STATE OF NEW MEXICO

ENERGY, MINERALS AND NATURAL RESOURCES DEPARTMENT

OIL CONSERVATION DIVISION

IN THE MATTER OF THE HEARING CALLED BY THE OIL CONSERVATION DIVISION FOR THE PURPOSE OF CONSIDERING:	
APPLICATION OF OCEAN ENERGY, INC., FOR COMPULSORY POOLING, LEA COUNTY, NEW MEXICO	CASE NOS. 13,036
APPLICATION OF DAVID H. ARRINGTON OIL AND GAS, INC., FOR COMPULSORY POOLING, LEA COUNTY, NEW MEXICO	and 13,039
	(Consolidated)

ORIGINAL

REPORTER'S TRANSCRIPT OF PROCEEDINGS

EXAMINER HEARING

BEFORE: DAVID K. BROOKS, JR., Hearing Examiner

March 27th, 2003

Santa Fe, New Mexico

This matter came on for hearing before the New Mexico Oil Conservation Division, DAVID K. BROOKS, JR., Hearing Examiner, on Thursday, March 27th, 2003, at the New Mexico Energy, Minerals and Natural Resources Department, 1220 South Saint Francis Drive, Room 102, Santa Fe, New Mexico, Steven T. Brenner, Certified Court Reporter No. 7 for the State of New Mexico.

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March 27th, 2003
Examiner Hearing
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A P P E A R A N C E S

FOR OCEAN ENERGY, INC., and
NADEL AND GUSSMAN PERMIAN, LLC:

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By: WILLIAM F. CARR

* * *

ALSO PRESENT:

WILLIAM V. JONES, JR.
Petroleum Engineer
New Mexico Oil Conservation Division
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* * *

WHEREUPON, the following proceedings were had at 3:45 p.m.:

EXAMINER BROOKS: Back on the record. At this time we'll call Case Number 13,036, the Application of David H. Arrington Oil and Gas, Inc., for compulsory pooling, Lea County, New Mexico,

and Case Number 13,039, the Application of David H. Arrington Oil and Gas, Inc. -- I'm sorry, Number 3- -- that's 13,039. 13,036 is the Application of Ocean Energy, Inc., for compulsory pooling, Lea County, New Mexico.

Call for appearances.

MR. BRUCE: Mr. Examiner, Jim Bruce of Santa Fe, representing Ocean Energy, Incorporated. I have three witnesses.

MR. CARR: May it please the Examiner, my name is William F. Carr with the Santa Fe office of Holland and Hart, L.L.P. We represent David H. Arrington Oil and Gas, Inc., and I also have three witnesses.

EXAMINER BROOKS: Okay, that's a lot of witnesses for this time in the afternoon, but let them stand and be sworn.

(Thereupon, the witnesses were sworn.)

EXAMINER BROOKS: Okay, I assume that -- Well, apparently by common consent Mr. Bruce is going first, which --

MR. BRUCE: Yes.

EXAMINER BROOKS: -- given the fact that you filed first, would seem to be appropriate.

You may proceed, Mr. Bruce.

MR. BRUCE: Thank you.

DEROLD MANEY,

the witness herein, after having been first duly sworn upon his oath, was examined and testified as follows:

DIRECT EXAMINATION

BY MR. BRUCE:

Q. Would you please state your name and city of residence?

A. Derold Maney, Houston, Texas.

Q. Who do you work for and in what capacity?

A. I'm a landman for Ocean Energy, Inc.

Q. Have you previously testified before the Division?

A. Yes, I have.

Q. And were your credentials as an expert landman accepted as a matter of record?

A. Yes, they were.

Q. And are you familiar with the land matters involved in these Applications?

A. Yes, I am.

EXAMINER BROOKS: Sorry, could you spell your

name?

THE WITNESS: D-e-r-o-l-d M-a-n-e-y.

EXAMINER BROOKS: Thank you. Proceed.

MR. BRUCE: Mr. Examiner, I tender Mr. Maney as an expert petroleum landman.

MR. CARR: No objection.

EXAMINER BROOKS: He is so qualified.

Q. (By Mr. Bruce) Mr. Maney, could you identify Exhibit 1 and describe what Ocean seeks in this case?

A. This is a land plat, in the orange outline indicating the unit, and the yellow portion in the west half of the proposed unit is the Ocean acreage that we hold.

Q. Okay. And do you seek to pool from the surface to the base of the Mississippian formation?

A. Top of the Mississippian.

Q. Top of the Mississippian, top -- what? To the top or is it the top 2- --

A. Test the top.

Q. Test the top of the -- say, the top 200 feet of the Mississippian?

A. Yes, sir.

Q. What is Ocean's proposed well location?

A. 660 from the south line and 1980 from the east line.

Q. And Arrington Oil and Gas has a different location, do they not?

A. Yes, they do.

Q. And will Ocean's geologist and engineer discuss the reasons for your proposed location?

A. Yes, they will.

Q. What is the -- I guess I got the exhibits out of order, but would you skip over to Exhibit 3 --

A. Yes, sir, this is --

Q. -- for a minute? And first of all, although we don't have an exhibit, I don't think, who are the working interest owners in the 320-acre well unit?

A. Ocean Energy, Inc.; McCombs Energy; Nadel and Gussman; and David H. Arrington Oil and Gas.

Q. Okay, and Arrington owns 50 percent?

A. Fifty percent, Ocean owns 26.67 percent, McCombs owns 13.33 percent, and Nadel and Gussman owns 10 percent.

MR. BRUCE: Okay. Mr. Examiner, I forget, I am also entering an appearance today on behalf of Nadel and Gussman Permian, LLC.

EXAMINER BROOKS: Very good.

Q. (By Mr. Bruce) Mr. Maney, McCombs and Nadel and Gussman are in agreement with Ocean --

A. Yes.

Q. -- on this well location?

A. Yes, we are under an operating agreement. We've drilled other wells in the area and under an operating agreement.

Q. Okay. Now, before we get to the proposal letter that you sent to Arrington Oil and Gas, I note that on Exhibit 1 it shows the east half, east half of Section 8 as being owned by ExxonMobil. That is not correct, is it?

A. No, it's not.

Q. That east half, east half is a new state lease just issued to Arrington Oil and Gas?

A. Yes, it is.

Q. Or owned by Arrington Oil and Gas, I should say?

A. Yes.

Q. Now, how long has -- getting back to Exhibit 3, how long has Ocean been looking at drilling a well in Section 8?

A. We first proposed the well to Exxon in November of 2000.

Q. And at that time the east half, east half was owned by Exxon?

A. Yes, it was.

Q. Okay, the lease has since expired?

A. Yes.

Q. Okay, then keep on going, please?

A. Okay, we proposed -- Well, excuse me, I sent my

first letter in November of 2002 to Exxon requesting a term assignment, and I followed that up in January of 2002 with a proposed well.

In February -- excuse me, May 28th, Exxon -- we got a term assignment covering the east half, northeast, and the southeast of Section 8 and the northwest quarter of Section 9. And -- that's not right. Section 9, it's the northeast of the northwest quarter is what we got from Exxon under the term assignment.

And early August, Exxon called and said that they were concerned as to the lease status of their lease K5926-1.

Q. And that was after you obtained a term assignment and paid for a term assignment?

A. Yes, yes.

Q. Okay, go ahead.

A. And at that point we withdrew the proposal to our partners Nadel and Gussman and McCombs, because we didn't want to drill a well if there was a title issue.

And then August 27th, Newfield, who had production in the west half of Section 8, they wrote a letter to the State of New Mexico, said the well was shut in and that they would pay shut-in in April of '03.

Q. Okay, and let me interrupt again. The production in the west half of 8 was on that same lease?

A. Yes.

Q. The east half, east half of Section 8 and some acreage in the west half of Section 8 was under the same lease?

A. That's correct.

Q. Okay. There was no production in the east half of Section 8?

A. No.

Q. Okay.

A. No. And about a month later, in September, I wrote a letter to the State of New Mexico and requested the lease status and October 8th we got a letter from the State of New Mexico saying that the lease was expired February 28th.

EXAMINER BROOKS: What year?

THE WITNESS: '02.

EXAMINER BROOKS: '02.

THE WITNESS: And in October or shortly thereafter, I attempted to nominate the lease at the state sale and was told we needed to wait 60 days, which we did, and we nominated in December for the January sale.

And January 21st the sale was held, and that lease went for $130,000 to Doug Schutz who, it's my understanding, purchased the lease for David H. Arrington. And we bid up to $128,000 before we discontinued bidding.

Q. Okay. So you have been -- Although there was a gap between your first two letters, Ocean has been proposing the well or attempting to drill it for over a year now?

A. Yes.

Q. Now, you mentioned you wrote to the State. Did you also personally visit with personnel in the State Land Office to discuss the situation of the east half, east half lease?

A. I did, I visited with Jeff Albers.

Q. At the Land Office?

A. Yes, I did.

Q. And so you were quite clear, were you not, that you wanted to make sure that the State knew what was going on and that Ocean didn't want to drill on a bad lease?

A. Correct.

Q. Okay. Now, after the new lease was issued, did you then propose the well to Arrington Oil and Gas?

A. I initially proposed it to Doug Schutz immediately, and then a day or two afterwards when I was certain that David H. Arrington Oil and Gas owned the rights to the lease, I proposed the well to him.

Q. And is your proposal letter submitted as Exhibit 2?

A. Yes, sir.

Q. And the second page of Exhibit 2 is simply a follow-up letter to Mr. Arrington?

A. Yes, it is.

Q. Okay, what response did Ocean receive?

A. I had a few conversations with Mr. Arrington about the lease. We talked about us buying the lease but we couldn't agree on terms. We had already pretty much reached our limit on what we thought it was worth, and so we couldn't come to an agreement.

Q. In your opinion, has Ocean made a good faith effort to obtain the voluntary joinder of the interest owners in the proposed well?

A. Yes, we have.

Q. And could you identify Exhibit 4 and discuss the costs of the proposed well?

A. Exhibit 4 is the AFE for the well. The dryhole costs are $986,400, and the completed well costs, $1,700,850.

Q. Is this cost in line with the cost of other wells drilled to this depth in this area of Lea County?

A. I believe it is.

Q. And does Ocean request that it be designated operator of the well?

A. Yes, we do.

Q. Do you have a recommendation for the amounts

which Ocean should be paid for supervision and administrative expenses if the parties cannot come to voluntary terms?

A. Yes, I do, $6000 per month for a drilling well and $600 per month for a producing well.

Q. And are these amounts equivalent to those normally charged by Ocean and other operators in this area for wells of this depth?

A. I believe they are.

Q. Do you request that this rate be adjusted periodically as provided by the COPAS accounting procedure?

A. Yes, sir, I do.

Q. And was Arrington Oil and Gas notified of this hearing?

A. Yes, they were.

Q. And is Exhibit 5 my affidavit of notice?

A. Yes, it is.

Q. Were Exhibits 1 through 5 prepared by you or under your supervision or compiled from company business records?

A. They were.

Q. And in your opinion is the granting of Ocean's Application in the interests of conservation and the prevention of waste?

A. Yes.

MR. BRUCE: Mr. Examiner, I'd move the admission of Ocean Exhibits 1 through 5.

MR. CARR: No objection.

EXAMINER BROOKS: One through 5 are admitted.

CROSS-EXAMINATION

BY MR. CARR:

Q. Mr. Maney, if I look at Ocean's proposal, you're seeking an order pooling the same acreage as David H. Arrington; is that not correct?

A. That's correct.

Q. You're proposing a well in the -- what is it, the southeast of the southeast of this --

A. Yes, I believe that's correct.

MR. BRUCE: Southwest --

THE WITNESS: Sorry --

Q. (By Mr. Carr) Southwest, that's right. Southwest southwest of the spacing unit. Mr. Arrington is proposing a well up in the northeast quarter?

A. Yes.

Q. And that's really the difference between the two proposals other than --

A. Yes.

Q. -- both wanting to operate?

A. Right.

Q. I believe you testified that in the proposed

spacing unit, the east half of 8, collectively Ocean, McCombs and Nadel and Gussman would have 50 percent of whatever well is drilled on that --

A. That's correct.

Q. You also operate the south half of Section 5, immediately north of there, do you not?

A. That's correct.

Q. And there is a well 660 feet off the north boundary of this standup east-half spacing unit?

A. Yes.

Q. That's an Ocean well?

A. Yes.

Q. What is the ownership in the south half of Section 5?

A. Ocean owns 53 percent, McCombs owns 26 percent, Nadel and Gussman owns 20 percent.

Q. What does that total? Is that all of it?

A. That's all of it.

Q. So you -- The same three partners that have 50 percent in the east half of 8 have 100 percent of the south half of --

A. That's correct.

Q. -- Section 5?

You proposed the well to Mr. Arrington on January the 28th. That was the first formal proposal to Arrington?

