



United States Department of the Interior

Bureau of Land Management

New Mexico State Office

1474 Rodeo Road

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Santa Fe, New Mexico 87502-0115

www.blm.gov

IN REPLY REFER TO:

SDR 02-01

3160 (93000)

NMNM 99144

NMNM 99003

BEFORE THE
OIL CONSERVATION COMMISSION
Case No. 12734 **A-27**
Exhibit #
Submitted By: Richardson Oper. Co.
Hearing Date: October 28 & 30, 2002

CERTIFIED MAIL RETURN RECEIPT REQUESTED

7001 0360 0001 0168 1013

San Juan Coal Company

c/o Modrall, Sperling, Roehl, Harris & Sisk

500 Fourth St. NW

Bank of America Centre, Suite 1000

Albuquerque, NM 87102

Decision Dismissing Protest of

Issuance of Applications for Permits

To Drill in Vicinity of Coal Mine and

Approval of APD's

Decision Remanded; Request for Stay Dismissed as Moot Request for Stay of Approval of Further Applications Dismissed

By letter dated October 18, 2001, Modrall, Sperling, Roehl, Harris & Sisk, P.A., as agent for San Juan Coal Company (San Juan), requested a Stay Pending Administrative Review and State Director Review (SDR) of a September 20, 2001, Decision of the Farmington Field Office (FFO). That Decision dismissed San Juan's August 31, 2001, protest of the issuance of applications for a permit to drill (APD's) in areas where San Juan has plans to mine. The decision also approved four Richardson Operating Company (Richardson) APD's. San Juan also requested the opportunity to present its arguments orally. The oral presentation occurred on November 19, 2001.

On October 29, 2001, we received a Reply to San Juan's request for administrative review from Richardson and on November 7, 2001, this office received a Reply from Dugan Production Corporation (Dugan). Dugan is an affected party through its existing oil and gas leases, and its current and proposed coalbed methane (CBM) development program. During the oral presentation on November 19, 2001, San Juan expanded upon its written arguments. Following San Juan's presentation, Richardson presented its oral arguments.

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Facts:

San Juan requested that Richardson's drilling operations be curtailed in the following lands:

T. 30 N., R. 14 W., N.M.P.M., San Juan County, New Mexico

Secs. 17-19, 30, 31; and

T. 30 N., R. 15 W., N.M.P.M.

Sec. 24.

These lands are located within San Juan's "Deep Lease" and "Deep Lease Extension," NMNM 28093 and NMNM 99144, respectively.

Leasing of the Federal oil and gas estate has occurred in this area since the first 'oil permit' was issued in 1923. There are seven active oil and gas leases in effect within the above-described area. Six of the leases were issued 27-33 years ago, and are held by production from other wells. Richardson operates lease NMNM 99003, obtained at a competitive lease sale in 1997. One well within the lease has produced since October 1999. Dugan operates two leases within the area.

Coal has been mined for residential use since the late nineteenth century. Large-scale surface mining began in 1958. Western Coal Company initiated surface mining of coal in 1973. The "Deep Lease," later acquired by San Juan, was issued to Western Coal Company in April 1980. San Juan's "Deep Lease Extension" was issued effective March 1, 2000, with a term of 20 years.

Section 15 of the lease has the following special stipulations:

- "1. The lessee will comply at its own expense with all reasonable orders of the Secretary respecting diligent operations, prevention of waste, and protection of non-coal resources.
2. This coal lease is subject to all prior existing rights, including the right of oil and gas lessees and other mineral lessees and surface users.
3. It is solely the responsibility of the coal lessee, not the responsibility of the Bureau of Land Management (BLM), to clear the coal tract of any legal encumbrances or pre-existing land uses that would impede or prevent coal mining on the tract."

We have minutes of four of the monthly meetings facilitated by the FFO, held between January and May 2001, in which San Juan, Richardson and Dugan met in an effort to optimize recovery of both coal and CBM, as well as potential gas reserves in deeper horizons. San Juan originally encouraged degassing prior to mining. In fact, it was this position that prompted the FFO to send demand letters to both Richardson and Dugan, requiring development of the CBM prior to mining as a means of recovering gas that otherwise would be lost. San Juan now opposes development of the CBM, due to safety concerns expressed by its ventilation engineer.

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Richardson submitted four APD's that triggered the August 31, 2001, protest from San Juan. After the September 20, 2001, decisions, Richardson drilled all four wells.

San Juan's Arguments:

Our review of the oral presentation, written material submitted by San Juan and Richardson, and case record data, demonstrated that this dispute has been ongoing for over a year. There are four main issues in the dispute, as articulated by San Juan.

1. Who has the priority right to develop his lease(s)?

San Juan admits that its lease postdates the oil and gas leases. However, it states that its plan of development predates any drilling plans filed by either company, and that BLM should look at actual plans of development, not merely lease issuance dates. In addition, San Juan states that the BLM is bound to consider the more valuable resource from the standpoint of public needs; coal is more valuable and returns more in royalties to the public.

