

STATE OF NEW MEXICO
ENERGY, MINERALS AND NATURAL RESOURCES DEPARTMENT
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 FED. WELL NO. 1, EDDY COUNTY, NEW MEXICO.

CASE NO. 14,472

De Novo

APPLICATION OF THE NEW MEXICO OIL CONSERVATION DIVISION,
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.

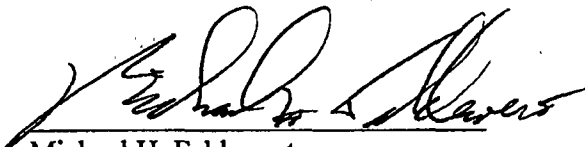
CASE NO. 14,547

PROPOSED ORDER OF JUDAH OIL, LLC

Pursuant to the Commission's instructions at the June 29, 2011, hearing in this matter,
Judah Oil, LLC, respectfully submits the attached proposed order for consideration by the
Commission.

Respectfully submitted,

HOLLAND & HART, LLP



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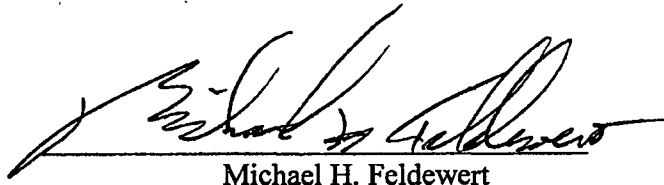
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CERTIFICATE OF SERVICE

I hereby certify that a copy of this Proposed Order of Judah Oil was served upon the following counsel of record this 13th day of July, 2011 via U.S. Mail postage pre-paid to:

J. Scott Hall
Montgomery & Andrews, PA
Post Office Box 2307
Santa Fe, New Mexico 87504

Sonny Swazo
New Mexico Oil Conservation Division
1220 South St. Francis Drive
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A handwritten signature in black ink, appearing to read "Michael H. Feldewert", is written over a horizontal line.

Michael H. Feldewert

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CASE NO. 14,547

PROPOSED ORDER OF JUDAH OIL, LLC

This cause came on for hearing on June 29, 2011 at Santa Fe, New Mexico, before the Oil Conservation Commission.

NOW, on this ____ day of ____, 2011, the Commission, a quorum being present, having considered the record and being fully advised in the premises,

FINDS THAT:

(1) On July 13, 2010, under Case No. 14,472, the Division entered Order R-13294. That Order addressed the Dow B Federal Well No. 1 (API #30-015-28676) and contained the following relevant conclusions:

- (6) Yeso has wholly failed to fulfill its obligations as operator under Division rules and orders, and its right to operate the subject well should be terminated.
- (7) COG has no interest in this property at this time except the possibility that their application to use this well as a disposal well will be granted.
- (8) Plugging the well should be suspended for six months to allow COG to pursue its application for an easement or other legal authority to take possession of the subject well."

Pursuant to these and other conclusions, the Division ordered as follows:

- (1) 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.
- (2) 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.
- (3) 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."

(2) Yeso Energy filed a request for de novo review of Order R-13294 in Case No. 14,472. However, by letter dated October 6, 2010, Yeso Energy withdrew from this case and did not appear at the de novo hearing in this matter.

(3) Since Yeso Energy, the party that applied for de novo review of Case No. 14,472, has now withdrawn from the case, the request for de novo review should be denied and Order R-13294, issued in Case No. 14,472, remains in effect.

(4) On August 11, 2010, one month after the entry of Order R-13294, Judah Oil submitted a fully executed Change of Operator Form C-145 to take over operation and financial responsibility for three wells formerly operated by Yeso Energy: the Dow B Federal No. 1, the Gulf McKay Federal No. 1, and the Dalton Federal No. 1. *See* Judah Ex. N; Tr. 45:11-46:13 (Sanchez testimony).

(5) On August 11, 2010, Judah Oil filed for approval with the BLM to become the operator of record for the Dow B Federal Well No. 1, the Dalton Federal No. 1 and the Gulf McKay Federal No. 1. *See* Judah Ex. F and I; Tr. 97 (Campanella testimony).

(6) On August 17, 2010, Judah Oil filed an administrative application with the Division seeking authority to convert the Dow B Federal Well No. 1 into a commercial disposal well.

(7) On or about August 31, 2010, COG filed a competing administrative application with the Division seeking authority to convert the Dow B Federal Well No. 1 into a private disposal well.

(8) In Case No. 14,547 the Oil Conservation Division ("Division") filed an application seeking guidance from the Commission on designating a new operator of record for the wells formerly operated by Yeso Energy, including the Dow B Federal Well No. 1, the Dalton Federal Well No. 1 and the Gulf McKay Federal Well No. 1.