A. Yes.

Q. Had not Mr. Arrington faxed a proposal to you the day before for the same property?

A. He may have.

MR. CARR: That's all I have, thank you.

EXAMINATION

BY EXAMINER BROOKS:

Q. I want to clarify the ownership on this -- You gave me the percentages. Arrington owns 50 percent, Ocean owns 26.67 and McCombs 13.33 and Nadel and Gussman 10 percent?

A. Yes, sir.

Q. That's -- the unit is all now --

A. That's the unit, right.

Q. Where is the tract that Arrington owns? Is that the east half of the east half?

A. East half of the east half, yes, sir.

Q. And Ocean owns the north --

A. We own the west half of the east half.

Q. Okay, do you own 50 percent, or what percent do you own? Do you own a percentage -- an undivided interest in all of the west half, or --

A. Yes --

Q. -- is that split up?

A. -- that's our 26 percent.

Q. Okay, and the others, they also own undivided interest --

A. Yes.

Q. -- in the entire west half?

A. Yes.

Q. So there's no split of ownership between the tracts in the west half?

A. No.

Q. Okay. And the vertical limitations are from the surface to the -- did you say to the top of the Mississippian?

A. Top of the Mississippian.

Q. Okay, and what is the pool in which this is located?

A. It is the Atoka-Morrow -- let's see.

MR. BRUCE: Mr. Examiner, it's the North Vacuum-Atoka-Morrow Gas Pool.

EXAMINER BROOKS: North Vacuum- --

MR. BRUCE: That is in the Application.

EXAMINER BROOKS: Okay. And Mr. Carr has put on here that it's undesignated. Is it within the --

MR. BRUCE: It's within a mile, I believe.

EXAMINER BROOKS: Within a mile?

THE WITNESS: That's right.

Q. (By Examiner Brooks) Okay, any other pools that

anybody knows of that are affected?

A. (Shakes head)

Q. And you're asking for a 320-acre unit. Are you asking for any smaller units in case any other --

A. No.

Q. -- formations are --

A. Not at this time, no, sir.

Q. Okay, I believe that's all I have. Oh, maybe I better get it on the record, because I picked it up off of your Exhibit 4 here. Exhibit 4 reflects the location -- your proposed location as being 660 from the south and 1980 from the east; is that correct?

A. That's correct.

EXAMINER BROOKS: Thank you. Nothing further.

MR. BRUCE: I have nothing further of this witness.

EXAMINER BROOKS: You may call your next witness.

MR. BRUCE: I call Mr. Lowe to the stand.

JAMES T. LOWE,

the witness herein, after having been first duly sworn upon his oath, was examined and testified as follows:

DIRECT EXAMINATION

BY MR. BRUCE:

Q. Would you please state your name and city of residence for the record?

A. My name is James T. Lowe, from Spring, Texas.

Q. Who do you work for and in what capacity?

A. I'm employed by James Tobin Associates in the capacity as a consulting geologist for Ocean Energy, Inc.

Q. Okay. Have you previously testified before the New Mexico Oil Conservation Division?

A. I have not.

Q. Would you summarize for the Examiner your educational and employment background?

A. I have a bachelor's degree in geology from the University of Wisconsin in Milwaukee and a master's degree from Western Washington University in geology from the University of Washington.

I have 30 years of exploration oil and gas experience, mostly in the lower 48. Twenty-six of those have been with Unocal, and the last 15 years of that 26 were in the Gulf Coast and mid-continent areas. The past two years I have been employed by BP as consulting geologist for west Texas in the Delaware Basin.

Q. Before we move on, there are three geologic exhibits presented by Ocean today, and they have the name of Frank Messa on them. Mr. Messa is also an Ocean geologist, correct?

A. Yes, sir.

Q. And he's kind of under the weather?

A. Yes, sir.

Q. Did you actually prepare Exhibits 6, 7 and 8?

A. I did.

Q. And you have reviewed all the data there, and it reflects your geologic opinion; is that correct?

A. Yes, sir.

MR. BRUCE: Mr. Examiner, I tender Mr. Lowe as an expert petroleum geologist.

EXAMINER BROOKS: Any objection, Mr. Carr?

MR. CARR: No.

EXAMINER BROOKS: So qualified.

Q. (By Mr. Bruce) Now, Mr. Lowe, could you identify your Exhibit 6 and discuss the structure in this area?

A. Exhibit 6 is a structure map of the Townsend-Morton areas on the top Morrow lime. The area shown on the map is a nine-section map with the section in question, Section 8, in the middle. The map is a scale of 1-to-3000. The red dots are currently producing Brunson sand, which is our primary objective. The contour interval is 100 feet. The area of Ocean Energy's lease position is colored in yellow, and the black area outlined in the east of 8 is the half-section in question.

The proposed well of Ocean Energy, the Dirt Devil 8-1, is on the southwest quarter of the east half of Section 8. The structural position is in a north -- I

should say the north end of a nose which goes to the north from south and is in a relative synclinal position shown by the contours.

The two red numbers above and below are the current gas production in MCF, and the denominator of that number is the current gas cum in million MCF on the map.

Q. Are the production figures from the Atoka?

A. The production figures are from the Brunson-Atoka sand, yes, sir.

Q. Okay. Do you have anything further on this exhibit, Mr. Lowe?

A. No, sir.

Q. Let's move on to Exhibit 7. What does that depict?

A. Exhibit 7 is an isopach map of the lower Atoka-Brunson sand, and it is the net isopach, and it was defined as shown in the legend below as the net pay greater than 8-percent density porosity, and the black number underneath that number shown by each well that penetrated the Brunson sand is the gross sand which has a character of less than 60 API units.

Again, the red dots show the producing wells that have penetrated the Brunson sand and are the same numbers that were shown on the structure map.

The interpretation of the Brunson sand as shown

in the lease, shows that there is a relative thick across Section 8 in the southern portion of that section, and our location shows the sand is approximately -- they estimate it to be 40 to 45 feet thick in that zone.

The sand channel that the Brunson sand has been interpreted as extends north-northeast from that location.

Q. Now, when you look at Exhibit 6, the southeast quarter of Section 8 is somewhat structurally higher than the northeast quarter; is that fair to say?

A. Can you say that again, please?

Q. The southeast quarter of Section 8 is somewhat structurally higher than a location in the northeast quarter?

A. That is correct.

Q. But the sands appear to be much thicker in the southeast quarter?

A. Yes, sir, they do.

Q. And would it be your conclusion that you would want to stay in the southeast quarter of Section 8 because of the thicker sand?

A. Yes.

Q. Okay. Now, keeping your Exhibit 7 in front of you, could you move on to your Exhibit 8 and discuss the wells in this cross-section?

A. Exhibit 8 is a stratigraphic cross-section

through the wells that go through Section 8 and also a section on either side of Section 8, to the north and to the south.

The cross-section has a scale of 1 inch equals 80 feet vertically, and no horizonal scale. The lime shown as datum top Morrow lime is the stratigraphic datum that the logs, the three wells, were hung on. The yellow portion across the map is the top and bottom of the Brunson sand as shown by the correlations in each wellbore. And the red numbers on each side of the well, on the side of each well, show the perforations and productive interval and the cumulative production of the wells surrounding our location.

The cross-section shows dramatically that the Ocean Energy location will be approximately the same thickness as the sand in the Marathon Oil Company State Community Number 2, Section 17, immediately to the southeast.

Q. Okay. There are some pretty good wells to the south and west of your proposed location, are there not?

A. Yes, sir, that is where the contours of the isopach show that the sand is cleanest and thickest.

Q. Okay, and the structural position of your proposed well is pretty similar to those 10- and 12- and 30-BCF wells to the west, is it not?

A. That is correct. It's slightly lower, but still in a relative high structural position.

Q. And from a geologic standpoint, is Ocean's proposed location in the southwest quarter of the southeast quarter the preferred location?

A. It would be easiest to drain that sand from that section, that portion of that section.

Q. Okay. Again, were Exhibits 6 through 8 prepared by you or under your supervision?

A. Yes, sir, they were.

Q. And in your opinion is the granting of Ocean's Application in the interests of conservation and the prevention of waste?

A. Yes, it is.

MR. BRUCE: Mr. Examiner, I'd tender Ocean Exhibits 6 through 8.

EXAMINER BROOKS: Any objection?

MR. CARR: No objection.

EXAMINER BROOKS: Ocean 6 through 8 are admitted.

EXAMINATION

BY MR. CARR:

Q. Mr. Messa, I just have -- I mean, I'm sorry. I just have one question here, really. Did you work with Mr. Messa in the preparation of --

A. Yes, I was under his supervision.

Q. And in the preparation of this Exhibit, both 6 and 7, the structure map and the isopach, did you use any information other than subsurface data?

A. I used subsurface data for the maps plus prior maps that were shown to me.

MR. CARR: That's all I have, thank you.

EXAMINER BROOKS: Well, Mr. Bruce referred to Mr. Messa as an Ocean geologist. I assume that's with a capital O.

(Laughter)

EXAMINER BROOKS: Okay, late in the day.

EXAMINATION

BY EXAMINER BROOKS:

Q. You have a known point here at A, and then you have a known point at this location over in the west half.

A. Of Section 8?

Q. Of Section 8.

A. Yes, sir.

Q. And what is it that makes you think that this -- high on the structure noses up into Section 8 the way you've shown it, as far as this just being somewhere in between -- anywhere in between those two known points?

A. Well, you can see on my structure map, you can see that the nose goes from A, which is 8033 feet, to 8162 in that well in question that you just asked for.

Q. Right.

A. And the next control point to the north are lower than --

Q. Right.

A. -- those other two. So I suggest that this whole structure noses down to the north-northeast and that our location would be somewhat in between those two.

Q. Yeah, the structure is -- There's considerably less thickness of structure in this Brunson-Atoka in either of the other two wells shown on your cross-section than there is in the State Com 17 Number 2 that's down in Section 17.

A. Yes, sir.

Q. And your theory is based on the postulate that the thicker sand continues up into Section 8, and I guess that's what I'm trying to figure out.

A. Okay, and my control --

Q. What reasons --

A. What do I have for that?

Q. -- would cause that thickness to project up into Section 8 --

A. Okay --

Q. -- when you don't have that comparable thickness anywhere else?

A. Okay, if you -- A regional review of the Brunson

sand in this area shows that these sands tend to accumulate in the low portions at the top of the Morrow lime structure. So when you contour the lower Morrow lime there's this trough, and these sands tend to follow this trough.

And in this case, since this trough is designed -- or interpreted to go north-northeast, that sandbody should follow the structural lows.

And in fact, if you were to go to the section northeast of Section 8, you'll see that there are values of around --

Q. You mean Section 4, right?

A. Section 4, there are values of 12 and 14 feet of sand, and I just interpret that channel to at least show that that sand goes in that direction, because directly to the west, where A' is, you can see there's a 5-foot net porosity thickness with a gross of 6. So that tells me that the channel doesn't go in that direction anymore. So it must proceed to the east of the A'.

EXAMINER BROOKS: Okay, thank you.

Does anybody want to follow up?

MR. BRUCE: I have no follow-up.

MR. CARR: No.

EXAMINER BROOKS: Next witness.

MR. BRUCE: Call Mr. Payne to the stand.

RAYMOND W. PAYNE,

the witness herein, after having been first duly sworn upon his oath, was examined and testified as follows:

DIRECT EXAMINATION

BY MR. BRUCE:

Q. Would you please state your name and city of residence for the record?

A. Ray Payne, Houston, Texas.

Q. What is your occupation?

A. Petroleum reservoir engineer.

Q. Who do you work for?

A. Ocean Energy.

Q. Have you previously testified before both the Oil Conservation Division and Commission as a petroleum engineer?

A. Yes, I have.

Q. And were your credentials as an expert accepted as a matter of record?

A. Yes, they were.

Q. Does your area of responsibility include this part of southeast New Mexico?

A. Yes, it does.

Q. And are you familiar with the geology involved in this case?

A. Yes, I am.

MR. BRUCE: Mr. Examiner, I'd tender Mr. Payne as an expert --

THE WITNESS: Or the engineering, excuse me.

MR. BRUCE: Didn't mean to hurt your feelings.

THE WITNESS: That's okay.

EXAMINER BROOKS: He could be familiar with the geology too.

MR. CARR: We think he's qualified as both.

EXAMINER BROOKS: So qualified.

