the Upper Wolfcamp.

Since only the Bone Spring is produced in Option I, and all hydrocarbons produced are deemed to be produced from the Bone Spring formation, any hydrocarbons that come from the Upper Wolfcamp would be defined as, and deemed to be, acceptable drainage under the Act. By approving Cimarex's Option I, the Division would be able to maintain the consistency of its conventional classifications and categories under the Act and its Rules, even though the geology in this area shows that there is communication between the formations. The convention that a specific formation designation corresponds to a specific pool and specific reservoir as described in §70-2-33(B) would be maintained pursuant to the pooling statute (§70-2-17(C)) because a unit covering a formation is "produced" only after being formally spaced and force pooled, and any hydrocarbons captured from outside the unit are deemed to be incidental "drainage" and not commingling of production. *See* Cimarex's Brief, pp. 6-10, for full discussion. Therefore, there is no violation of the segregation requirement under Cimarex's Option I.

Under Option II of its plan, Cimarex would drill its Third Bone Spring wells but then space and pool both the Bone Spring formation and the Wolfcamp formation. The spacing and force pooling of the Bone Spring formation, pursuant to §70-2-17(C), would allow Cimarex's Third Bone Spring wells to produce the Third Bone Spring formation; and the spacing and forced pooling of the Wolfcamp formation pursuant to the pooling statute would allow any hydrocarbons captured from the Upper Wolfcamp formation to be deemed "production" instead of "drainage." Thus, under Cimarex's Option II, with the spacing and compulsory pooling of both formations, Cimarex's Third Bone Spring wells would produce both the Third Bone Spring formation and the Upper Wolfcamp formation.

The hydrocarbons from each formation would be deemed to be produced from each formation and single pool; however, given that under this scenario both formations are being produced, the lack of frac baffles between the formations would result in communication and commingling of production between the pools in violation of the segregation requirement under 19.15.12.9(A) NMAC. Therefore, under its Option II, Cimarex would need to seek an exception pursuant to 19.15.12.9(C).

Fortunately, Cimarex is able to provide a method for allocating production between the formations that allows it to determine the percentage of production that would come from the Third Bone Spring formation and the percentage that would come the Upper Wolfcamp formation, thereby allowing the Division to approve Cimarex's request for an exception to Rule 19.15.12.9(A). *See* Findings of Fact at ¶ 23; *see also* Cimarex's Brief at p. 18 (discussing how it would determine percentages of production from each formation in order to satisfy the allocation language of the pooling statute). Pursuant to 19.15.12.10(e) NMAC, Cimarex can provide the Division an "alternative method" based on an assessment of PhiH porosity which can show a certain type of measurement of percentages of production that would come from the Third Bone Spring, currently estimated, based on Cimarex's plan for Option II, at 72.8%, while it is currently estimated that 27.2% of production would come from the Upper Wolfcamp. Findings of Fact at ¶ 23.⁴ The single wellbores proposed by Cimarex in the Third Bone Spring allow for this kind assessment prior to drilling, and the data collected after drilling and production would refine the measurements; in contrast, the distortion of the multidirectional

⁴ Permian Resources wrongly argues that Cimarex's Option II violates the allocation language in Sec. 70-2-17(C); with Cimarex's alternative method for determining the percentage produced from each formation, Cimarex would be able to calculate the interest of each owner pursuant to the allocation language in the pooling statute. *See* Cimarex's Brief, p. 18 (describing in detail how the allocation language of §70-2-17(C) would be applied to Cimarex's Option II).

fractures created by Permian Resources from its sets of wells drilled into the Third Bone Spring and Upper Wolfcamp, its giant blender approach, precludes an accurate assessment, as such drilling creates an indistinguishable blend of production. *Id.* at ¶ 23. Thus, Permian Resources plan is predicated on the false premise that its Third Bone Spring wellbores will produce only the Third Bone Spring pool and its Upper Wolfcamp wells will produce only the Upper Wolfcamp pool, a premise that is in no way supported by the actual geology. *Id.* at ¶¶ 21-22 and 24.

