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June 28, 2011

Ms. Florene Davidson, Secretary  
New Mexico Oil Conservation Commission  
1220 S. St. Francis Drive  
Santa Fe, NM 87505

**Hand Delivered**

Re: NMOCC Case No. 14472 (De Novo): Application of COG Operating LLC for Cancellation of Operator's Authority and Termination of Spacing Units, Yeso Energy, Inc. Dow "B" 28 Federal Well No. 1, Eddy County, New Mexico

NMOCC Case No. 14547; Application of the NMOCD, Through the Compliance and Enforcement Manager, for An Order Authorizing the Division to Recognize an Operator of Record for Wells Currently Operated by Yeso Energy, Inc.; Lea, Eddy and Chaves Counties, New Mexico

Dear Ms. Davidson:

Attached for filing during the June 29, 2011 hearing in the above consolidated matters and for distribution to the Commissioners are an original and four copies of COG Operating LLC's Proposed Findings and Conclusions.

Very truly yours,

J. Scott Hall

JSH:kw  
Attachments

cc: Sonny Swazo, Esq., Attorney for NMOCD  
Cheryl Bada, Esq., Attorney for NMOCC  
Michael Feldewert, Esq., Attorney for Judah Oil, LLC  
Phil Brewer, Esq., Attorney for Yeso Energy, Inc. via e-mail

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

**APPLICATION OF COG OPERATING, LLC  
FOR CANCELLATION OF OPERATOR'S  
AUTHORITY AND TERMINATION OF SPACING  
UNITS, YESO ENERGY, INC. DOW "B" 28  
FEDERAL WELL NO. 1, EDDY COUNTY, NEW  
MEXICO**

**CASE NO. 14472 (De Novo)**

**APPLICATION OF THE NMOCD, THROUGH  
THE COMPLIANCE AND ENFORCEMENT  
MANAGER, FOR AN ORDER AUTHORIZING  
THE DIVISION TO RECOGNIZE AN OPERATOR  
OF RECORD FOR WELLS CURRENTLY  
OPERATED BY YESO ENERGY, INC.; LEA,  
EDDY AND CHAVES COUNTIES, NEW MEXICO**

**CASE NO. 14547**

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**COG OPERATING LLC'S  
PROPOSED FINDINGS AND CONCLUSIONS**

COG Operating LLC, ("COG"), submits the following proposed findings and conclusions in this matter:

**FINDINGS:**

(1) Yeso Energy, Inc. ("Yeso") has a long history of operator non-compliance with the Division's rules, regulations and orders. It has been party to a number of agreed compliance orders, violations of compliance orders and subsequent enforcement actions brought by the Division in examiner adjudicatory hearings.

(2) In 2007, the Division filed an enforcement action in Case No. 14008 asserting that Yeso had, among other matters, failed to file production reports and had operated wells and conducted injection operations following the suspension of its authority. On April 7, 2008, after hearing, the Division entered Order No. R-12930, which contained the following significant findings, conclusions and directives to Yeso Energy:

a. Yeso knowingly and willfully violated Division Rule 701 by injecting into Courtland Myers Wells No. 2 and 5 and the Knight Wells No. 9, 10 and 11, in each of the months of December 2006 and January through May, 2007. Rule 701 provides that 'the injection of water into any formation for the purpose of water disposal shall be permitted only by order of the division . . . .' The termination of Yeso's injection authority pursuant to Rule 1115.C effectively cancelled any order of the Division authorizing

injection of water into these wells, and, accordingly, injection subsequent to November 20, 2006 violated Rule 701.

Order No. R-12930, Findings ¶ 18 (April 7, 2008).