Q. (By Mr. Bruce) Up front, Mr. Payne, you know, there has been a change in ownership. Ocean's well location is based on geology and engineering regardless of the leasehold ownership; is that correct?

A. Yes, sir, we've had that location spotted for some time now.

Q. Okay. And your conclusion is that the southwest quarter, southeast location is better from an engineering standpoint, as well as Mr. Lowe's conclusion that it's better from a geologic standpoint?

A. Yes, sir.

Q. Would you identify your Exhibit 9 and discuss its contents for the Examiner? And perhaps, Mr. Examiner, if you'd keep, perhaps, one of Mr. Lowe's exhibits out in front of you, Exhibit 6, say --

A. It may be helpful if I had some of those exhibits

with me too.

Q. Just so that you can see the well or wells he's talking about.

Again, Mr. Payne, could you identify Exhibit 9 and specify for the Examiner where the Texaco 5-1 well is located?

A. Yes, this is the monthly production history for the Texaco 5-1, located in Section 5, just north of our proposed unit.

EXAMINER BROOKS: That's the A'?

THE WITNESS: Yes, that's the start of the -- that's A'.

EXAMINER BROOKS: Cross-section.

THE WITNESS: Yes, sir.

EXAMINER BROOKS: Okay.

THE WITNESS: And it shows the cumulative oil production as of December, 2002, at just under 3000 barrels of oil and 562 million cubic feet of gas.

Q. (By Mr. Bruce) What is Exhibit 10?

A. Exhibit 10 is a pressure and cumulative production history for the same well, the Texaco State 5-1.

Q. Okay. And then move on to your Exhibit 11. What does that depict?

A. Exhibit 11 is a decline-curve analysis for the same subject well, the Texaco State 5-1.

Q. What is your conclusion as far as ultimate recovery from this well?

A. Estimated recovery from the Texaco State 5-1 is 1.2, 1.3 BCF of gas, based on the decline curve.

Q. Okay. And then what is Exhibit 12?

A. Exhibit 12 is a P/Z plot for the same subject well, and it's -- using the pressure data on Exhibit 10, it's suggesting an ultimate recovery from this Texaco State 5-1 of 1.1 BCF, which is consistent with the decline-curve analysis.

Q. Okay. Now, on this Exhibit 12 you've got black diamonds and red squares. What does that depict?

A. The black diamonds are the P/Z data. It's shown in the legend on the right-hand side of the graph, and the sort of reddish squares are just the pressure from the buildups.

Q. Okay. Now, before we move on to your final exhibit, in looking at the data from the Texaco 5-1 well, why does Ocean prefer to drill in the southwest of the southeast, rather than at a location in the northeast quarter of Section 8?

A. At this time I can't support adequate reserves in the north part of that unit. So it would be -- I couldn't justify an economic well.

Q. The 5-1 should pay out, shouldn't it?

A. The 5-1 should pay out, but there's not enough reserves remaining, and your cumulative production from the 5-1 currently is at about .6 of a B, and the ultimate recovery of that area is going to be 1.2 BCF, so that a new well sharing in that remaining .6 BCF of gas would not be economical, as we understand the reservoir today.

Q. And there has been a substantial decline in the bottomhole pressure of that well, has there not?

A. That is correct, and --

Q. Now, in looking at the production data on Mr. Lowe's Exhibit 6, there are better wells closer to your proposed location in the southwest of the southeast than if you move the well to the north; is that correct?

A. That is correct.

Q. And based on the geology, does your engineering support the well in the southwest of the southeast?

A. Yeah, based on the reserve study we've done in that area, the remaining reserves in that area of the reservoir would support an economic well.

Q. Now, another factor -- and I don't think it's reflected on these exhibits, Mr. Payne -- in the west half of Section 9, has there been a well recently drilled there?

A. Yes, there has.

Q. Where was that well located?

A. It's in the northwest quarter section. Ocean has

a small interest in that. It's underneath the yellow square there. That's called the -- It's the Mewbourne Oil Eureka 9-1.

Q. That was drilled by Mewbourne Oil Company?

A. That is correct.

Q. And Ocean participated in the well?

A. Yes, we did.

Q. And what were the results of that well?

A. It had not sand development. It's also suggestive that the reservoir is not as extensive in that area.

Q. And that's another reason not to drill in the northeast quarter of Section 8?

A. Absolutely. I'd also point out the Mewbourne well shown on Exhibit 6, in Section 18, in the northeast quarter section. It was recently drilled in and amongst wells that have been produced since the 1970s with these, you know, 11 BCF of cum and 9 BCF of cum. It found a bottomhole pressure of only 1000 pounds, yet it looks like it's going to produce 2.5 BCF of gas.

Q. That's the well that has -- the bottom number is 1386 under it?

A. Yes, that's the current cumulative production. The reserve estimate on that well is 2.5 BCF.

Q. Okay. So that encourages you to drill at your

location also?

A. That's right.

Q. Let's move on to your final exhibit, Exhibit 13. There's a lot of data on here. Could you go through that for the Examiner?

A. Yeah, I don't want to go through each and every well, but what it is is using the data available through the state reporting system, it just shows pressures versus time in the area of interest, and it shows that these wells are in generally producing from a common reservoir. The reservoir pressures drop in a pretty good trend.

Q. Okay, it's what you'd expect to see when you drill a well out here?

A. Yes, I would expect to see partial depletion. And in fact, the Texaco State 5, referring back to Exhibit Number 10, the original pressure when it was drilled was estimated at 3210 pounds average pressure, which is significantly below the original reservoir pressure of the area of about 5000 pounds.

Q. Okay.

A. So even though it was quite a distance away from any significant production, it had seen some pressure depletion.

Q. Okay. I mean, you would expect pressure depletion even at your proposed location?

A. Absolutely.

Q. But on the other hand, geologically and engineeringwise it would be better than the northeast quarter where you are closer to a -- not a great well and a dry hole?

A. That's right, the tank is in the south. That's where the thick sand is at, and that's where the geologic and engineering data support the most economical well.

Q. Were Exhibits 9 through 13 prepared by you or under your supervision?

A. Yes, they were.

Q. And in your opinion is the granting of Ocean's Application in the interests of conservation and the prevention of waste?

A. Yes, sir.

MR. BRUCE: Mr. Examiner, I'd move the admission of Ocean Exhibits 9 through 13.

EXAMINER BROOKS: Objection.

MR. CARR: No objection.

EXAMINER BROOKS: Ocean 9 through 13 are admitted.

Mr. Jones, do you want to take on this witness?

MR. CARR: I'd like to --

EXAMINER BROOKS: It's in your area of expertise.

MR. CARR: Mr. Examiner, I'd also like to cross

this witness.

(Laughter)

EXAMINER BROOKS: Oh, I'm sorry, Mr. Carr, you get first cut. Go right ahead, I apologize.

MR. BRUCE: I object.

(Laughter)

MR. CARR: I will assume that that does not reflect on your opinion of my ability to cross-examine this witness in the least.

(Laughter)

CROSS-EXAMINATION

BY MR. CARR:

Q. Mr. Payne, I'd like to direct your attention to the well in the southeast corner of Section 5. That's the Ocean Texaco -- what is that, the 5-1?

A. Yes, sir.

Q. I think you indicated that you had been interested in drilling down in the southeast quarter of Section 8 for sometime.

A. Yes, sir.

Q. Well, your interest down there predated the time that you actually drilled the well in the south half of Section 5; isn't that correct? I thought Mr. Messa said it was back in the end of 2000 that you were actually starting to --

A. The Texaco well was drilled in 2001. It was actually drilling when I hired on with Ocean Energy, and I personally didn't get involved with that prospect.

Q. It's a fairly good well?

A. It's a fairly good well. It's -- you know, at 1.2 BCF I would say it's a below average Morrow well.

Q. And producing 267 MCF a day at this time?

A. 267 MCF a day, that sounds correct.

Q. It's 660 feet off of the north line of the spacing unit in the east half of Section 8; is that correct?

A. Yes, sir.

Q. In your opinion, is the Texaco 5-1 well draining reserves from the northeast quarter of Section 8?

A. I think that's a possibility, yes, sir.

Q. If I understood the testimony, the location in the southeast quarter is preferable because it's actually in a thicker portion of the reservoir; is that correct?

A. Yes, sir.

Q. Isn't the location proposed by Mr. Arrington in the northeast quarter in a thicker portion of the reservoir, as mapped, than the Texaco 5-1 well in the south half of Section 5?

A. No, sir.

Q. Aren't there locations in the northeast quarter

that would be thicker?

A. No, sir, not to my understanding.

Q. How thick is the section in the 5?

A. I think we may -- You know, as a reservoir engineer I define thickness as the container, the average thickness over the drainage area. The thickness of the wellbore itself is not as important as the area which I'm draining.

So if you look at the location where we spot the well, the reservoir is much thicker. That's getting into the heart of the reservoir and where you'd want to place your well for optimum drainage purposes. Up in the neck of the sand where you see the rapid pressure decline in the Texaco 5 and in that area, suggesting that the reservoir, although it may be thicker, but it's not as extensive.

Q. If we look at the well in the south half of Section 5 --

A. Yes, sir.

Q. -- how thick is the formation there?

A. In the south half of Section 5?

Q. Uh-huh.

A. Seven feet, if I recall correctly.

Q. And how thick would you say the formation is at the Arrington location in the northeast of 8?

A. I don't know. I don't know where the Arrington

location is at.

Q. If you -- You haven't compared that location?

A. We've looked at several locations and discussed some locations. The last location I personally was involved with and discussed with Arrington was not -- if I recall correctly, was still in the southeast quarter.

Q. If we -- You said you had how many feet in the well in the southeast of 5? Just a minute ago.

A. Yeah, I said 7 feet, the map is showing 5 net, 6 gross.

Q. Okay. If we look at the northeast of Section 8, there are areas where they're -- based on Ocean's own mapping, the formation is at least 30 feet thick; isn't that fair to say?

A. Yes.

Q. Okay. And so there are locations in the northeast which would be substantially thicker than the location in the 5-1 well? That's all I'm trying to ask.

A. Yes, sir, that's correct.

Q. Now, when you talked about these wells -- And that well may be draining down into the northeast quarter; I believe that was your testimony?

A. Yes, sir.

Q. You looked over in Section 9 at the Mewbourne well -- that was a dry hole -- and you said that would

further discourage you from developing in the northeast quarter; is that accurate?

A. That's correct.

Q. I didn't hear you mention the well that has been drilled by Texaco in the southwest of Section 4. Did we discuss that well?

A. No, we have not.

Q. That's a recent drill, is it not?

A. Yes, it is.

Q. And it's in the channel -- or in the structure or the isopach as mapped by Ocean; isn't that true?

A. As -- mapped as 12 feet, 14 gross.

Q. And isn't that well producing now 2 million a day?

A. I'm not sure what the current production is, but the reported initial production was 2 million a day, and I do believe it's a significantly better well than our Texaco 5 well.

Q. And it's got about twice as much thickness, based on your mapping, as your Texaco 5-1?

A. Yes, sir.

Q. And we could get maybe three times that again by moving down into the northeast of Section 8; isn't that right, just in terms of thickness?

A. Well, again, you were talking about the thickness

at the wellbore where you're looking at the drainage in the area. My reserve estimates of that well in my data is somewhat limited on the Texaco Shoe Bar 4-2, suggests that it's draining those reserves rather rapidly.

If you look at the production plot on -- I'm showing on Exhibit 11, you'll note that you have a significant change in the decline curve in the second half of 2002. That was the result of the production from that Shoe Bar 4-2 well.

Q. So do you believe that -- In that Shoe Bar 4, that's the well in Section 4?

A. Yes, I think we would have --

Q. That could also be draining from the northeast; isn't that right?

A. Yes, sir, I do believe that's possible.

Q. Now, have you made any estimate of the pressure that might be available to a well in the northeast quarter of Section 8?

A. Current operations on the Texaco 5 as the well was producing -- It's not currently producing 260 MCF a day. I misspoke. We performed an acid -- what we call an isotrol treatment on the well this week to try to enhance the production to the best of our ability.

During that operation we noted a shut-in tubing pressure, fluid in the well, of 650 pounds. I have not

confirmed that with a dip in pressure, but if that is accurate then my current reserve estimates of 1.2 BCF may be optimistic.

Q. Okay.

A. So bottom line, your answer to the question what the pressure is, I think it could be 600 pounds.

Q. In the northeast quarter?

A. Yeah, 600 to 1500 pounds would be my range.

Q. Now, if we look at your Exhibit 10 -- this is on your well, the 5-1 -- you initially encountered a 2981-pound pressure in that well; is that right?