(9) By Order No. R-13309, issued August 23, 2010, Mark Fesmire, Acting Director of the Oil Conservation Division, found that Case Nos. 14,472 and 14,547 arise from common facts, and that the resolution of the issues in one case will likely affect the resolution of the other case.

(10) Director Fesmire exercised his discretion pursuant to 19.15.4.20.B NMAC to direct the Oil Conservation Commission to hear Case No. 14,547, and directed that Case No. 14,547 be heard with Case No. 14,472.

(11) The Division has subsequently approved Judah Oil as the Division designated operator for the Gulf McKay Federal Well No. 1, and the well has put placed back into active status by Judah Oil. Judah Ex. E; Tr. 97 (Campanella testimony).

(12) The Division has not yet approved Judah Oil as operator of the Dow B Federal No. 1 and the Dalton Federal No. 1, and Division records still reflect Yeso Energy as the Division designated operator of record these two federal wells.

(13) With respect to Judah Oil's qualifications and efforts to assume financial responsibility for the Dow B Federal No. 1 and the Dalton Federal No. 1, the evidence establishes that:

- a. Since August 31, 2010, Judah Oil has been the BLM approved operator of record for these wells. *See* Judah Ex. F and I
- b. Judah Oil has undertaken efforts to return these federal wells to beneficial use within the time frame required by the BLM and with oversight of BLM personnel.
 - (i) With respect to the Dalton Federal No. 1, Judah Oil has addressed environmental issues and demonstrated to the BLM that the well is capable of producing oil. *See* Judah Ex. G and H; Tr. 101-104 (Campanella testimony)
 - (ii) With respect to the Dow B Federal No. 1, Judah Oil has submitted to the BLM, and the BLM has approved, a plan to convert this well to a commercial salt water disposal well. *See* Judah Ex. J.
- c. In August of 2010, Judah Oil obtained and the BLM approved all of the bonds necessary to take over operations of these two federal wells and to convert the Dow B Federal No. 1 to a commercial salt water disposal well. *See* Judah Ex. L.
- d. In August of 2010, Judah Oil filed an administrative application with the Division for approval to inject saltwater into the Dow B Federal No. 1. *See* Judah Ex. K.
- e. In August and September of 2010, Judah Oil submitted the applications to the BLM to obtain a right of way to add the Dow B Federal No. 1 as a commercial

injection well for to its Cedar Lake Disposal Facility. *See* Judah Ex. M; Tr. 114-116.

- f. Judah Oil has filed with the BLM for approval of its Cedar Lake Disposal Facility and expects approval of the facility in a short period of time. *Id.*
- g. Judah Oil has all of the bonds required by the Division to operate wells in New Mexico.
- h. Judah Oil is the only operator that has applied with the Division to become operator of record for these two wells. *See* Judah Ex. N.

(14) With respect to COG's qualifications and efforts to assume financial responsibility for the Dow B Federal Well No. 1, the evidence establishes that:

- a. On or about August 31, 2010, COG appears to have filed a competing administrative application with the Division seeking approval to inject salt water into the Dow B Federal No. 1. *See* COG Ex. 9. However, COG's application is not signed and certified, nor is there evidence that notice to affected parties was provided as required by Division rules. *Id.*
- b. On September 24, 2010, COG filed an administrative application with the BLM seeking a right of way for the purpose of utilizing the Dow B Federal No. 1 as a private disposal well. *See* COG Ex. 2. That application has not been approved by the BLM.
- c. COG has not filed to become operator of record for this well with either the BLM or the Division, nor has the company undertaken steps to bring this federal well under its current bonds. *See* Tr. 73-77 (Evans testimony).
- d. Since COG is not the operator of record recognized by the BLM, COG has no current right to use the Dow B Federal No. 1 and has provided no other evidence of any current right to use this wellbore.
- e. COG has presented no evidence of any approved plan filed with the BLM to use the Dow B Federal No. 1 as a private disposal well.

(15) COG's status with respect to the Dow B Federal No. 1 remains effectively the same as it did when the Division entered Order R-13294 in July of 2010: "COG has no interest in this property at this time except the possibility that their application to use this well as a disposal well will be granted" and has not obtained any other "legal authority to take possession of the subject well."

(16) 19.15.9.9(C) NMAC identifies the circumstances under which the Division may deny approval of a new operator. The evidence establishes that none of these circumstances exist with respect to Judah Oil.

- a. The evidence establishes Judah Oil is in compliance with the inactive well rule, Subsection A of 19.15.5.9 NMAC. *See* Judah Ex. D; Tr. 51 (Sanchez testimony).
- b. Since filing to become the Division designated operator of record for these two federal wells, Judah Oil has expressed a willingness to enter into an agreed compliance order as necessary to bring these two wells into compliance with the inactive well rule. *See* Tr. 128, 175-76 (Campanella testimony). *See also* Tr. 58 (Sanchez testimony).