(3) Accordingly, in Order No. R-12930, the Division made the following determinations:

a. The authority of Yeso Energy, Inc. (OGRID 221710) to transport from or Inject into all wells that it operates in the State of New Mexico was properly terminated by the Division effective November 20, 2006, AND was not reinstated at any time on or prior to June 1, 2007.

b. A civil penalty in the amount of \$3,000 is assessed against Yeso Energy, Inc. on account of its knowing and willful failure to file production reports (Form C-115) for all wells operated by it for the month of May, 2006. This penalty is assessed by reason of Yeso's failure to file such reports at any time during the period from September 8, 2006 through and including November 29, 2006.

c. A civil penalty in the amount of \$30,000 is assessed against Yeso Energy, Inc. on account of its knowing and willful injection of water without a valid permit into the Courtland Myers well No. 2 (API No. 30-025-11195), Courtland Myers Well No. 5 (API No. 30-025-11119), Knight Well No. 9 (API No. 30-025-20352), Knight No. 10 (API No. 30-025-20351), and Knight No. 11 (API No. 30-025-20350), for the period from December 1, 2006 through May 31, 2007.

Order No. R-12930, Conclusions ¶¶ (1), (2) and (3) (April 7, 2008).

(4) Following a further failure by Yeso to abide by the requirements of Order No. R-12930, in 2009 the Division initiated an enforcement proceeding in Case No. 14294. On March 31, 2009, an examiner hearing was held on the Division's Application. Yeso failed to appear for the hearing. On June 17, 2009, the Division accordingly entered Order No. R-12930-A. That order contained the following significant findings, conclusions and directives:

a. The Division seeks an order finding Yeso Energy, Inc. [OGRID 221710] ("Yeso" or "Operator") in violation of Division Rules 7.24 (failure to timely file production reports) and 25.8 (inactive wells). The Division further seeks an order pursuant to NMSA 1978, Section 70-2-14(B) requiring Yeso to plug and abandon all its wells by a date certain, and if it does not do so, allowing the Division to plug the wells and forfeit applicable financial assurance.

b. Yeso was not represented by counsel and did not appear at the hearing or file any response. No other party entered an appearance in this case or otherwise opposed this application.

c. On November 20, 2006, due to Yeso's failure to comply with then Division Rule 1115.C (lack of reporting production, failure to file form C-115), the Division cancelled the authority of Yeso to transport from or inject into any of its wells.

d. On August 20, 2007, the Division heard a compliance case involving six wells operated by Yeso (including at least two of the wells that were the subject of ACOI-137) and issued Order No. R-12801 requiring those six wells to be returned to compliance with then Division Rules 201 (concerning inactive wells) and allowing the Division to plug those wells in the event of non-compliance.

e. In addition, the Division presented testimony and exhibits as follows:

1. As of February 17, 2009, Yeso Energy, Inc. was the operator of record of . . . 12 wells (the subject wells) . . .

2. Yeso has failed to file production reports (required by Rule 7.24) for wells with approved form C-104. The Division presented Exhibit 16 showing approved C-104's for selected Yeso operated wells.

Order No. R-12930-A, Findings ¶¶ (2), (4.b), (4.d), (6.a) and (6.b) (June 15, 2009).

(5) Accordingly, in Order No. R-12930-A, the Division made the following determinations:

a. Yeso Energy, Inc. (OGRID 221710) is hereby ordered to appear at the examiner hearing on August 20, 2009, or later date agreed upon by the Division, and ordered to present evidence of compliance with Division Rules 7.24, 8.9, and 25.8.

b. If Yeso fails to appear on August 20 as hereby ordered, and Division records then demonstrate that Yeso is in violation of one or more Division rules applicable to any well it then operates, the Division Director may then issue an order directing Yeso to plug all of the wells that it operates by a date certain, and further directing that if Yeso fails to comply with that order, the Division is authorized to plug and abandon the subject wells and forfeit all applicable financial assurance.

Order No. R-12930-A, Conclusions ¶¶ (1) and (3) (June 15, 2009).