In its oral presentation, San Juan stated that the Resource Management Plan Amendment for Coal Leasing effectively modified the lessees' potential to develop their existing oil and gas leases.

2. Development of the CBM will result in safety hazards to mining equipment and personnel

San Juan made several statements regarding increased safety hazards if CBM development occurs prior to mining. The hazards result from the actual steel well casing itself, fire might be caused through mining equipment striking the casing and creating a spark that ignites coal fines or methane. There is an additional risk for spontaneous combustion of the coal if CBM completion techniques include hydraulic fracturing of the coal. San Juan states that hydraulic fracturing of the carbonaceous shale overlying the coal could result in further risk to equipment and employees if it weakens the roof of the mine. If the coal is de-watered and de-gassed ahead of mining, the coal will be more susceptible to oxygen adsorption through an opened cleat system, thereby increasing the risk for spontaneous combustion.

3. Development of the CBM will result in a major economic loss to San Juan

San Juan states that development of the CBM would result in reduced recovery of coal. San Juan states that underground mine safety regulations require that no mining occur within 300 feet from any existing wells. This would reduce coal recovery by 300,000 tons around each well. It would also require San Juan to reposition its equipment around each well, which is both time consuming and expensive. If there is more than one well within a particular mining block, it might make that block uneconomical to develop, resulting in the loss of three million tons of coal.

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might make that block uneconomical to develop, resulting in the loss of three million tons of coal.

4. The BLM planning and environmental documents are flawed and do not comply with FLPMA

San Juan states that the 1998 Farmington Resource Management Plan Amendment (RMPA) for coal leasing activity is flawed, in that it did not consider the coal versus CBM conflict, nor provide a method to resolve the conflict. The Environmental Assessments (EA's) prepared for Richardson's APD's do not consider alternatives to drilling that were developed in the RMPA.

Richardson's and Dugan's Arguments

Richardson states that its rights are senior to San Juan's, and that the "first in time, first in right" concept is not outmoded. Richardson cites the stipulations attached to the "Deep Lease Extension" lease, and states that they are controlling; these lease terms were attached in an attempt to eliminate arguments over priority in coal versus CBM resource development. Richardson notes that, in spite of those stipulations, San Juan has failed to conduct due diligence by taking steps necessary to minimize legal and technological risks to the mine, and instead has passed the burden to BLM and Richardson.

Richardson states that its oil and gas lease predates the RMPA, and thus, it cannot alter valid existing rights. Richardson adds that it actively participated in commenting on the RMPA to be sure BLM was aware of the potential adverse effects to its plans to develop the coalbed methane.

Richardson and Dugan disagree with San Juan's conclusion that the EA's failed to consider all reasonable alternatives, including alternative well locations, and a no-action alternative.

Dugan identifies its lease interests, and notes that they predate San Juan's lease. Dugan noted that it currently operates 18 wells within the subject area; the wells produce 850 MMBTU/day. Dugan describes the infrastructure needed to produce the gas, and its investment of more than \$6 million.

Dugan also notes that the development potential of CBM has only surfaced recently, and that advances in technology have made recovery of CBM economical in this under pressured area. Dugan notes those existing regulations would allow it to drill an additional 24 wells within the subject area, and that if well density is increased, 38 additional CBM wells could be drilled.

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Analysis and Response

Following is our response to each argument:

1. Priority

We find no justification for San Juan's argument that we should consider the date that plans of development were approved, in lieu of actual lease issuance dates. The terms of San Juan's coal lease provide our rationale, that the oil and gas lessees have priority in development of their gas resources.

San Juan's coal lease contained special stipulations as a means of resolving future development conflicts. Section 15 of the lease states that it is San Juan's sole responsibility to resolve conflicts with prior oil and gas lessees. The terms clearly state that the oil and gas leases are valid existing rights, and that San Juan is solely responsible for removing impediments to coal mining.

In addition, the Protocol for the Mediation of Adverse Impacts on Oil and Gas Revenues, signed by San Juan, recognizes the senior stature of valid existing oil and gas leases. By signing the lease form and the protocol, San Juan agreed to those provisions. The protocol committed San Juan to honor existing Federal and fee oil and gas leases, and to avoid or mitigate adverse impacts to the oil and gas lessees. San Juan agreed to compensate the oil and gas lessees by paying damages for decreased production. If production would permanently cease, San Juan would compensate the lessees for the fair market value of lost production.

Finally, San Juan's asserted that the RMPA for Coal Leasing effectively modified the oil and gas lessees' potential to develop their existing oil and gas leases. This is untrue - the BLM cannot retroactively constrain development by applying new, restrictive stipulations to existing leases. We do agree with San Juan that the Plan requires that future drilling activity would be coordinated with the BLM and mining company.