(17) The evidence established no corporate relationship between Judah Oil and Yeso Energy, and the companies do not share common directors, officers or personnel. *See* Judah Ex. A; Tr. 90-91, 94 (Campanella testimony).

(18) The Division has expressed concern that a purchase and sale agreement involving these federal wells between Yeso Energy as seller, and Judah Oil as buyer, may have created an "affiliate" arrangement within the meaning of 19.15.9.8(B) and NMAC.

(19) With respect to the purchase and sale agreement, the evidence establishes that:

- a. Judah Oil entered into the purchase and sale agreement with Yeso Energy to acquire whatever rights Yeso had to several wells, including the Dow B 28 Federal No. 1 and the Dalton Federal No. 1. *See* Judah Ex. B.
- b. Judah Oil did not have any prior dealings with Yeso Energy and was first approached by Yeso Energy to acquire contractual rights to these wells in July of 2010. *See* Tr. 92-93 (Campanella testimony).
- c. Under the purchase and sale agreement, the conveyance of rights from Yeso Energy to Judah Oil became effective on August 11, 2010.
- d. Under the terms of the agreement, Yeso Energy is entitled to receive additional consideration if the Dow B 28 Federal No. 1 is permitted as a salt water disposal well, namely an additional \$50,000, a fee of \$.05 per barrel of water disposed into the well, and an overriding royalty of ten percent of the net revenue (after state and federal taxes or fees) attributable to oil collected by the salt water disposal operations and sold.
- e. The agreement also provides that Yeso Energy will receive additional consideration if Judah Oil decides to sell the Dow "B" 28 Federal No. 1 within a certain period of time. *See* Tr. 87-88 (Campanella testimony).
- f. Under the agreement, Yeso Energy retains no operational rights to the wells; does not retain any control over the use, sale or other disposition of these federal wells; and retains no contractual responsibility for these wells. *See* Tr. 90 (Campanella testimony).

(20) The current contractual arrangement between Judah Oil and Yeso Energy does not create an "affiliate" arrangement within the meaning of 19.15.9.8(B), or as defined in 19.15.36.12(B) NMAC (dealing with approval of a permit for a surface waste management facility). *See* Judah Ex. C.

(21) Judah Oil's current right to use the Dow B Federal No. 1 is not dependent on its purchase and sale agreement with Yeso Energy and exists instead as a result of its current status as the recognized operator of record with the BLM.

(22) While the Commission has some concerns about Yeso Energy retaining a contingent contractual right to additional revenue from these federal wells, any concern is tempered by the fact that if this contingent right to additional revenue comes into existence, it may provide a means by which the Division can seek to recover amounts owed by Yeso Energy to the State of New Mexico for plugging operations conducted by the Division on properties formerly operated by Yeso Energy. Tr. 49-50 (Sanchez testimony).

(23) Approval of Judah Oil as operator of the Dow B Federal No. 1 is important to the Cedar Lake Disposal Facility, a commercial disposal facility that is expected to serve the needs of an anticipated 50 trucking companies in the area and provide an anticipated disposal capacity of 30,000 to 40,000 barrels of produced water per day. *See* Tr. 114-115 (Campanella testimony).

(24) It appears that the other well at issue - the Dalton Federal No. 1 - is currently capable of producing and ready to commence production once Judah Oil is approved as operator of record by the Division. *See* Tr. 58 (Sanchez testimony); Judah Ex. G and H.

(25) Judah Oil has provided proof of a current right to assume operations of these two federal wells and has effectively taken over financial responsibility for these federal wells.

(26) With respect to wells located on federal lands, it has been the practice and the policy of the Division to recognize, whenever possible, the same operator as the BLM. *See* Tr. 31:18-23; 52:1-5 (Sanchez testimony).

(27) The evidence presented as the hearing demonstrates no reason why Judah Oil, the current BLM operator of record for the Dalton Federal No. 1 and the Dow B Federal No. 1, should not likewise be recognized by the Division as the operator of record.

IT IS THEREFORE ORDERED THAT:

(1) The request for *de novo* review of Case No. 14,472 is dismissed.

(2) The Division shall approve Judah Oil, Inc. as the Division designated operator for the Dalton Federal No. 1 (API #30-015-25259) and the Dow B Federal No. 1 (API #30-015-28676).

(3) Jurisdiction of this case is retained for the entry of such further orders as the Commission may deem necessary.

DONE at Santa Fe, New Mexico, on this ____ day of ____ 2011.

STATE OF NEW MEXICO
OIL CONSERVATION COMMISSION