(6) Yeso again failed to obey the directives of the previous compliance orders. Consequently, the Division initiated a "show cause" proceeding in Case No. 14294. A "show cause" hearing was convened before one of the Division's examiners on August 20, 2009, and again Yeso failed to attend. Accordingly, on September 15, 2009, the Division entered Order No. R-12930-B which provided, *inter alia*, as follows:

a. The Division seeks an order finding Yeso Energy, Inc. [OGRID 22170] (Yeso) in violation of Division Rule 25.8 (inactive wells), and requiring Yeso to plug and abandon all of its wells, or transfer its wells to another unaffiliated operator, by a date

certain, and, in the event Yeso fails to comply with that order, authorizing the Division to plug the wells, and forfeiting any applicable financial assurance.

b. Yeso wholly failed to appear at the hearing on August 20, 2009.

c. In addition to being out of compliance with Division Rule 25.8, Yeso is out of compliance with Division Rule 5.9 because 100% of the wells that it operates are inactive, and because it violated the specific directive of Order No. R-12930-A directing that it appear at the hearing on August 20, 2009.

Order No. R-12930-B, Findings ¶¶ (2), (4), (6) (September 15, 2009).

(7) Accordingly, in Order No. R-12930-B, the Division made the following determinations:

a. Yeso Energy, Inc. [OGRID 22170] shall properly plug and abandon each of the wells described in Finding Paragraph 6.a of Order No. R-12930-A, or transfer each of said wells to another operator, *not affiliated with Yeso and approved by the Division*, not later than March 15, 2010.

Order No. R-12930-B, Order ¶ 1 (September 15, 2009) (emphasis added).

(8) Yeso ignored the directives of the Division in Order No. R-12930-A to either plug and abandon its wells or transfer them to an unaffiliated operator by March 15, 2010. The Division accordingly placed the Yeso wells on its plugging list. The plugging of the Dow “B” 28 Federal Well No. 1 was imminent.

(9) By failing to comply with the Division’s rules, regulations and orders, and to either plug the wells or transfer them, Yeso effectively abandoned the wells and all regulatory permits and authorizations.

(10) COG has been very active in the vicinity of the Dow “B” 28 Federal Well No. 1, having drilled over 50 wells in the nearby Skelly Unit. COG has development plans, which have been submitted to the United States Bureau of Land Management (BLM), to drill another 50 wells in the unit. Correspondingly, COG has an immediate need for additional capacity for the disposal of produced water.

(11) In April of 2010, COG learned that the abandoned Dow “B” 28 well was about to be plugged within a matter of days. COG made inquiry of the Division as to what steps should be taken to assume operatorship of the well and convert it to injection operations. By correspondence dated April 5, 2010, COG requested the Division delay plugging of the abandoned well and the Division agreed.

(12) COG then filed its application in Case No. 14472, *Application of COG Operating, LLC for Cancellation of Operator’s Authority and Termination of spacing Units, Yeso Energy, Inc. Dow “B” 28 Federal Well No. 1, Eddy County, New Mexico*. A hearing on COG’s

Application was held on May 13, 2010 before one of the Division's examiners. Yeso was represented at the hearing by counsel, but produced no witnesses, testimony or evidence. Both COG and OCD appeared at the hearing and presented evidence.

(13) On July 13, 2010, the Division entered Order No. R-13294. The order found, *inter alia*, at paragraph 5, that OCD had presented the following testimony:

a. OCD found that Yeso had abandoned the subject well and ordered Yeso to either properly plug and abandon the well, or transfer operations to a nonaffiliated Division-approved operator on or before March 15, 2010 (Order No. R-12930-B, issued in Case No. 14294 on September 15, 2009).

Order No. R-13294, Findings ¶ 5(a) (July 13, 2010).

(14) Accordingly, in Order No. R-13294, the Division made the following determinations:

a. The Division hereby terminates the authority of Yeso Energy to act as operator of the Dow "B" 28 Federal Well No. 1 (API No. 30-015-28676) located in Section 28, Township 17 South, Range 31 East, (Unit P) NMPM, in Eddy County, New Mexico.

b. The Division shall not plug the subject well prior to July 30, 2011 unless COG advises that it is no longer pursuing its plan to obtain the right to use this well.

c. COG shall file an application with the Division to use the subject well for disposal operations without the necessity of a change of operator that would be ordinarily required.

Order No. R-13294, Order ¶¶ (1), (2) and (3) (July 13, 2010).