Furthermore, Cimarex was well aware of the actual geology, *viz.*, the lack of frac baffles between the formations, and accounted for the communication between the produced formations in its proposal for Option II by requesting in its initial pooling application for the Division to approve the need for commingling. *See* Cimarex's Pooling Applications in Case Nos. 23594 – 23601. Thus, under Cimarex's Option II, the commingling would be approved, and the alternative method of allocation would credit the owners with their just and equitable share of production, thereby protecting the owners' correlative rights.

5. Cimarex's plan prevents waste and protects correlative rights, while Permian Resources' plan results in excessive waste and violates correlative rights.

Under the Act, correlative rights are specifically defined as:

the opportunity afforded, so far as is practicable to do so, to the owner of each property in a pool to produce *without waste* the owner's *just and equitable share* of the oil or gas or both in the pool, being an amount so far as can be practically determined and so far as can be practicably obtained *without waste, substantially in the proportion* that the quantity of recoverable oil or gas or both under the property bears to the total recoverable oil or gas or both in the pool and, for such purpose, to use the owner's just and equitable share of the reservoir energy.
(Emphasis supplied)

NMSA 1978, § 70-2-33(H).

As an initial matter, the statutory definition of correlative rights requires that each owner's share "in the pool" be measured, substantially in proportion to the quantity of recoverable oil and/or gas under the owner's property bears to the total recoverable oil "in the pool."

This definition is problematic for Permian Resources because when it drills and produces the Upper Wolfcamp formation and pool, a majority the of its production will come from the Third Bone Spring formation, not the Wolfcamp formation. The converse is also true: when Permian Resources drills and produces the Third Bone Spring formation and pool, a certain amount of production will come from the Upper Wolfcamp. Findings of Fact at ¶¶ 21, 23-24. Because Permian Resources' Bone Spring wells and Wolfcamp wells would be completed in close proximity it creates a blender effect making it impossible to make a reasoned allocation of the quantity of hydrocarbons each well is producing from each formation. *Id.* Therefore, Permian Resources under its plan will not be able to determine each owner's just and equitable share within the pool as required by the statutory definition of correlative rights. Instead, the only share that Permian Resources will be able to provide under its plan is the proportion of recoverable oil under the owner's property that bears to the total oil produced from both pools (the Third Bone Spring and Upper Wolfcamp) and not from the single pool in which the owner's property is located as required by the statutory definition of correlative rights.

In sum, Permian Resources plan will result in an improper denominator for the proportion described in the statutory definition – Permian Resources' denominator being the total recoverable oil produced from the two separate formations and pool designations thereby precluding applying the statutory formula that is required to determine each owner with their just and equitable share of oil. Because Permian Resources cannot accurately determine each owner's

proportionate share of production it cannot, as a matter of law, protect the owners' correlative rights.

On the other hand, Cimarex is able to satisfy the formula required under the statutory definition of correlative rights. Under Option I, Cimarex will produce from only the Bone Spring formation and will be able to easily calculate the proportion of the recoverable oil for each owner thereby ensuring that each of them receives their just and equitable share of production.

Cimarex's Option II is also able to satisfy the statutory formula for correlative rights because under that Option Cimarex will employ a method for determining the percentage of production that would be produced from the Bone Spring and the percentage of production that would be produced from the Wolfcamp based on the specific geology of the Subject Lands. *Id.* at ¶ 23. Thus, under either Option, Cimarex would be able to protect the correlative rights of each owner.

In addition to violating the correlative rights of each owner due to its inability to allocate the production from its wells, Permian Resources also violates the owners' correlative rights by imposing on the owners' interest an excessive and unnecessary economic burden violating the stricture to "produce without waste." This wasteful burden strips the owners of their right to a "just and equitable share of oil" since their return on investment would be crushed under a mountain of wasteful spending. *Id.* at ¶¶ 11-13.

Permian Resources proposes to drill eight additional, unnecessary wells in the Upper Wolfcamp that increase the costs of the plan by slightly more \$95 Million, without any significant increase to production or EUR. *Id.* at ¶ 11. In addition, Permian proposes to drill ten unnecessary wells in the Bone Spring formation, consisting of two wells in the Upper 2nd Sand and eight wells in the 3rd Bone Spring, at a cost of slightly more than \$114 Millions. *Id.* at ¶ 13. In sum, between the cost of these additional 18 unnecessary wells and the higher AFEs proposed

for its remaining 30 wells (eight wells in the First Sand, six in the Upper Second Sand, eight in the 2nd Sand, and eight in the 3rd Sand), the total cost of Permian Resources development plan is \$270 Million greater than Cimarex's (\$539 Million minus \$269 Million). *Id.* Let that sink in for a moment - Permian Resources is proposing to burden the working interest owners with more than a quarter billion dollars of costs without giving them any significant increase in EUR.