A. Yes.

Q. And what is the bottomhole pressure in the Well 4? Do you know what that would be?

A. It was reported to me when they drilled it, it was reported at 2400 pounds.

Q. Now, if we then look at your plots for the wells, I believe this plot -- it's Exhibit 13 -- is for wells down to the south and west of your location, your proposed location?

A. Yes.

Q. What is the current pressure range for those wells?

A. Can you ask that question again, please?

Q. If I look at the curve, it seems to me that if I

go over and start looking at the wells that are depicted on Exhibit 13 --

A. Yes, sir.

Q. -- these are the wells basically south and southwest of the spacing unit --

A. Yes, sir.

Q. -- we're talking about --

A. Yes, sir.

Q. -- and those pressures have dropped down to what? About 900 pounds?

A. Yes, sir.

Q. And so we have 900 pounds down offsetting your location and we have something in the neighborhood of 2000 pounds offsetting the Arrington location?

A. My best estimate, I believe I said, was somewhere between 600 and 1500 pounds, in our -- in the offset to --

Q. You would agree with me that there are substantially higher pressures north?

A. 600 to 1500. They could be lower or could be, you know, 1500 --

Q. We only have your numbers.

A. Right.

Q. You have 900 south and you have what, 1600 north?

A. That's the high side.

Q. And -- I'm just asking you for your numbers.

What are they?

A. I believe I said that I felt that the pressures in the north half of that unit, in my opinion, would be somewhere between 600 pounds and 1500 pounds. It could be substantially higher --

Q. Do you have anything --

A. -- 900 pounds.

Q. Do you have anything to support a 600-pound pressure north of this unit, north of this spacing unit?

A. Yes, sir, the shut-in tubing pressure on the Texaco State 5 that we just collected a few days ago is suggestive of the lower pressure.

Q. Okay.

A. And I'd like to also add that the -- you know, pressure in itself, it's just not the only measure of the reserve potential. It's the size of the reservoir. A thousand pounds pressure in a bigger tank will yield a lot more reserves than a 1000-pound pressure in a smaller part of the reservoir.

Q. Wouldn't you agree that a well with 30 feet of pay as mapped at the same pressure as a well with five to six feet of pay as mapped would produce substantially more?

A. Not necessarily.

Q. Let me ask you this. If no well is drilled in the northeast quarter, the reserves in the northeast

quarter are going to be drained, are they not? By some other well?

A. I believe that's correct.

Q. And the only other well would be the Ocean-operated well in Section 5, and the Texaco-operated well in Section 4; isn't that right?

A. No, I don't think that we've ever testified that it would -- Currently I could not economically justify a well in that northern --

Q. I'm not -- I'm asking you if --

A. That doesn't mean that we're not going to -- that a well won't be --

Q. If you don't understand my question, tell me and I'll restate it. But my question is this: It was my understanding that you said if no other wells are drilled north of this spacing unit, that reserves will be drained from the northeast quarter of Section 8; is that right?

A. Yes, sir.

Q. And if there are no other wells drilled up there to drain those reserves, there are only two; isn't that right?

A. No, I believe the well that we're proposing to drill would also drain those reserves.

Q. Is that north of the northeast quarter?

A. No, sir. The location that we're proposing would

also --

Q. I'm not asking you about your location. I'm asking you about the northeast quarter. And if there are no other wells, what wells will drain those reserves?

A. Reserves from the northeast quarter?

Q. Yes, sir.

A. Yes, I believe the well we're proposing will drain the reserves, as well as those wells to the north in Section 5 and Section 4.

Q. So you're saying a well 660 out of the southwest quarter of this unit will drain the northeast quarter as effectively as a well 660 feet from the line?

A. No, not necessarily.

Q. Well then, what are you saying?

A. I think that you can drain some of those reserves, as demonstrated by the original pressure on the Texaco 5 was at 3200 pounds when it was drilled, and there was no other well over a mile away when that well was drilled. Yet, you know, nearly 50 percent of the reserve potential had already been drained. So yes, these wells can drain over a large area.

If you locate your wellbore in a very thick portion of the well where your abandonment pressures are very low, I think that you could potentially recover significantly more reserves than what we will in the Texaco

5.

Q. Let me ask you this. If you are designated operator and prevail in this case, is Ocean prepared to drill two wells in the east half of Section 8?

A. Currently I couldn't justify an economic well in that quarter section.

MR. CARR: That's all I have, thank you.

EXAMINER BROOKS: Well, Mr. Jones, I'll let you go ahead of me.

EXAMINATION

BY MR. JONES:

Q. I'll be brief here. This Texaco State 5-1 in about the third quarter of '02 took a drastic hit on their reserves, I can tell. And you're saying that was the effect of the Chevron Shoe Bar 4-2?

A. Yes, sir. That well was completed and brought on line in May of 2002.

Q. Okay. Is that because of proximity, or is that because of heterogeneity, in other words, maybe a southwest-northeast permeability trend there or --

A. I'm not -- I couldn't -- I'm not aware of any permeability preferences in one direction or the other. The sand, when you catch it, is very permeable. We've got rotary sidewall cores, and our Texaco 5 well is suggesting 5 millidarcies of permeability.

So I think it's -- you know, when you catch it, even a thin sand -- We've got examples of four or five foot of sand producing 11 BCF and 40 foot of sand producing 5 BCF. So I think it's more important to be near or close to the tank, the big part of the sand, for you to maximize your reserve recovery.

Q. Okay. Speaking of that, there's some other red intervals colored in on this cross-section. Are there other Atoka and possibly even Morrow intervals that you might get preferably by drilling in the southeast quarter versus the northeast quarter?

A. I have not been made aware of any potential significant reserve accumulations in any other sand other than the Brunson. I know the Fat Lady does pay to minor quantities in the area, but it's not been considered in our economic evaluation.

Q. So you don't ever plan on -- That State 5 Number 1 had a significant -- it did have some of that sand in the upper Atoka show up. So is that -- and it didn't seem to show up as much in the wells to the south and the west. Can you possibly anticipate, if you did drill up in the north and the east, that you might hit -- have a better chance of getting that?

A. I have not see any geologic interpretation on it, and the completions that I'm familiar with for that sand

are very limited reserve potential. But that could -- Pending that geologic interpretation, that could encourage us to drill there.

Q. And there's no other bailout zones that would preferentially convince you to drill where you're at, like maybe the Abo? Because the North Vacuum-Abo is real close to where you're --

A. We're down off --

Q. -- a few miles away, I guess.

A. Yeah, we're down off the structure here, so --

Q. Okay.

A. -- all these reservoirs would be stratigraphic traps. And again, I'm not -- This is the only target that I've been made aware of.

EXAMINER JONES: Okay, pass. That's all of my questions.

EXAMINATION

BY EXAMINER BROOKS:

Q. Mr. Carr asked you about drainage from the northeast quarter, and you said that it could be drained by -- the Texaco 5-1 could be drained by the Shoe Bar 4-2, and it could also be drained by your proposed Dirt Devil 8-1.

A. Yes, sir.

Q. Which make sense to me. But Mr. Carr then also asked if a well that's 660 feet from the line wouldn't

drain a lot more than a well that's -- what? Almost half a mile from the line, at 1980 feet from the line. And that also seems to make sense to me.

But it seemed to me you had an explanation of why you thought that might not necessarily be true, that the Texaco 5-1 might not necessarily drain substantially more from the northeast quarter than what the well down in the southeast quarter -- I didn't really follow that explanation, so I wanted to try again.

A. Okay, well -- and I probably wasn't very clear.

Q. Well, I'm not very knowledgeable, so...

A. These reservoirs, you can take them to very abandonment pressures. We're talking about trying to -- You know, our expected bottomhole pressure in our well is -- if we get 1000 pounds, we'll be very happy. And to be successful, we're going to need to have an abandonment pressure that's below 100 pounds, p.s.i.

So if you can catch a good, high-permeable, high-quality sand, you can deplete the reservoir to a much, much lower abandonment pressure. If you have a thin well that maybe is not as permeable, then your abandonment pressures are much, much higher, such that you would be able to produce more reserves out of the reservoir. I don't know if that was any clearer or not, but I can try it again.

Q. Okay, what you're saying is, because you

anticipate higher permeability down in the southeast that --

A. It's a combination of thickness and permeability both. If you have 5 millidarcies of perm and only 2 foot of sand --

Q. Right.

A. -- you're at the economic rates that you can produce the well, and you have to shut it in because the well becomes uneconomic. But if you have 40, 50 foot of sand with that same permeability, then you can continue to produce the well at economic rates for much longer and, in effect, have a much lower abandonment pressure.

Q. And because you can continue to produce the well at the lower pressures -- Is that what you're saying?

A. Yes, sir.

Q. Because you can continue to produce the well for a longer period of time as the reservoir pressure goes down, then maybe you can draw more out of that reservoir than a well that will reach economic limit sooner?

A. Yes, sir, and the well is located closer to the tank, to the big part of the reservoir where the majority of the production is currently being produced.

Q. And what you're saying is, because the zone is thicker and the permeability is higher, then even at lower pressures you can continue to produce that well before you

reach the point where the lifting costs exceed what you're producing?

A. Exactly.

EXAMINER BROOKS: Okay, I think I understand the logic of that.

Any follow-up, anyone?

MR. BRUCE: I have a question or two, Mr. Examiner.

EXAMINER BROOKS: Go ahead.

REDIRECT EXAMINATION

BY MR. BRUCE:

Q. I just want to clarify something, Mr. Payne. Based on the geology, you think the reservoir is there in the northeast quarter?

A. Yes, sir.

Q. But based upon the pressure, et cetera, you can't economically justify drilling the well in the northeast northeast?

A. Certainly not at this time.

Q. And looking at your Exhibit 11, which is your decline curve, your well is obviously being affected by the well in Section 4; is that correct?

A. Yes, sir.

Q. And so if you drill another well there, you'll have basically three wells, oh, a couple of thousand feet

apart, combined, from each other?

A. Yes, that's correct.

Q. I mean, basically three wells in the space of 120 acres or so, or maybe even less?

A. Yeah.

Q. And if you drill in the southeast quarter you don't have that same well concentration, do you?

A. No, sir.

Q. So you would hope to have, number one, thicker reservoir, based on the geology, and you would not be affected as much by the pressures; is that fair to say?

A. Well, the pressures are going to probably -- may be as low or possibly even lower, but the reservoir should be a lot thicker in that area, which will more than compensate for that lower pressure.

Q. And that's evidenced by the Mewbourne well?

A. Absolutely, correct. In the current production, all those wells to the south are producing, and producing in greater quantities than our Texaco 5 well is, and they've been on line for 20, 30 years. So that's very suggestive that the tank is to the south, not to the north.

MR. BRUCE: Thank you.

MR. CARR: I just want to follow up on one thing that Mr. --

EXAMINER BROOKS: Go ahead.

RECROSS-EXAMINATION

BY MR. CARR:

Q. Mr. Payne, you said that it wouldn't be wise to put a well in the northeast quarter, because then you'd have three wells in fairly close proximity to each other producing these reserves; is that right?

A. That would -- I think that -- Currently, that's my understanding of the reservoir, that's correct.

Q. Would Mr. Arrington share in any of the reserves without that third well?

A. Excuse me, say that question again.

Q. Would Mr. Arrington share in any of the reserves produced without that third well?

A. Certainly he would. He's got reserves in the well that we're proposing to drill.

Q. So he gets a share of what you get out of the southeast quarter, while the reserves in the northeast are drained by wells to the north?

A. No, I think I testified that I believe that our well can drain those reserves.

MR. CARR: Thank you.

FURTHER EXAMINATION

BY EXAMINER BROOKS:

Q. Now, let me get this clear. Are you suggesting that even though -- Are you suggesting that regardless of

the fact that it may not be worth the drilling costs of two additional wells, are you suggesting that if you drilled two additional wells, that they would actually result in less production than --

A. No, sir.

Q. -- less total production than from the existing well plus one more?

A. No, I'm referring to economics.

Q. Okay, so --

A. No, you're absolutely correct.

Q. -- you're not suggesting that there would be reservoir damage or depletion of drive pressure or anything like that as a result of drilling two wells in this unit?

A. No, sir, ultimately I think all those reserves will be drained adequately from the existing wells in and out of our unit, and an additional well would only increase the recovery under that tract but not improve the economics of that tract.

Q. Yeah, so all of the reserves will be drained from out of the northeast quarter, but some of them will be drained by wells located off of that quarter section?

A. Yes, sir, they will.

EXAMINER BROOKS: Any follow-up from anybody?