(15) On August 9, 2010, Yeso Energy, Inc. filed its Application for Hearing De Novo in Case No. 14472.

(16) On approximately August 31, 2010, COG filed with the Division its C-108 Application for Authorization to Inject in order to convert the Dow "B" 28 well to a disposal well. COG changed the name of the well to the "Skelly Federal 28 SWD No. 1". COG's C-108 Application also provides for operation of the well as a private "closed" facility.

(17) On September 2, 2010, COG signed and subsequently submitted to the BLM an Application for Transportation and Utility Systems and Facilities on Federal Lands in order to use the Dow "B" 28 well and adjacent surface as a disposal facility.

(18) Previously, on August 16, 2010, Yeso executed a C-145 Change of Operator form, purporting to change operations to Judah Oil, LLC ("Judah Oil"), "Effective on the date of approval by the OCD".

(19) On August 17, 2010, Judah Oil filed a C-108 Application for Authorization to Inject with the Division, seeking approval to use the Dow "B" 28 Well as a commercial salt water disposal well.

(20) Subsequently, on August 25, 2010, Yeso and Chica Energy, LLC ("Chica") entered into a Purchase and Sale Agreement with Judah Oil for the sale and transfer of the wells formerly operated by Yeso, including the Dow "B" 28 well. Subsequently, On September 10, 2010, Yeso executed a Conveyance of Oil and Gas Leases in favor of Levi Oil and Gas, LLC.

(21) The August 25, 2010 Purchase and Sale Agreement among Yeso and Chica as Sellers and Judah Oil as Buyer, provided for, *inter alia*, the transfer to Judah Oil of "All Sellers' right, title and interest in all permits and licenses . . . to the extent the same are used or obtained in connection with the Leases ("Permits)".

(22) The Purchase and Sale Agreement made specific provision for the transfer of the Dow "B" well, on the condition that ". . . in the event it is successfully permitted as a salt water disposal (SWD) well . . .".

(23) Under the Purchase and Sale Agreement, at the time a disposal permit is issued to Judah Oil for Dow "B" well, Yeso and Chica are to receive \$50,000.00. In addition, Yeso and Chica reserve the following interests in the well:

- a. a fee of \$.05 per barrel of water disposed into the SWD;
- b. a 10% overriding royalty interest on recovered and sold oil;
- c. the right to receive 20% of the proceeds in the event of a sale of the well; and
- d. the right to receive 20% of the proceeds in the event of a sale of the system.

(24) On September 30, 2010, Judah Oil submitted to the BLM its own Application for Transportation and Utility Systems and Facilities on Federal Lands in order to use the Dow "B" 28 well and adjacent surface as a commercial disposal facility.

(25) Both the COG and Judah Oil BLM applications remain pending before that agency.

(26) Yeso has purposefully intended to avoid its responsibilities as a well operator under its permits and under the Division's rules, regulations and orders.

(27) The August 25, 2010 Purchase and Sale Agreement and the related efforts of Yeso and Chica are intended to circumvent the Division's operator compliance and enforcement authority.

## CONCLUSIONS:

(1) The jurisdiction and the authority of the Division are broad in scope. Among other matters, Section 70-2-12(B) of the Oil and Gas Act provides:

Apart from any authority, express or implied, elsewhere given to or existing in the oil conservation division by virtue of the Oil and Gas Act or the statutes of the state, the division is authorized to make rules, regulations and orders for the purposes and with respect to the subject matter stated in this subsection:

to prevent crude petroleum oil, natural gas or water from escaping from strata in which it is found into other strata;

to require wells to be drilled, operated and produced in such manner as to prevent injury to neighboring leases or properties;

to regulate the disposition of water produced or used in connection with the drilling for or producing of oil or gas or both and to direct the surface or subsurface disposal of the water, including disposition by use in drilling for or production of oil or gas, . . . in a manner that will afford reasonable protection against contamination of fresh water supplies designated by the state engineer;

[and]

to regulate the disposition of nondomestic wastes resulting from the oil field service industry, the transportation of crude oil or natural gas, the treatment of natural gas or the refinement of crude oil to protect public health and the environment, including administering the Water Quality Act [74-6-1 NMSA 1978] as provided in Subsection E of Section 74-6-4 NMSA 1978.