Under the Act, the term "waste" is defined by "its ordinary meaning." *See* NMSA 1978, Sec. 70-2-3. Spending more than a quarter of a billion dollars without any significant increase in EUR is the epitome of "waste" under even the strictest meaning one could possibly ascribe to the term "waste." Given the magnitude of waste associated with production under Permian Resources' plan, it violates the correlative rights of each owner as a matter of law. Therefore, Cimarex has presented the only plan in the contested hearing that affords owners the opportunity to enjoy "without waste" their just and equitable share of oil, and thus, it is the only plan that protects correlative rights.

In the present cases, CLM Production and Warren Associates (collectively referred to herein as "Warren") own a very small percentages (0.125%) in the Upper Wolfcamp but own no interest in the Bone Spring. Findings of Fact at ¶ 28. Permian Resources is claiming that Cimarex's Option I is a textbook violation of correlative rights because Option I would only produce the Bone Spring and therefore exclude Warren's ability to produce its interests in the Wolfcamp. *See* Permian Resources' Response in Opposition to Motion to Continue at ¶ 3. Permian Resources interpretation of correlative rights in this situation misreads and misapplies the statute. As set forth above, Permian Resource's plan exceeds the cost of Cimarex's plan by more than a quarter of a billion dollars without any significant increase in production rendering it inherently wasteful. Thus, if Permian Resources' plan were implemented, Warren's interest

would be developed with waste thus violating Warren's correlative rights, as well as violating the correlative rights of every owner in the Wolfcamp formation. *See* Sec. 70-2-33(H). Thus, under either Cimarex's Option I or under Permian Resources' plan, Warren's correlative rights would be violated.

Furthermore, under Permian Resources plan, not only would the correlative rights of all owners in the Wolfcamp formation not be protected due to the massive waste associated with that plan, it also would violate the correlative rights of all of the Bone Spring owners. If Permian Resources' argument regarding Warren was given any weight, it would severely punish 100% of the Bone Spring owners and more than 99.875% of the Wolfcamp owners. Essentially, in exchange for developing Warren's 0.125% interest in the Wolfcamp formation, a development that fails to protect Warren's correlative rights, Permian Resources somehow believes that it is "just and equitable" to burden all of the Bone Spring owners and 99.87% of the Wolfcamp owners with more than a quarter of a Billion Dollars of unnecessary costs.

It is important to note that under Cimarex's plan for Option I, parties that own a greater interest in the Wolfcamp formation than the Bone Spring would nonetheless receive a greater return on their investment than what they would receive under Permian Resources' plan. Findings of Fact at ¶ 12. Conversely, under Permian Resources' plan, owners who own in both the Bone Spring and Wolfcamp formations would receive a much lesser share of the total proceeds from production even if they owned a greater interest in the Wolfcamp formation than in the Bone Spring. *Id.* For example, Sections 5 and 8 (Mighty Pheasant/Joker) MRC Permian, which has the largest ratio of ownership in Wolfcamp to Bone Spring, 3.0008, meaning that it owns 3 times more interest in the Wolfcamp than the Bone Spring, would still receive approximately \$20,044 more per acre PV10 under Cimarex's plan when compared to what it

would receive under Permian Resources' plan. *Id.* And HOG Partnership which owns more in the Wolfcamp than the Bone Spring by a factor 1.37, receives \$30,343 more PV10 per acre under Cimarex's plan for Option I than what it receives under Permian Resources' plan. *Id.*

Second, Permian Resources further violates the owners' correlative rights by imposing an excessive economic burden on the owners' WI that strips the owners of their opportunity to "produce without waste" their just and equitable share of oil. In its disregard for the geology of the Subject Lands, Permian Resources proposes to drill 8 additional, unnecessary wells in the Upper Wolfcamp that increase the costs of the plan by \$95 million without an increase to production or EUR and proposes to drill 10 additional, unnecessary wells in the Bone Spring formation, for a total increase of a quarter of a billion dollars in costs. Under the Act, the term "waste" is defined by "its ordinary meaning." *See* 70-2-3. Thus, such an excessive magnitude of cost to drill and operator wells that are not necessary for the optimal production of the Subject Lands clearly constitutes economic waste as understood by its ordinary meaning. Therefore, under Permian Resources plan, the owners would be forced to produce their share of oil "with waste" as opposed to "without waste" as required by the definition of correlative rights, and their correlative rights would not be protected.