MR. BRUCE: I have no further questions, and that ends my direct case.

EXAMINER BROOKS: Mr. Jones?

EXAMINER JONES: No.

EXAMINER BROOKS: Very good. Mr. Carr, you may call your first witness.

MR. CARR: At this time we call Enick Diffee.

EXAMINER BROOKS: Off the record.

(Off the record)

MR. CARR: May it please the Examiner, much of our presentation is consistent with what was previously presented, and we will try to move this along and not just repeat things that have been previously said.

EXAMINER BROOKS: That will be appreciated.

ENICK DIFFEE,

the witness herein, after having been first duly sworn upon his oath, was examined and testified as follows:

DIRECT EXAMINATION

BY MR. CARR:

Q. Would you state your name for the record, please?

A. Yes, my name is Enick Diffee. And Mr. Examiner, that's spelled E-n-i-c-k D-i-f-f-e-e.

Q. Mr. Diffee, where do you reside?

A. Roswell, New Mexico.

Q. By whom are you employed?

A. I am a self-employed independent petroleum landman.

Q. And what is your relationship to David H. Arrington Oil and Gas in this matter?

A. I work for Arrington on a consulting basis.

Q. Have you previously testified before the New Mexico Oil Conservation Division?

A. I have.

Q. At the time of that testimony, were your credentials as an expert in petroleum land matters accepted and made a matter of record?

A. Yes.

Q. Are you familiar with the Applications filed in this case by Mr. Arrington and by Ocean?

A. Yes, sir.

Q. Are you familiar with the status of the lands in the area which is the subject of this Application?

A. I am.

MR. CARR: We tender Mr. Diffee as an expert in petroleum land matters.

MR. BRUCE: No objection.

EXAMINER BROOKS: So qualified.

Q. (By Mr. Carr) Would you briefly state what Arrington seeks with this Application?

A. They're seeking an order pooling all minerals from the surface to the base of the Mississippian formation under the following described acreage, which lies in

Section 8, Township 17 South, Range 35 East, in Lea County, and the lands would be the east half for all formations and/or pools developed on a 320-acre spacing, which includes the Undesignated North Vacuum-Atoka-Morrow Gas Pool, and also the northeast quarter for all formations and/or pools developed on 160-acre spacings, the proration unit to be dedicated to the Pink Cahill State "8" Well Number 1, and this well will be drilled at a standard gas well location, being 1300 feet from the north line and 990 feet from the east line, which is Unit H of Section 8.

Q. Mr. Diffee, have you prepared exhibits for presentation here today?

A. Yes.

Q. Would you refer to what's been marked as Arrington Exhibit Number 1 and identify that?

A. Yes, we've prepared a plat, and I'll draw your attention to the east half of Section 8. You'll see colored in yellow, being the east half of the east half, the oil and gas lease that was recently acquired by Arrington in January of 2003 from the State of New Mexico. The 320 acres would also consist of the west half of the east half, and the west half of the east half if also State of New Mexico oil and gas leases.

Q. Mr. Diffee, you were present for Mr. Maney's testimony concerning the ownership in the area?

A. Yes.

Q. Do you have any disagreement or anything that -- in terms of your presentation that would differ from the ownership as presented by Mr. Maney?

A. I agree with Derold's ownership as to the west half of 8. I would just simply make the point that in the south half of Section 5 I show Texaco to still own a 25-percent interest in that lease. But for the sake of this hearing, I'll agree with Mr. Derold Maney's ownership of 100 percent.

Q. Mr. Arrington doesn't own anything in the south half of 5?

A. He does not.

Q. Let's go to what's been marked as Exhibit 2. Could you identify that, please?

Before we do that I want to ask you, if we are -- if Mr. Arrington gets a pooling order, at this point in time have you been able to reach an agreement with any other interest owner in the spacing unit?

A. Arrington, of course, owns 100 percent in the east half, east half. And of course we're at a dispute covering the west half of the east half.

Q. And the owners in the west half are standing with Ocean on their proposal. We have our 50 percent in the east half?

A. That's my understanding.

Q. Okay. Could you go to what has been marked as Exhibit Number 2 and review that for the Examiner, please?

A. Yes, Exhibit 2 is a copy of the certified letter that was dated January 27th of 2003, in which the Pink Cahill State "8" Number 1 well was proposed. The location of this well initially was 1980 from the north line and 1990 from the east line, and the well was proposed to a total depth of 12,800 feet, and the proration unit was identified as being the east half of Section 8.

And also as a part of the package was a copy of the AFE that had been prepared by Arrington's technical staff, and a copy of the AFE is also attached for your review.

Then of course McCombs Energy, LLC, was sent a well proposal along with an AFE, and Nadel and Gussman Permian, LLC, was sent a letter again proposing the well, attached with an AFE.

Then I bring your attention to a letter dated February the 28th of 2003, and this is a letter from Arrington's office stating that they would like to amend the location of the well to again a standard location of 1300 feet from the north line and 990 feet from the east line. And as the letter states, we felt like that we were in a competitive position as to the reserves that existed

from the south half of Section 5 extending south into the northeast quarter of Section 8. And letters, of course, were sent to Nadel and Gussman and McCombs Energy.

Q. Mr. Arrington acquired the lease on the east half of the east half of 8 at the state lease sale January 21st of this year, did he not?

A. Correct.

Q. And then he proposed the well January the 27th, 2003?

A. Yes, and it's my understanding that not only was it sent by certified mail, but the letter was also faxed on the same day.

Q. Let's go to what has been marked as Exhibit Number 3. Would you just identify that, please?

A. Yes, this is the AFE proposed for the Pink Cahill State Number 8.

Q. And what are the costs as reflected on that AFE, both drilling and total?

A. The dryhole cost, $923,850, and the completed well cost of $1,401,360.

Q. Is Arrington Exhibit 4 a copy of the accounting procedures for joint operations from -- the standard COPAS form?

A. Yes.

Q. Does this form provide for the periodic

adjustment of overhead and administrative costs?

A. It does.

Q. Does Mr. Arrington requests that if he prevails in this case that the order authorize the adjustment of these costs in accordance with these COPAS procedures?

A. Yes.

Q. And have you made an estimate of the overhead and administrative costs while drilling this well and also while producing it, if it is a success?

A. Yes, it would be $6000 per month and $600 a month, and according to our recent review of the 2002/2001 Ernst and Young survey these amounts are below the average and median cost for wells drilled to this depth.

Q. These are also the figures that are being proposed by Ocean?

A. That's correct.

Q. So there's no dispute as to overhead costs?

A. Absolutely.

Q. Does Mr. Arrington seek to be designated operator of the well?

A. Yes, he does.

Q. Is Exhibit Number 5 an affidavit confirming that notice of this hearing has been provided in accordance with the Rules and Regulations of the Oil Conservation Division?

A. Yes, sir.

Q. Mr. Diffee, were Arrington Exhibits 1 through 5 either prepared by you or have you reviewed them and can you testify as to their accuracy?

A. Yes.

MR. CARR: At this time we'd move the admission of Arrington Exhibits 1 through 5.

MR. BRUCE: No objection.

EXAMINER BROOKS: Arrington 1 through 5 are admitted.

Mr. Bruce?

CROSS-EXAMINATION

BY MR. BRUCE:

Q. Mr. Diffee, just a couple of questions. Do you know why the well location was changed from 1980 feet from the north line to, I believe, 1300 feet from the north line?

A. You know, our technical staff, being present, is going to give you a more in-depth discussion of that, Mr. Bruce. But I know it was, again, based on the competitive nature of having, you know, the thought that reserves were being drained by the well located in the southwest quarter of Section 5.

Q. Now, Mr. Diffee, if Arrington Oil and Gas signed a JOA with Ocean as soon as Ocean's well is drilled, it could propose a well in the northeast of the northeast,

could it not, under the usual JOA?

A. It could happen.

Q. And do you recognize that under a force pooling order, a force pooling order only applies to one well?

A. I agree.

Q. And so even under a force pooling order they could propose a second well in the northeast of the northeast, could they not?

A. Under the terms of the standard JOA they could.

MR. BRUCE: Thank you, that's all I have.

EXAMINATION

BY EXAMINER BROOKS:

Q. Well, first of all, I need to clarify about this location. What is the location that you are currently proposing?

A. It would be the location of 1300 feet from the north line and 990 feet from the east line, Unit H.

Q. Okay, so the distance from the east line remains the same?

A. Yes, sir.

Q. But you're moving it 680 feet further north?

A. That's correct.

Q. Now, you said something about a letter in here that proposed the new location, and I couldn't find it while you were going through these. Can you tell me where

that is?

A. Yes, sir, attached as Exhibit 2 there are a number of letters, and if you would turn to the very back you will see the letter to McCombs Energy, and that's a letter dated February the 28th of 2003, and that's where we, in the first paragraph --

Q. Okay.

A. -- call your attention, "Based on this determination...Arrington...is revising the well proposal to a standard of 1300 from the north line and 990 from the east line."

Q. I see that, yes. Okay.

Mr. Carr asked you, does Mr. Arrington seek to be designated the operator, and you answered yes. Would it not be more correct to say that David H. Arrington Oil and Gas, Inc., seeks to be nominated as operator?

A. That would be correct.

EXAMINER BROOKS: Thank you.

Mr. Jones?

EXAMINER JONES: (Shakes head)

EXAMINER BROOKS: Very good, no questions.

Any follow-up?

MR. CARR: (Shakes head)

EXAMINER BROOKS: You may step down.

THE WITNESS: Thank you.

MR. CARR: At this time we'd call Bill Baker.

BILL BAKER, JR.,

the witness herein, after having been first duly sworn upon his oath, was examined and testified as follows:

DIRECT EXAMINATION

BY MR. CARR:

Q. Would you state your name for the record, please?

A. Bill Baker, Jr.

Q. Mr. Baker, where do you reside?

A. I reside in Midland, Texas.

Q. By whom are you employed?

A. David H. Arrington Oil and Gas, Inc.

Q. What is your position with David H. Arrington Oil and Gas, Inc.?

A. I am the exploration manager.

Q. Have you previously testified before this Division and had your credentials as an expert in petroleum geology accepted and made a matter of record?

A. Yes, sir, I have.

Q. Are you familiar with the Application filed in this case on behalf of Mr. Arrington?

A. Yes, sir, I am.

Q. On behalf of David H. Arrington Oil and Gas, Inc. Are you also familiar with the Application filed in these consolidated cases by Ocean?

A. Yes, sir, I am.

Q. Have you made a geological study of the area which is the subject of this Application?

A. Yes, sir, I have.

Q. And are you prepared to share the results of your work --

A. Yes, sir, I am.

Q. -- with the Examiner?

A. Yes, sir.

Q. Mr. Baker, what's the primary objective in the Arrington well?

A. The primary objective of this, sir, will be the lower Atoka-Brunson gas pay sand.

Q. So it's the same for both wells that are at issue here today?

A. Yes, sir, it's going to be the same sand.

Q. And as you go through your presentation, is it your position that a well is needed in the northeast quarter to protect this acreage from drainage from wells to the north?

A. Absolutely, yes, sir.

Q. If Ocean prevailed, Arrington could propose under a standard JOA a well in the northeast quarter; is that not correct?

A. Yes, sir, we certainly could.

Q. And what would happen?

A. We would end up having to operate the well down and then tender operations to Ocean.

Q. And once you drill the well you would then have to give up operations?

A. Yes, sir, we would.

Q. And is that an acceptable proposal to David H. Arrington Oil and Gas?

A. No, sir, it is not.

Q. Let's take a look at what has been marked as Arrington Exhibit Number 6. Would you identify this and review it, please?

A. Yes, sir, Arrington Exhibit Number 6 is a structure map on the top of the lower Morrow limestone out here. This is a well-recognized regional structural horizon out here that the majority of the geologists use as a structural horizon. The lower Atoka-Brunson sand sits almost directly on top of the lower Morrow limestone, so basically you could say that the structure of the lower Morrow limestone influenced the depositional patterns of the lower Atoka-Brunson pay interval.

On this particular map right here, I have shown all the lower Atoka-Brunson pay producers will be colored in orange. I have also indicated our proposed proration unit, being the east half of Section 8. I have indicated

Arrington's acreage in the east half of the east half of Section 8 is shaded in yellow. I've also indicated that there will be a cross-section, which is Exhibit Number 8 that I will get to shortly, that will be labeled cross-section A-A'.

This particular map basically shows that Arrington's location of the Pink Cahill State Number 1 will be located on the west side of a structural re-entrant. It is my belief that this structural re-entrant was part of the influence, depositional influence, of the lower Atoka-Brunson interval that I'll show.