N.M.S.A. 1978, § 70-2-12(B)(2), (7), (15) and (22) (2004).

(2) Section 70-2-11(A) of the Oil and Gas Act provides:

The division is hereby empowered, and it is its duty, to prevent waste prohibited by this act and to protect correlative rights, as in this act provided. To that end, the division is empowered to make and enforce rules, regulations and orders, **and to do whatever may be reasonably necessary to carry out the purposes of this act**, whether or not indicated or specified in any section hereof.<sup>1</sup>

N.M.S.A. 1978, § 70-2-11(A) (1935) (emphasis added).

(3) In past cases, the Division and Commission have cited to this specific provision of the Oil and Gas Act as authority supporting the Agency's broad construction of its powers to act as "cumulative and not exclusive." *See, e.g.,* Order No. R-11573-B, Case No. 12601,

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<sup>1</sup> *See also* N.M.S.A. 1978, § 70-2-6(A) (1935) ("[The Division] shall have jurisdiction, authority and control of and over all persons, matters or things necessary or proper to enforce effectively the provisions of this act . . .").



*Application of Bettis, Boyle and Stovall To Re-Open Compulsory Pooling Order No. R-11573* (February 15, 2002), Conclusion of Law.

(4) Specifically as to the plugging of abandoned wells, under Section 70-2-12(B)(18) of the Oil and Gas Act, the Division has broad authority to “do all acts necessary and proper to plug dry and abandoned oil and gas wells . . . including disposing of salvageable equipment and material removed from oil and gas wells being plugged by the state[.]” N.M.S.A. 1978, § 70-2-12(B)(18) (2004). The Division is also authorized by Section 70-2-38(B) of the Act to make expenditures from the reclamation fund for the plugging of wells “in accordance with the provisions of the Oil and Gas Act and the rules and regulations promulgated pursuant to that act.” N.M.S.A. 1978, § 70-2-38(B) (2010).

(5) In furtherance of its authority to, *inter alia*, regulate disposal wells, the plugging and abandonment of wells and to obtain operator compliance with the Oil and Gas Act, the Division has appropriately acted under *its* regulations to plug the Yeso wells (19.15.5.10.B.4 NMAC), terminate Yeso’s permits (19.15.5.10.B.5 NMAC), deny the changes of operator (10.15.14.10 NMAC), and terminate allowables for the non-compliant operator (19.15.16.19.B NMAC).

(6) The effort of Yeso to sell the Dow B “28” Federal Well No. 1 wellbore and any related permits to Judah Oil was intended to circumvent the Division’s authority. Further, the August 25, 2010 Purchase and Sale Agreement by Yeso was undertaken in derogation of the provisions of the Oil and Gas Act cited above and in avoidance of the Division’s rules, regulations and orders.


(7) The Commission is not bound by and is not otherwise obliged to recognize Yeso Energy’s August 25, 2010 Purchase and Sale Agreement. *See* Order No. R-11573-B, Case No. 12601, *Application of Bettis, Boyle and Stovall To Re-Open Compulsory Pooling Order No. R-11573* (February 15, 2002), Findings ¶ 24.

(8) Yeso Energy has abandoned the Dow B “28” Federal Well No. 1 and all regulatory permits and authorizations issued by the State. Further, all such regulatory permits and authorizations were properly revoked by the Division.

(9) The Division is directed to withhold approvals of any application of Judah Oil to utilize the Dow B “28” Federal Well No. 1 for injection.

(10) To the extent not in conflict with this Order, Division Order No. R-13294 is confirmed and shall be, and remain, in full force and effect. COG continues to be authorized to pursue an application to utilize the Dow B “28” Federal Well No. 1 for injection.

Respectfully submitted,  
Montgomery and Andrews, P.A.

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**Certificate of Service**

I hereby certify that on June 29, 2011, a true and correct copy of the foregoing was hand delivered to the following parties:

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