In contrast, Cimarex's plan avoids the drilling of 18 unnecessary wells as it achieves optimal production from the Subject Lands without economic waste. Findings of Fact at ¶¶ 5 and 25. Therefore, it is the only plan presented in the contested hearing that affords owners the opportunity to produce "without waste" their just and equitable share of oil, and thus, it is the only plan that protects correlative rights. In order to exercise its correlative rights under the statutory definition, an owner must be able to "produce without waste the owner's just and equitable share of the oil." *See* 70-2-33. Thus, if an owner is presented a plan in which it cannot

produce its interest without waste, then under the statutory definition, the owner does not have a right to produce its interest under that plan.

Under both the Act and New Mexico case law, correlative rights are not absolute but are fully conditional, with “waste” being the overriding and limiting factor. *See Cont. Oil Co. v. OCC*, 1962-NMSC-062, ¶¶ 11-12 (holding that “the prevention of waste is the paramount power [of the Division], inasmuch as this term is an integral part of the definition of correlative rights,” and therefore the Division “must determine, insofar as practicable” what portion of an owner’s share “can be recovered without waste.”) (emphasis in the original). The *Continental* court held that “the extent of the correlative rights must first be determined” before the commission or division can act to protect them. *See id.* (emphasis added). Thus, if an owners’ interest cannot be recovered or produced without waste, then it stands to reason that the owner has no right, under §70-2-33(H), to the development of its interest. *See id.* at ¶ 27 (the court stating that “the protection of correlative rights must depend upon the commission’s [or Division’s] finding as to the extent and limitations of the right.”) The *Continental* court further clarified that an owner’s correlative right is “not absolute or unconditional,” stating that the right is “merely an opportunity to produce” but “only insofar as it is practical to do so,” and the production itself must be “without waste.” *See id.* at ¶ 27; see also *Cimarex’s* Brief, pp. 1-3, for a discussion of correlative rights.

Thus, because of the excessive magnitude of the costs imposed on owners under Permian Resources’ plan, Warren, as well as the other owners in both the Wolfcamp and Bone Spring, cannot produce their interest without waste; thus, Permian Resources’ plan has effectively invalidated the correlative rights of the owners. Because correlative rights are conditional, New Mexico case law provides a number of examples in which correlative rights have been either

invalidated, restricted, or superseded by concerns that demand higher priority. In *Bass Enters. Prod. Co. v. Mosaic Potash Carlsbad Inc.*, 2010-NMCA-065, the New Mexico Supreme Court determined that the Commission was correct to deny a drilling permit, directly prohibiting owners from exercising their correlative rights to produce oil and gas under their proposed plan because their operations would result in waste of potash resources and alternative plans for the production of oil and gas were available. *See Mosaic Potash* at ¶¶ 23-27. Thus, the Division should choose the plan that best protects and promotes correlative rights which in the present cases is Cimarex's plan.

Furthermore, in *Santa Fe Exploration Co. v. OCC*, 1992-NMSC-044, the Commission restricted an operator's right to produce from its well and limited oil production from a pool. The New Mexico Supreme Court upheld the Commission's restrictions of the operator's correlative rights stating that the broad grant of power given to the Commission to protect correlative rights and prevent waste allows such restrictions, and additionally, "the Division and the Commission are 'empowered to make and enforce rules, regulations and orders, and do whatever may be reasonably necessary to carry out the purpose of this act, whether or not indicated or specified in any section hereof.'" *See id.* at 28; *see also* NMSA 1978 §70-2-11. Thus, the Santa Fe court concluded that the restriction on the operator's correlative rights was justified under the evidence and allowed the Commission to fashion "a creative solution" to resolve the dispute. *See Santa Fe*, 1992-NMSC-044, ¶ 39.