2. Safety

We agree with the September 20, 2001, FFO decision letter that the risks of degassing the coal seam are difficult to quantify. San Juan presented only its concerns about potential safety hazards. San Juan presented no data that demonstrate that hydraulic fracturing of the coal would increase the potential for spontaneous combustion, or weaken the mine roof. San Juan's arguments regarding potential safety hazards if CBM development preceded mining may be addressed by underground mine safety rules requiring the 300 foot buffer around existing wells.

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3. Economics

We agree that Richardson's CBM development plans could impair coal mining, and could force San Juan to bypass recoverable coal reserves. Nonetheless, San Juan could mine through a well location if it milled out the casing prior to mining. While San Juan states that this is a slow and expensive procedure, it would maximize the economic recovery of the coal resource. San Juan implies that Richardson and Dugan are filing APD's to jeopardize its mining operations, then holding out on a settlement to obtain "... many multiples of such value ...". The BLM has seen no evidence of the two companies filing APD's merely to impede underground mining, or force an unfair buyout. Rather, Richardson and Dugan appear to be proposing drilling operations, and carrying out development in an attempt to recover CBM prior to mining. Evidently, the two companies are unconvinced, as is the BLM, that there would be recoverable CBM following mining, such that they might obtain some economic benefit of their leases post mining.

4. The 1998 FFO Resource Management Plan Amendment and individual EA's for Richardson's CBM wells are flawed.

We believe the RMPA adequately addresses the oil and gas development versus coal mining issue. It offers a sufficient range of alternatives for the BLM to consider.

The State Office examined the Environmental Assessment (EA) prepared by Permits West, Inc. (Richardson's contractor), dated August 16, 2001. We also reviewed the Finding of No Significant Impact (FONSI) and Decision Record, completed by the FFO on August 29, 2001, and approved September 4, 2001.

We find that the EA did not comprehensively address all issues regarding other mineral resources and potential conflicts. Similarly, the FONSI should have recognized the lack of such analysis. Specifically, there was no analysis of potential impacts to the coal resource. We note that the EA were prepared prior to San Juan's protest letter. At that time, degassing of the coal was considered as a positive effect.

Decision

This decision has been coordinated with our Field Solicitor in Santa Fe, and Department of the Interior solicitors in Washington, D.C.

We understand San Juan's concerns regarding mine safety and the economic costs of remediating well bores within its mine area. It is unfortunate that San Juan only recently recognized the potential adverse impacts of CBM development on its ability to mine the coal. The BLM had encouraged our lessees to accelerate development of the CBM in advance of mining to ensure recovery of methane that otherwise would be lost, and to reduce the safety threat of methane degassing during mining operations.

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We believe that Richardson has a prior existing right to develop the CBM. This is true even if it would cause reduced recovery of coal reserves, and adversely affect the economics of San Juan's mine. San Juan must adjust its mine plan to provide necessary safety to mine personnel. Accordingly, we sustain the FFO decision with regard to: 1) priority; 2) safety; and 3) economics.

We disagree with San Juan's fourth argument that the APD approvals do not comply with the 1998 Coal Leasing RMPA. The Decision Record for the RMPA was issued after the effective date of Richardson's oil and gas lease. The RMPA cannot unreasonably constrain development of pre-existing rights.

We agree with San Juan that the EA's do not address alternatives to oil and gas development identified in the 1998 RMPA. We herein remand the case to FFO for review of the EAs prepared for the Richardson wells.

The FFO must ensure that cumulative impacts to the coal resource are analyzed, and consider alternatives that would reduce adverse impact to coal development. After the FFO have completed its analysis, and reported its conclusions to the State Director, we will decide this last issue.

The request for the State Director to stay FFO approval of the Richardson APD's is rendered moot by the completion of all four wells prior to our receipt of the SDR request. The request to stay approval of other applications within the area identified is dismissed as premature. We cannot stay applications prior to their approval.

This Decision may be appealed to the Interior Board of Land Appeals, Office of the Secretary, in accordance with the regulations contained in 43 CFR, Part 4 and Form 1842-1 (copy attached). If an appeal is taken, your notice of appeal must be filed in this office within 30 days from your receipt of this decision. The appellant has the burden of showing that the Decision appealed from is in error.

If you wish to file a petition for stay of the effectiveness of this Decision during the time that your appeal is being reviewed by the Board, the petition for stay must accompany your notice of appeal. A petition for a stay is required to show sufficient justification based on the standards listed on the attached (Form 1842-1). Copies of the notice to appeal and petition for stay must be submitted to each party named in the Decision and to the Interior Board of Land Appeals, and to the appropriate office of the solicitor.

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(see 43 CFR 4.413) at the same time the original documents are filed with this office. If you request a stay, you have the burden of proof to demonstrate that the stay should be granted.

Sincerely,



Carsten F. Gott
Deputy State Director
Division of Resource Planning,
Use and Protection

/Enclosure

cc:

WO(310)
MSO(920)
WSO(920)
USO(920)
NM(010)
NM(020)
NM(030)
NM(040)
NM(050)
NM(060)
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NM(930)

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