Q. Mr. Baker, let's go to the isopach map --

A. Okay.

Q. -- and let's also at the same time take out the structure map, so let's look at Arrington Exhibits 7 and 8 together.

A. Okay, Arrington Exhibits 7 and 8 will actually be a net-interval isopach of the lower Atoka-Brunson interval, and then Exhibit Number 8 is a cross-section A-A'.

And prior to actually looking at the isopach, Mr. Examiner, I would like to just go through the cross-section first to familiarize yourself with the pay horizon. I know that Mr. Lowe and Ocean have already been through it, so we'll be basically looking at the same productive interval, but I will go through this cross-section first so that

you'll be familiar, and then we'll take a look at the isopach.

If you'll start on the left-and side of Exhibit Number 8, cross-section A-A', this well is located in the west half of Section 8, and this is the Mobil Oil Corp State Number 1 "NN". This particular well was drilled in September of 1976. The well has produced a total cumulative of 11.2 BCF and 112,000 barrels of oil.

My last reported rate on this well was 3 MCF of gas per day in February of 2002. At that time we showed an estimated bottomhole pressure in this well of approximately 300 pounds. And that is by *Dwight's* information that our reservoir will follow up with in his testimony a little bit later.

It is my understanding that this well has now been P-and-A'd, and this particular well was actually the well I believe that was holding the acres that Mr. Arrington leased later in January.

If you'll notice that it has an Atoka-Brunson interval -- and I'm sorry for the scale on this, Mr. Commissioners, it is a little bit small. But we basically showed 7 net feet of pay sand over a gross interval of about 10. And like I said, this well has made 11.2 BCF and has 300 pounds of bottomhole pressure.

Now, as you move to the right I am going to show

what we call a permeability barrier there, and I will discuss this a little bit later and the reasons for this in just a little bit. But basically I want to show a perm barrier between this particular sand and the wells located up in Section 4 and 5.

As you continue on this cross-section, you're going to see the proposed location for Arrington's Pink Cahill "8" Number 1, and this location is at a current location of 1300 feet from the north line and 990 from the east line.

We originally proposed the well at 1980 from the north line and 990. It was after multiple discussions with the Ocean technical staff, as well as getting with our technical people and our engineers and doing some sophisticated engineering, we determined that we actually felt like we needed to be closer to the wells in Section 4 and 5. And that was the reason why we sent a subsequent well proposal to Ocean, revising the location, is, we felt like we were being drained from wells in Sections 4 and 5, and we actually needed to be up closer to those wells.

Now, my original intent was to not be right up on the line for the very reason of sticking three wells, basically, in a 160-acre pattern. I was actually trying to back off enough to still be in what I considered to be a commercial geological position and encounter and recoup

unique reserves to Mr. Arrington's acreage down here.

So that is the reasoning behind where our proposed location is at and why we moved the location.

If you will move on, as you move to the cross-section, you will see Ocean Energy's Texaco State Number 1 in Section 5. And this well was drilled in August of 2001, and basically they encountered approximately -- I have it 6 and 8 feet, I believe they had it as 5 and 6 feet, of net pay in here. You can tell by the log characteristic that it's definitely a channel sand. It's got a fining-upward sequence; this is very indicative of a channel sand.

They IP at the well at 1.16 million cubic feet of gas per day at a flowing tubing pressure of 1400 pounds. We got the bottomhole pressure from Mr. Messa and Mr. Payne. They shared the information with us, and we got the estimated bottomhole pressure, 3200 pounds. I show that they've made a current cumulative of about .54 BCF, and I actually show their well making 550 MCF a day as of November, 2002.

I should also state for Mr. Payne's ego here that we actually show an EUR here of 1.1 BCF out of this well, and I think that coincides very closely with what Mr. Payne actually showed for this particular well.

But as you move on across to the Texaco, we show in Section 4 the Texaco E&P Shoebar "4" Number 2, and I

believe this well was drilled by Texaco as a direct result of Ocean's well drilled in Section 5. It's also my understanding that Ocean Energy doesn't have an interest in this particular well.

This well was drilled in 4-10 of 2002. They perforated the well, and as you can see, first of all, they encountered a much thicker interval. They actually got about 16 feet of sand. I show 11 feet of actual net pay in here. They perforated it and tested a rate of 2 million a day. Once again from Ocean's technical staff, we got the bottomhole pressure of approximately 2800 pounds. To date we show a total cumulative of .34 BCF, and I show the well in November of 2002 producing at a rate of 2.5 million cubic feet of gas per day and four barrels of oil. And we actually show an EUR of this particular well of 2.1 BCF.

As you continue on to the last well in the cross-section, this was Mewbourne's well, and this was most recently drilled, in February of 2003. And this particular well is a dry hole.

And as you can see, I have chosen -- They actually encountered some sand here. I discussed it with Mr. Messa, I don't know if specifically whether he considers this Brunson or not. I do not. I consider this an overbank deposit that's slightly higher in this section than the Brunson interval. If you'll look, it's actually

got a coarsening-upward sequence here. It looks different on the logs. No matter what, it was tight. They didn't have hardly any gas show in it. I don't recall whether they ran a drill stem test on it or not, but they did not complete the well in it.

EXAMINER BROOKS: You're talking about the well in Section 9?

THE WITNESS: Yes, sir, the Eureka State Number "9" well.

So basically, this pretty much shows what I consider to be the pay horizon that we're going after in this immediate area. And it was because of the Ocean well and the Texaco well that Mr. Arrington went to the state land sale in January. And basically we had actually gone out and scouted the Texaco well and the Ocean well and knew in January that the Texaco well was still producing in excess of 2 million a day. Okay?

With that, we felt that this was some pretty good acreage. And I mean this, by my standards -- and I'm an old Texas Oil and Gas geologist -- this is an old TXO corner shot, as we'd call it. Okay?

We went to the state land sale, and Mr. Arrington purchased the acreage. We were aware of Ocean being the other interest owners in here. And we felt because of depletion and because of what the Texaco well is producing,

what the Ocean well is producing, that we needed to propose a well as soon as possible, because with every day of their production we're losing reserves.

I know Mr. Payne was hesitant to say it's draining from the northeast quarter, but we know preferential permeability trends, that well is going to drain from the northeast quarter. And so right now, even as we speak here today, sir, we're being drained in our position.

Q. (By Mr. Carr) Mr. Baker, if there is no well in the northeast quarter, you will be drained?

A. Yes, sir.

Q. What would a well in the northeast quarter cost, based on your AFE estimate?

A. $1.4 million.

Q. And is Mr. Arrington prepared to drill a well and spend $1.4 million to obtain his share of the reserves from the northeast quarter of the section?

A. Yes, sir, we definitely are. Yes, sir.

Q. Do you believe that the location proposed by Ocean in the southwest of the southeast is a poor location?

A. I simply believe that it's got a geological shot, but they will have a bottomhole pressure, we're estimating, in the 500-pound to 600-pound bottomhole pressure range.

Q. If Mr. Arrington is designated operator of the

east half, is he also prepared to drill a well at that location?

A. Yes, sir, we are.

Q. Are you prepared to make a recommendation to the Examiner as to the risk penalty that should be assessed against any interest owner who doesn't voluntarily participate in the well?

A. Yes, sir, I am.

Q. And what is that?

A. Two hundred percent, the maximum.

Q. And what do you base that on?

A. Based on that fact there is -- This is the Morrow, this is the Atoka-Morrow, it's risky, and Mewbourne found that out very shortly. So we can drill a dry hole.

Q. In your opinion, will granting this Application be in the best interests of conservation, the prevention of waste and the protection of correlative rights?

A. Yes, sir, I think so.

Q. How soon does David H. Arrington Oil and Gas plan to spud this well?

A. As soon as possible, sir.

Q. Were Exhibits 6 through 8 prepared by you?

A. Yes, sir, they were.

MR. CARR: I move the admission into evidence of Arrington Exhibits 6 through 8.

EXAMINER BROOKS: Objection, Mr. Bruce?

MR. BRUCE: I have no objection?

EXAMINER BROOKS: Arrington 6 through 8 are admitted.

Mr. Bruce?

CROSS-EXAMINATION

BY MR. BRUCE:

Q. Okay, just a few questions, Mr. Baker. What is, or was the virgin pressure in this reservoir?

A. More than likely, the virgin pressure in this reservoir was probably around 4000 pounds.

Q. You don't think 5000 pounds is a more accurate number?

A. No, sir, I have drilled probably 30 wells in this area, I've done extensive -- drilled from 1435 all the way down through 1735, and the highest I've seen in the Brunson was one well that was drilled by Kukui, and it had 4600 pounds. The majority -- normal pressure gradient in this area would give you a 4000-to-4200-pound bottomhole pressure.

Q. I hand you what's Ocean Exhibit 13. Do you disagree with the 5000-pound pressures on the --

A. No, sir, you can't disagree with two points of control at 5000 pounds.

Q. Regardless of whether it's 4000 or 5000, looking

at your Exhibit 7, your isopach --

A. Yes, sir.

Q. -- if there's permeability barriers, then why was -- the first well drilled in this -- you've got a permeability barrier to the south and a permeability barrier to the north, then why is the first well drilled in that little reservoir at 3200 p.s.i.?

A. Because that I have found -- and I have seen this in two or three different wells -- these permeability barriers are basically where the sands get down to probably less than five feet. But it means the sand doesn't completely go away. So you're going to see some pressure movement across it.

I've actually offset a well that had 800 pounds and had 2600 pounds, and there was no way to explain that well other than some tight sand in there.

I'm not saying that there's not some communication across here, but these are fine to medium-grain sands. And actually -- We talk about great permeability. It's got great porosity and very low perm.

We create the perm. If you'll look at all these wells out here, the majority of these great big, thick ones, nowadays we have to frac these wells, and Yates has shown that over and over again, to create that perm.

Q. Now, based on the testimony you just gave, the

Chevron well in Section 4 --

A. Yes, sir.

Q. -- has better net thickness, does it not?

A. Yes, sir, it sure does.

Q. And it started out with a lower pressure --

A. Yes, sir.

Q. -- than the 5-1, but it has better reserves --

A. Yes, sir.

Q. -- in your opinion?

A. Yes, sir.

Q. Doesn't that prove what Mr. Payne was saying, that if you have the thicker reservoir, that's more determinative than the pressures?

A. Well, it certainly can be, but I'm not concerned really about Ocean's location to the south as I am -- as getting in my share of the reserves in the northeast quarter.

Q. Well, isn't -- Ocean's location, which also affects you in the southwest of the southeast, couldn't you say the same thing, that that's being drained by the wells in Sections 17 and 18?

A. Actually, Mr. Bruce, me and our reservoir engineer determined that that well should have been drilled 10 years ago. That would have been a very good location. So yes, sir, it's drained. And it's continuing to be

drained.

Q. Okay. So the northeast quarter is being drained and the southeast quarter is being drained?

A. Yes, sir.

Q. That's all I have -- One other question.

On your Exhibit 6 -- I need new bifocals -- the well name, it looks like it's the Fink Cahill?

A. No, sir, that's Pink. You do need new bifocals, Mr. Bruce.

(Laughter)

THE WITNESS: That's Pink. Yeah, you did that on purpose.

MR. CARR: May it please the Examiner --

MR. BRUCE: No, no, we're not going into well names again, Mr. Carr.

MR. CARR: -- the last time Mr. Bruce and I had an issue with well names we finally agreed that when Mr. Arrington named a well the Red Eyed Squealy Worm it was being named after Mr. Bruce.

(Laughter)

MR. CARR: We are prepared today to stipulate that that was not true. The Fink well is --

(Laughter)

EXAMINER BROOKS: Well, it's getting late in the afternoon.

THE WITNESS: Yes, sir.

EXAMINATION

BY EXAMINER BROOKS:

Q. Mr. Baker, you said you thought there was a permeability barrier between the well that's over in the west half of Section 8 and the wells up in the north, and I can understand why you would think that. But what makes you think it is located across the east half of Section 8, the way you've drawn it?

A. Geological discretion, sir. There's no particular basis that I have at that. We feel -- I think us and Ocean both agree that that sand -- This main big body was fed from the same feeder system --

Q. Right.

A. -- but I'm saying because of the pressure differential between -- I mean, even the 3200 pounds is substantially higher than what the bottomhole pressure in this big tank that Mr. Payne talked about. There has to be something in between there, in my opinion, that is causing that pressure to be there.

Now, whether that perm barrier is there, it could be at the Pink Cahill, and that would add to my 200-percent risk, and I'd just drill a dry hole because that perm barrier moved up to there.