Therefore, pursuant to New Mexico case law and the Act, Cimarex provides the only plan, in both its Option I and II modes, that (1) allows the owners of the proposed units to produce without waste their just and equitable share of oil by avoiding the excessive economic waste of drilling unnecessary wells; and (2) satisfies the statutory formula under the definition of

correlative rights for determining the percentage owed each owner based on the production from the single formation produced, which Permian Resources cannot satisfy because their plan commingles production without accountability or proper allocation.

- 6. Permian Resources submitted pooling applications for 48 wells that cannot possibly meet the deadlines required by Division Orders; whereas, Cimarex submitted pooling applications for 10 wells to show the Division that Cimarex is serious about meeting all Division deadlines for accomplishing the first installment of its 30-well development plan.**

On Day 3 of the contested hearing, a number of questions arose during cross-examination of Permian Resources' Landman about the meaning and requirements of Paragraphs 19 and 20 in a standard Division Order involving the specific language describing the 1-year drilling commencement deadline and the automatic termination of the Order if all the initial wells proposed are not commenced by the deadline. *See* Tr. (DD 8-11-23) 27: 11-25; 28: 1-25; 30: 1-25; and 31: 1-25. The language stating that the Order will terminate if an operator fails to commence the drilling of all initial wells is unambiguous and clear in the Order and therefore must be respected and not disregarded or taken for granted, as the Division has expressed clearly its expectations in these two paragraphs 19 and 20. Thus, whether drilling one initial wells will perfect and maintain an Order is as important to consider as the question of what procedural standards and expectations does this language demand.

Even if drilling a single well would perfect and hold an Order in place, which is a question yet to be resolved, the overriding issue of this languages speaks to the requirement that an operator respect the directives of the Division and its procedural expectations and not abuse or over burden the proceedings by flooding the Division with applications that an operator could not conceivably fulfill, thus knowingly burdening the Division with future applications and hearings for extensions of time the moment the original pooling applications themselves are

filed. Cimarex submits that such practices are a misuse of the adjudicatory services provided by the Division.

In the present cases, Permian Resources has flooded the Division with applications for 48 initial wells, many more than the number that could be drilled in a year, as acknowledged by Permian Resources itself. *See* Tr. (DD 8-10-23) 226: 22-25; 227: 1-3 (Permian Resources geologist explaining that it will take several years to drill all the wells proposed). In comparison, Cimarex filed applications for its first set of 10 wells, a reasonable number, to be initially drilled in a timeframe that would meet the commencement deadline of the Division's Orders, as Cimarex pursues its development plan that will culminate with 30 wells for the development of the Subject Lands. It is still possible due to unforeseen circumstances that Cimarex might fall short of its commencement deadline by one or two wells, but under such circumstances, Cimarex would apply, pursuant to Paragraph 20, for a time extension by showing good cause based on the unforeseen circumstances. In the meantime, Cimarex has every good faith intention to meet the Order's express requirements.

Cimarex respectfully submits that a good faith application for "good cause" must be predicated on a good faith intention at the time the original application is filed to meet the commencement deadline, with good cause premised on unforeseen circumstances that occur unexpectedly during the operator's good faith efforts to meet deadlines clearly prescribed by the Order.

When an operator submits applications knowing full well at the time of their submission that it will not meet the directives of the Order, then "good cause" should not be available to such operator who clearly had no intention of meeting the commencement deadline. Drilling a certain number of wells in the unit might hold the unit in place, but an operator should not be

allowed to overly burden and misuse the proceedings of the Division by sacking the Division with future hearings or by attempting to monopolize multiple units by proposing more wells than the operator can drill at the time of the application. What Paragraphs 19 and 20 in the Division Order signify is the reasonable and responsible use of the adjudicative process by operators.

7. Conclusion:

As the record clearly shows, Cimarex made every effort to request that Permian Resources take some additional time to consider the complexity of issues involved in the present cases and have a pre-hearing conference to clarify a number of the unresolved issues. See Cimarex's Motion to Continue Hearing, at p. 1. Permian Resources repeatedly asserted that the issues were not complex and insisted on moving forward with the contested hearing as soon as possible. *See* Permian Resources' Response in Opposition to Motion to Continue at ¶ 11. In doing so, Cimarex submits that Permian Resources, in its haste to produce the two formations without taking into account that it was dealing with a single reservoir instead of two reservoirs, ran head on into irremediable complications involving the geology of the Subject Lands and erroneously proposed the drilling of numerous unnecessary wells at exorbitant costs because it disregarded and neglected the actual nature of the geology and the actual single pool and common source of supply that spanned across both formations instead of two distinct pools as wrongly assumed by Permian Resources. Consequently, Permian Resources has presented a plan that violates the segregation requirements of 19.15.12.9 NMAC, violates the correlative rights of the owners, and violates the statutory requirement to prevent waste and avoid the drilling of unnecessary wells. On all accounts, Permian Resources plan undermines the purpose of the Act and its Rules.

Under the Act, a “pool” by definition means an underground reservoir containing a common accumulation of crude petroleum oil, and “pool” is synonymous with “common source of supply” and with “common reservoir.” *See* § 70-2-33(B). However, in the present cases, given the lack of frac baffles between the two formations, the Third Bone Spring and Upper Wolfcamp, the two formations that have been designated as two pools with two pool codes actually represent a single reservoir and single common source of supply. Thus, there is a misalignment between the two formations designated as pools and the actual geology of the formations.

It is this misalignment of geology that Cimarex in good faith has made every effort to address in its development plan, in the location and number of the wells it proposed to efficiently produce the Subject Lands, and in the communications it has had with the Division, both in its testimony and exhibits and in the pleadings leading up to the contested hearing. Permian Resources has been fully aware of the geology of the formations because, when asked about it during the hearing, its expert witnesses clearly acknowledged the lack of frac baffles and the resulting communication between the formations. And yet, Permian Resources insists on using the misalignment of pool designations to justify at great and unnecessary costs the drilling of wells into both the Third Bone Spring and Upper Wolfcamp formations even though the wells it proposes, based on the geology, would penetrate and produce from the single common source of supply, thereby wreaking havoc with correlative rights and undermining the application of the administrative rules.

Consequently, Cimarex is the only party that has proposed a plan that would efficiently produce the Subject Lands based on the actual geology involved while maintaining, to the extent possible under the circumstances, compliance with the Act, its Rules, and New Mexico case law;

Cimarex has made every effort to provide the Division with all available options (I & II), as well as the means for implementing Cimarex's plan in order to prevent waste, protects correlative rights, and avoid the drilling of unnecessary wells. Because of Permian Resources' haste, the Division was not able to address prior to the hearing the misalignment issue under the statutory definition of "pool," and therefore, Cimarex respectfully requests that the Division adopt and approve one of three options to account for the misalignment at this point in the proceedings: (1) grant Cimarex operatorship of the Subject Lands pursuant to its Option I, which would produce the Bone Spring formation as a single common source of supply subject to any incidental drainage from the Upper Wolfcamp formation, an arrangement that reflects the vast majority of units in this this area; (2) grant operatorship of the Subject Lands pursuant to its Option II, which would produce both the Third Bone Spring and Upper Wolfcamp formations in a manner that provides a method for determining the percentage of oil produced by each formation thus maintaining segregation and protecting correlative rights; or (3) increase the vertical depth of the Bone Spring formation to cover and account for the full extent of the single common source of supply, or combine the Third Bone Spring formation with the Upper Wolfcamp formation to create a single pool that covers and accounts for the single common source of supply and implement Cimarex's development plan pursuant to such adjustment. Cimarex has provided the Division with all available options and elements for it to fashion a solution to these matters in order to uphold the purpose of the Act as authorized by the *Santa Fe* court and §70-2-11. *See Santa Fe* 1992-NMSC-044, ¶ 39; *see also* Cimarex's Amended Motion for an Order to Prohibit the Drilling of Wells in the Upper Wolfcamp to Protect Correlative Rights and Optimize Production of the Subject Lands.

Finally, Cimarex has surpassed and outperformed Permian Resources in all of the seven (7) factors that the Division considers when selecting the best development plan in a contested hearing, and therefore, Cimarex respectfully requests that the Division select its development plan, thereby granting it operatorship, and deny the development plan proposed by Permian Resources..

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CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing was filed with the New Mexico Oil Conservation Division and was served on counsel of record via electronic mail on September 21, 2023:

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