Q. Yeah. You've drawn -- Your contour map looks

very similar the other gentleman's, but your isopach looks very, very different. Can you give me any supporting data for -- or reasoning for why you think that these thicknesses are more nearly in accord with the way you've drawn them, which is quite different from the way Mr. Messa drew them?

A. Well, actually, I believe that pretty much industry standard is, drill this Brunson interval -- It's been the main target out here for the last five years.

Q. Right.

A. And I've probably looked at a half a dozen other geologists' interpretations. As a general rule, we all believe these are pretty much north-south-trending systems.

The one exception is, when you get down to the Vacuum system right here, there is actually a huge high that sits just south, and there's a fault system, and all these things fed into here and slammed up against this Morrow high in here, and that's what kind of reworked these sands almost in an east-west or northwest-southeast pattern, is they were reworked along here.

Q. Now, that high would be south of these wells in Section 16, 17 --

A. Yes, sir, I mean, it's just south of it off this map right here. Everything really climbs dramatically, so that this was -- I mean, you kind of had a roll over here,

and then it really climbed up --

Q. Right.

A. -- and I think that's what's banked all this sand up against here, and it kind of changed it. And I believe in Mr. Messa's interpretation, Mr. Lowe, they chose to take their sand -- I went north with mine through 5 and 6, and they chose to continue on in a northwest pattern, is the main difference, in the big, thick sand, as he said, and out that way.

There's no particular rhyme or reason. I actually stayed within the constraints of these wells up here in 31. I also have 1000 pounds bottomhole pressure, and the reserves are only a BCF out of some pretty thick wells up here.

So once again, that might lead me to believe that it was more tied to Mr. Payne's tank than something separate, you know.

That's just the discretion of each geologist as to how he wants to explain it and interpret it.

EXAMINER BROOKS: Okay. Mr. Jones?

EXAMINATION

BY EXAMINER JONES:

Q. Mr. Baker, the trend you have for the -- in Section 8 up to Section 4, that little lens of sand, that's -- Does that go along with your regional geologic

prediction of the Morrow meandering sands, or -- and have you seen that in other areas?

A. Well, Mr. Commissioner, that's a good question. There is areas where these things appear to get down as low as a quarter to a half a mile wide, and some of them I've got up in 16-35, in Sections 10 up there, and 14, appear to be a mile and a half wide.

But also up there the well control is so thick you can't put dry holes in between them, but yet you've got pressure differentials in there.

So once again, this thing could be a little bit wider. We know it can't be much wider to the east, Mewbourne proved that. There is a little discretion. This thing could balloon out a little bit more to the north and the west as you head on up that way.

The fact that Texaco's well only encountered 16 feet -- This is actually more normal thickness as you move north.

The Brunson is typically a 15- -- 10-, 12-, 15-foot interval, until you get down in this area here where you get this big pod of sand that Mr. Payne actually talked about.

So once again, that's hard to answer. I've seen them both.

Q. And these perm barriers are -- So some of this

Morrow is -- you're talking secondary changes into actual original deposition, so perm barriers could be some kind of secondary silts coming through?

A. There might be. One thing about the Atoka-Brunson that we have seen, as a general rule, is that this is a very fine- to medium-grained sand. And as you approach the edge wells, I mean, it almost gets silty. Well, now we really haven't seen evidence of major clay deposits. We have seen evidence of, believe it or not, some dolomite recrystallization in some cores that we took up north.

So there's possibility of some secondary stuff going on in here. I can't say that happens everywhere consistently, we've just seen it periodically. And I've seen over and over -- I mean, there's a well directly north off this map here in Section 4 that has 800 pounds. And then you've got the two wells in 4 and 5 where Ocean and Texaco drilled that once again came in with high pressures again.

The well up there that had 800 pounds was a Yates well. Well, Arrington drilled a well north of it, the Palomino Midge, that had 2600 pounds. And stratigraphically they're the same.

Q. And these pressures pretty much build up over the same amount of time?

In other words, if it's extremely low permeability in some cases -- which is probably not the case with the Morrow, right? You would have to run along the --

A. Right, right.

Q. -- like slopes, Abo or something. Okay.

The source for the Morrow, what was that? Mississippian or something?

A. Well, no, sir, we don't actually believe it was Mississippian. We believe that -- There's two theories of the source, and the majority of the theories are that this stuff was sourced from the north somewhere, and that these were just part of a large distributary system coming down from the north.

There's a new system -- or a new theory now, that's actually saying that part of this was an erosional material coming off of the Vacuum high, coming from south of us, going off to the north. Okay? And that's simply because the number of wells starting to be drilled out in here suggests almost two possible depositional systems.

EXAMINER JONES: Okay, that's all I had. Thank you very much.

EXAMINER BROOKS: Anything further?

Next witness.

MR. CARR: At this time we call Tony Beilman.

TONY BEILMAN,

the witness herein, after having been first duly sworn upon his oath, was examined and testified as follows:

DIRECT EXAMINATION

BY MR. CARR:

Q. Would you state your name for the record, please?

A. Yes, my name is Tony Beilman. My last name is spelled B-, as in boy, e-i-l-m-a-n.

Q. Where do you reside?

A. I reside in Dallas, Texas.

Q. By whom are you employed and in what capacity?

A. I'm retained by David Arrington Oil and Gas, Inc., as a petroleum engineer and operations supervisor.

Q. Have you previously testified before the New Mexico Oil Conservation Division?

A. I have not.

Q. Would you summarize for the Examiners your educational background and review your work experience?

A. Yes, I received a bachelor of science degree from New Mexico Tech in Socorro in 1982. I was employed by Phillips Petroleum Company as a reservoir engineer for 12 years, and then at that time I was given the opportunity to start a consulting firm called Trinity Engineering, and that's currently where I am now.

Q. Are you familiar with the Applications filed by

Ocean and Arrington in these consolidated cases?

A. Yes, I am.

Q. Have you made an engineering study of the area which is the subject of these consolidated Applications?

A. Yes, I have.

Q. And are you prepared to share the results of your work --

A. Yes, I am.

Q. -- with the Oil Conservation Division?

MR. CARR: Are the witness's qualifications acceptable?

EXAMINER BROOKS: Yes, they are -- Any objection, Mr. Bruce?

MR. BRUCE: No, sir.

EXAMINER BROOKS: They are acceptable.

Q. (By Mr. Carr) Mr. Beilman, would you identify and review Arrington Exhibit 9?

A. Yes, this is very similar to the exhibit that Mr. Payne presented, and basically we assumed and got the same data, and it's a bottomhole-pressure-versus-time. And what I tried to show on this plot was the bottomhole pressure of all of the wells to the west of our proposed location, dipping down into Section 18 and 17, and then also compare those bottomhole pressure versus time to the wells in Section 5 and 4.

Q. And what does this show us?

A. It shows that -- as everybody has pretty much stated, that the wells to the -- in Section 7, 18 and 17 experience a lot less bottomhole pressure than the wells in Section 4 and 5.

As you'll note, it's kind of interesting, because it looks like the wells in Section 7, 18 and 17 are basically producing from one large tank, and bottomhole pressure seems to be somewhere around 500 pounds.

Q. If we look at the isopach, which is marked Arrington Exhibit 7 --

A. Okay.

Q. There are a number of wells in Sections 16, 17, 18 and 7 that have produced for some period of time.

A. That's correct.

Q. For about -- How long has this particular Atoka-Morrow reservoir been produced?

A. Well, the earliest production -- bottomhole pressure numbers and production numbers run in the late, oh, 1972, 1973 vintage, all the way into new wells being drilled, and -- we've got some new wells drilled in the 1980s. But it's been basically been producing 30 years.

Q. If there were not some sort of permeability restriction or barrier somewhere in the center of the spacing unit, in the east half of Section 8, would you

still expect to see bottomhole pressures in the wells that have recently been drilled in 5 and 4 in the 2000- to 3000-pound range?

A. I would expect to see a substantial -- less pressure than what we're seeing now. This perm barrier that Bill refers to, I really refer to it as a perm restriction. I don't know that it -- It just could be a lower perm number than what we might be seeing in the heart of the channel. It could be --

Q. At what rate is it your understanding that the Ocean Texaco State 5 Well Number 1 in the south half of 5 -- at what rate is that well producing?

A. As of December, it looked like it was doing about 460 MCF a day.

Q. Do you have an opinion as to whether or not that well will be draining reserves from the northeast of Section 8?

A. Yes, I do, I believe that the reserves in the northeast of Section 8 are being drained by that well.

Q. In your opinion, if a well is not drilled in the northeast of Section 8, will those reserves be drained by wells offsetting it to the north?

A. Yes.

Q. Let's go to what has -- I think at this time, Mr. Beilman, I'd ask you to take out our AFE which has been

marked as Arrington Exhibit 3, and the Ocean AFE which has been marked as their Exhibit Number 4.

A. Okay.

Q. And I'd like you to look at these two and first of all tell me what the differences are between the AFE figures for completed wells at the proposed locations.

A. Okay, the difference -- the completed well cost for the well that Ocean proposed is basically $1.7 million to drill that well. Our proposed well and our AFE reflecting our proposed well is $1.4 million. So basically $300,000 difference between the two wells.

Q. And have you been able to ascertain what the differences are?

A. Yes, I have. If you look at certain categories, primarily the rental category, in our AFE we show $19,000 of rental equipment. If you look at Ocean's AFE they're showing $157,000. So there's a big difference there.

There's a difference in the location cost. They show $74,000 for a location, we show $32,000. And I think our numbers are even a little bit high.

We just built a location for Steve's Hopper about five miles north of this that was -- $15,000 was our cost, so... And there's some minor differences in some of the others.

And there's one other big difference, and that's

on the tangible equipment, the production equipment. We show $30,000 and they show $60,000, I believe.

Q. Are the costs in the Arrington AFE based on your actual experience for similar wells?

A. Yes, we just completed or drilled a well about four miles north of this called the Double Hacklepea, and those numbers reflect the numbers that we're using in here. We also, just -- about halfway down on a well called the Steve's Hopper just outside of Lovington, and again this AFE was commensurate with the bids that we received on the Steve's Hopper, which we just got the 1st of February, so...

Q. Do you consider the costs on the Ocean AFE to be reasonable for wells in this area?

A. I think it's a little bit high.

Q. If you were to participate in the Ocean well, as opposed to the Arrington well, with a 50-percent interest like Mr. Arrington, in fact, it would cost you $150,000 more to pay your AFE share, just to avoid being pooled; isn't that right?

A. That's correct.

Q. Was Exhibit 9 prepared by you?

A. Exhibit 9 was prepared by me, yes.

MR. CARR: At this time we move the admission of Arrington Exhibit 9.

MR. BRUCE: No objection.

EXAMINER BROOKS: Nine is admitted.

MR. CARR: That concludes my direct.

EXAMINER BROOKS: Mr. Bruce?

CROSS-EXAMINATION

BY MR. BRUCE:

Q. Just a couple of questions. Do you have Arrington Exhibit 7 in front of you, Mr. Beilman?

A. Yes, I do.

Q. Have you done a volumetric calculation on the reserves in that small reservoir in the northeast of 8 and stretching into 5 in Section 4?

A. We started to, but the problem was we didn't know what the boundaries were and what size acreage to put into the volumetrics to determine what the volumetric size of that reservoir would be.

Q. So what kind of reserves do you need to justify drilling a well?

A. A BCF would probably do. I think it would be more of a function of what the deliverabilities of those wells would be, and drilling a well in the heart of the channel, much like the Chevron well, would increase the deliverability, and so obviously the payout would be a lot quicker.

Q. But you can't tell me if there's a BCF of

reserves in the northeast quarter?

A. No, I can't tell you that. That's why we're willing to risk drilling the well.

Q. Just eyeballing this map, would it show a BCF of reserves in the northeast quarter?

A. You need -- If you're going to do the volumetrics, you need about 400 to 500 acres of a reservoir to equate giving a BCF to Ocean's well, giving a BCF to us, and giving 2 BCF to Chevron's well or Texaco's well.

Q. Does this look like it has 500 acres in this reservoir?

A. Well, I'm not going to -- I didn't planimeter it, so I don't know.

Q. Okay. As to the pressure data, you agree with Mr. Payne that the virgin pressures were about 5000, do you not?

A. I don't know about the virgin pressures. I can tell you what the pressures were on the Chevron well and the pressures that were reported by Ocean.

Q. Well, what does Exhibit 9 show?

A. Exhibit 9 shows the pressures that were reported to the State off of the Chevron well and off of the Ocean well.

Q. Okay, but what does it show for the New Mexico DK State Com well?

A. Well, you're right, I'm not going to dispute whether it was 4000 or 5000 pounds. I'm not going to argue --

Q. Okay.

A. -- it could very well be that.

Q. Now you mentioned the well cost. What well did you mention that Arrington drilled for $1.4 million?

A. The Double Hacklepea.

MR. BAKER: Peacock.

THE WITNESS: I mean Double Peacock. And we have the Steve's Hopper Number 1 being drilled now.

Q. (By Mr. Bruce) Were the Double Hackle Peacock costs that you must mentioned taken off the drilling report?

A. Taken off of actual accounting.

Q. Okay. Were you in charge of drilling Arrington's Mustang Midge 28-1 well?

A. I was not.

Q. Do you know what the final well costs were on that well?

A. I do not.

Q. Do you know what the AFE was for that well?

A. I do not.

MR. BRUCE: That's all I have, Mr. Examiner.

EXAMINER BROOKS: Mr. Jones?

EXAMINATION

BY EXAMINER JONES:

Q. Let me get your last name one more time.

A. It's Beilman, and it's spelled B-, as in boy, e-i-l-m-a-n.

Q. Okay, you probably knew some of our other Examiners here at New Mexico Tech.

A. Yeah, actually Mr. Stogner was one of my --

Q. You have my condolences.

(Laughter)

Q. I hope you've had lots of therapy.

Considering -- I think that was a good question about the volume in that -- mapped, as Mr. Baker has mapped that reservoir, coming up into Section 4 and seeing if three wells, especially considering two of them have already produced for a while, can actually -- I understand, though, that Mr. Baker's map can be expanded or contracted, so -- But you really do think you could drill a well there and pay it out and still make money?

A. We feel like we can, yes.

Q. Okay, and -- but you also -- it looks like you could also drill a well in the south part of that 320 acres and get into the big tank that way?

A. Absolutely.

Q. And these pressure charts that you have,

bottomhole pressures, that State 5 square yellow dot, what well is that?

A. That's the Ocean well.

Q. Okay, that's the Ocean well. And that's --

A. No, I'm sorry, that's the TMBR/Sharp well.

Q. TMBR/Sharp. Where is that?

A. It's way up there on the north part of Section 5.

Q. Okay. It looks like somebody ought to be drilling around that one, huh?

Okay, so basically from your pressure chart it looks like that they did get into some higher pressures?

A. That's what we feel.

Q. So that's a part of your -- one of your big arguments here?

A. That's what our concern and argument is, you know, typically we want to crowd up to where there's some pressure to work with.

EXAMINER JONES: Okay, Mr. Brooks?

EXAMINER BROOKS: I don't really think I have anything to add to your questions, Mr. Jones.

Anybody have some follow-up?

MR. CARR: I do not.

EXAMINER BROOKS: Very good.

MR. CARR: That concludes our presentation in this case, although I believe Mr. Bruce wants to close.

EXAMINER BROOKS: Well, given the hour, you know --

MR. BRUCE: I do have a closing, although I go after Mr. Carr's. But I would like to recall, if he could sit right here, Mr. Payne to the stand to ask something.

EXAMINER BROOKS: Yeah, the witness may stand down, Mr. Beilman may stand down.

RAYMOND W. PAYNE (Recalled),

the witness herein, having been previously duly sworn upon his oath, was examined and testified as follows:

DIRECT EXAMINATION

BY MR. BRUCE:

Q. Mr. Payne, you heard Mr. Beilman testify about the AFE, did you not?

A. Yes, sir.

Q. Are you familiar with the Arrington-operated Mustang Midge 28-1 well?

A. The 28-1 well was drilled in this general area, in the same type of target to a partially depleted sand, the same depth, same casing program, very similar well.

Q. What was the AFE for that well?

A. The AFE was for $1.4 million.

Q. And what was the actual cost of that well?

A. Well, the drilling report showed $1.4 million, but the actual costs were $1.7 million, which compares

almost exactly to what our AFE is written for.

MR. BRUCE: Thank you.

MR. CARR: I have just one question, if I could.

EXAMINER BROOKS: Go ahead.

CROSS-EXAMINATION

BY MR. CARR:

Q. I just can't figure out what you plan to rent for $157,000.

MR. BRUCE: Me.

(Laughter)

MR. CARR: Then it's a very bad deal.

MR. BAKER: That's the blow-out equipment.

Q. (By Mr. Carr) Do you know what's included in that category?

A. Could I see the exhibit, please? I don't know if I'll be able to answer your question, but I'll give it a shot.

Q. There's $57,000 listed in rental equipment. Do you know what that figure could cover?

A. Yeah, half of that looks like it's for drilling and half of it's completions. And typically rental equipment includes things -- You know, sometimes the rig doesn't have BOPs on it. I don't know if we've got a drill stem test that we might have in here for some rental equipment. I'm going to defer that. I really don't know.

MR. CARR: That's all I have.

THE WITNESS: But yeah, the overall gross cost, I think, is comparable to what the operators are drilling in the area.

EXAMINER BROOKS: Okay, there's some kind of convention between counsel about closing statements. I guess, Mr. Carr, you --

MR. CARR: May it please the Examiner, Mr. Bruce always cites it as the Carr rule when he wants to go last, and I always hear that as, I have something to say that I don't want to let you refute.

EXAMINER BROOKS: Well, of course, you know, I spent 12 years on the bench, and we always let one party open and close, but being here is a little different. But you guys are here so often I want you to get along, so we'll follow the Carr rule.

MR. CARR: Being put at that disadvantage, knowing that he has something to say that he doesn't want me to respond to, I'm prepared to go forward.

EXAMINER BROOKS: Go ahead.

MR. CARR: May it please the Examiner, as a member of the New Mexico Bar this year, we have a film on professionalism that we're asked to review. And after listening to it for two hours the only thing I can remember is that a federal judge announces that the highest calling

of a lawyer is to make clear that which is clear.

I didn't know what that meant until I got here today, but it seems to me certain things are clear.

You can play with the geology all you want. Both geologists basically see a northeast-southwest sort of trend across the east half of Section 8. And both see that there are reserves under the northeast quarter. Both agree without additional drilling these reserves are going to be drained.

I think it's clear that these reserves are going to be produced either by a new well, which Mr. Arrington proposes to drill, or it's clear that they're going to be produced by the two wells to the north of there, one owned by Texaco, one 100-percent owned by Ocean and its partners. I think it's clear they would rather have 100 percent of those reserves than the 50 percent they would get out of the well in the northeast quarter.

It's also clear that unless the well drilled by Arrington is drilled as proposed by Arrington, he's going to be denied the opportunity to receive his share of the reserves under this tract, no matter how many there are. He's willing to spend $1.4 million to get his share. He doesn't own an interest in the wells to the north. And yet without the well he proposes, they get it all.

And I also think its clear under the Oil and Gas

Act that it is your duty to afford him that opportunity. And if you deny him that, you are outside your statutory mandate. I think it's clear why they want to drill a well on this acreage as far away as they can get it from the better wells to the north. By authorizing that with an order designating Ocean operator, I submit, you impair the correlative rights of Mr. Arrington, the largest owner in the spacing unit. That's what I think is clear in this case.

On the facts of this case, Arrington is the largest owner. Arrington acquired the property within a week, was prepared to go forward with drilling a well. He has lower AFE costs. Those are the costs, no matter what happened on another well, that Ocean will pay their share of to participate. And he has a location that, if it isn't drilled, is going to be drained by wells owned by others. More than that, he's willing to drill both wells. That's what they've testified to here today.

On these facts, to meet your statutory duty to protect correlative rights, you must grant the Application of Arrington and deny the Application of Ocean.

EXAMINER BROOKS: Mr. Bruce?

MR. BRUCE: Mr. Examiner, let's get out of the way a couple of things that I disagree with. I don't think it's as clear as Mr. Carr says, although on one point we

agree. First of all, operatorship. That's going to be determined by the well location we choose. We don't need to argue over that.

Secondly, regarding the AFE, an AFE is simply that, an estimate. Based on the testimony of Mr. Payne, the last well that Arrington was in with Ocean cost about $1.7 million. Both are fair reasonable. If it is too expensive there's always a chance later under a pooling order to challenge the well costs. That's of no importance.

Let's make another thing clear, is that Ocean isn't out here to drain reserves off of Arrington's acreage. At one point Ocean had a hundred percent of the east half, and it was willing to drill a well.

What happened? The operator of the well in the west half of Section 8 ceased producing that well and the lease terminated. That was long before Arrington had an interest in this section. It could -- It was willing to go forward last summer and drill the well. And you may not remember this, Mr. Examiner, but we actually came up here for a pooling case against Exxon because we had trouble getting the term assignment out of them.

We force-pooled this acreage once, and we were willing to drill. And then we were told by Exxon, after Ocean had spent tens of thousands of dollars for a term

assignment, that hey, they lease is no good.

Also, they do not have an interest. Ocean and Nadel and Gussman and McCombs do not have an interest in the Section 4 well, the Chevron Shoe Bar well. They are being affected by that well too, but they were willing to go drill the southwest quarter of the southeast quarter nine or ten months ago, and they believe that was the correct decision then, and it's the correct decision now.

Now, there are certain things you should take into account. Under Commission Order R-10,731-B, which sets forth some of the factors, I think you have to look at certain factors. One of them is interest ownership in the well. In this case, although Ocean's interest is split up, it's 50-50. Nobody has a priority there.

EXAMINER BROOKS: Now, there wasn't -- I don't recall anything in the evidence about the McComb interest. Are they a -- have they signed over --

MR. BRUCE: Yes, Mr. Maney testified that McCombs owns a portion of the interest that we call Ocean.

EXAMINER BROOKS: Okay, go ahead.

MR. BRUCE: And they are subject to a JOA.

Another factor to look at is time spent in getting this prospect going. While frankly all these wells that you're looking at here today were set up by the Ocean Texaco "5" Number 1 well in the southeast southeast of

Section 5, they drilled that well, that set up the interest for Chevron to drill its well, and it also set up the interest for Ocean to continue drilling in Section 8. They obviously have been out here for quite some time now, under Mr. Maney's testimony, at this point two years, trying to get a well drilled. That factor is in their favor.

As a matter of fact, a review of the Division records, which I asked the Examiner to incorporate, will show that Ocean has an APD for this well. I think it might have lapsed at one point, or it expired under the one year and they renewed it. So they have had an APD out here to drill this well for quite some time. That's another factor in their favor.

But when you come right down to it, you do have to look at the geology and engineering.

EXAMINER BROOKS: As I recall, that's what the Commission Order says is the most important thing.

MR. BRUCE: It is the most important. And I think what you have to look at -- And we understand why Arrington is interested in drilling the well. But if you look at their exhibits, there's just not enough reservoir -- there's too much risk to drill in the northeast quarter. The southeast quarter has thicker sand, a better pressure regiment. It's the best location, and if you compare that with the new Mewbourne well drilled, I think, in Section

18, it confirms Mr. Payne's engineering study. Simply put, I think you have to drill the best location first. That location is in the southeast quarter of Section 8.

Once that well is drilled, if Arrington wants to propose a second well he can certainly do so, but let's drill the best location first. Please approve Ocean's Application.

EXAMINER BROOKS: Well, would this be a case, gentlemen, when the order providing for additional wells form might be put into use?

MR. BRUCE: I believe it could be.

EXAMINER BROOKS: Since it's clear that everybody has some interest -- obviously Arrington much more than Ocean, but everybody has some interest in more than one location.

MR. BRUCE: Rather than coming back here and fighting over another one, I don't see why not.

EXAMINER BROOKS: It seems to make sense.

Okay, if there's nothing further, Case Number 13,036 and Case Number 13,039 will be taken under advisement.

(Thereupon, these proceedings were concluded at 5:55 p.m.)

* * *

I do hereby certify that the foregoing is a complete record of the proceedings in the Examiner hearing of Case No. _____, heard by me on _____ 19 ____.

_____, Examiner
Oil Conservation Division

CERTIFICATE OF REPORTER

STATE OF NEW MEXICO)
) ss.
COUNTY OF SANTA FE)

I, Steven T. Brenner, Certified Court Reporter and Notary Public, HEREBY CERTIFY that the foregoing transcript of proceedings before the Oil Conservation Division was reported by me; that I transcribed my notes; and that the foregoing is a true and accurate record of the proceedings.

I FURTHER CERTIFY that I am not a relative or employee of any of the parties or attorneys involved in this matter and that I have no personal interest in the final disposition of this matter.

WITNESS MY HAND AND SEAL April 7th, 2003.

STEVEN T. BRENNER
CCR No. 7

My commission expires: October 16th, 2006