

## **Draft Order Submitted by OCD**

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

IN THE MATTER OF THE HEARING  
CALLED BY THE OIL CONSERVATION  
COMMISSION FOR THE PURPOSE OF  
CONSIDERING:

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

### **ORDER OF THE COMMISSION**

#### **BY THE COMMISSION:**

This cause came on for hearing at 9 o'clock a.m. on \_\_\_\_\_, 2011, at Santa Fe, New Mexico,  
before the Oil Conservation Commission of New Mexico, hereinafter referred to as the "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) In Case No. 14,472 COG Operating, LLC (OGRID 229137) ("COG") seeks an order  
cancelling the authority of Yeso Energy, Inc. (OGRID 221710) ("Yeso") as the operator of the Dow "B" 28  
Federal Well No. 1 (API No. 30-015-28676) and terminating all spacing and proration units dedicated to  
the well. The case is before the Commission on *de novo* review at Yeso's request.

***Before the OCC  
Case 14472  
Case 14547  
OCD Exhibit 26***

(2) In Case No. 14,547 the Oil Conservation Division (“Division”) seeks an order authorizing the Division to recognize an operator of record for wells currently operated by Yeso.

(3) By Order No. R-13309, issued August 23, 2010, Mark Fesmire, Acting Director of the Oil Conservation Division, found that Case No. 14,472 and Case No. 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. 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.

(4) Due notice has been given in Case No. 14,472 and Case No. 14,547, and the Commission has jurisdiction of the subject matter.

(5) The Division, COG and Judah Oil LLC (OGRID 245872) (“Judah”) appeared through counsel in Case No. 14,472 and Case No. 14,547 and presented testimony and witnesses.

(6) Division records currently identify Yeso as operator of record of the following three wells:

- Dalton Federal No. 001, 30-015-25259
- Dow B 28 Federal No. 001, 30-015-28676
- Morgan Federal No. 001, 30-005-20667

(7) The operator of record with the Division for a well is the operator responsible for regulatory filings with the Division and the entity the Division looks to first for compliance with the Oil and Gas Act and the rules of the Oil Conservation Commission.

(8) The operator of record with the Division may or may not hold the lease associated with the well, and in the case of federal wells, may or may not be the operator of record recognized by the Bureau of Land Management. The regulatory requirements for change of operator do not require the Division to consider the operator’s right to operate the wells, unless the existing operator of record is not available to transfer operations to the new operator. In that situation, the new operator must provide proof of its right to assume operations.

(9) 19.15.9.9.C NMAC sets out two methods for changing the operator of record for a well:

“The operator of record with the division and the new operator shall apply for a change of operator by jointly filing a form C-145 using the division’s web-based online application. Or, if the operator of record is unavailable, the new operator shall apply to the division for approval of change of operator without a joint application. The operator shall make such application in writing and provide documentary evidence of the applicant’s right to assume operations. The new operator shall not commence operations until the division approves the application for change of operator.”

(10) In practice, if the operator of record is unavailable, counsel for the OCD hearing examiners reviews the application for change of operator and the documentary evidence of the

applicant's right to assume operations. If counsel is satisfied that the operator of record is unavailable and the applicant has the right to assume operations, the Division gives the applicant the authority to make the change using the OCD's online system. If counsel does not approve the application, the applicant may request that the matter be set for hearing.

(11) 19.15.9.9.C NMAC provides that the director or the director's designee may deny a change of operator in certain situations. One such situation is if the wells are subject to a compliance order requiring the wells to be brought into compliance with the inactive well rule, 19.15.25.8 NMAC, and the new operator has not entered into an agreed compliance order setting a schedule for compliance with the existing order.

(12) The Dalton Federal No. 001, the Dow B 28 Federal No. 001 and the Morgan Federal No. 001 are subject to R-12930-B, a compliance order requiring the wells to be returned to compliance with the inactive well rule.

(13) R-12930-B provides, in relevant part,

"(1) Yeso Energy, Inc. [OGRID 22170] shall properly plug and abandon each of the wells ...or transfer each of said wells to another operator, not affiliated with Yeso and approved by the Division, not later than March 15, 2010.

(2) If Yeso fails to comply with Ordering Paragraph (1) with respect to any of the subject wells within the time provided the Division is hereby authorized to plug any of the subject wells with respect to which Yeso fails to comply, and to restore the well sites, as provided in Division Rules, and all applicable financial assurance shall be forfeited, as provided in NMSA 1978, Section 70-2-14."

(14) Yeso did not plug and abandon or transfer the three wells at issue by March 15, 2010.

(15) After March 15, 2010, the Division placed the wells at issue on its list of wells to be plugged.

(16) Chica Energy, LLC (OGRID 271866) ("Chica") registered with the Division as a well operator in New Mexico, and Yeso and Chica filed an on-line application to transfer Yeso's wells to Chica.

(17) The Division obtained information that the managing member of Chica was the daughter of the president of Yeso, and asked the managing member of Chica if the two companies were affiliated.

(18) Chica withdrew its application for change of operator. Although Chica expressed its intent to re-file an application to become operator of record of some of the Yeso wells, that application never came before the Division for approval.

(19) A representative of COG contacted Division Compliance and Enforcement Manager Daniel Sánchez, and expressed interest in becoming the operator of record of the Dow B 28 Federal No. 001.

(20) The COG representative spoke to counsel for the Division hearing examiners about the process for applying to become operator of record when the current operator does not agree to the change.

(21) As a result of that conversation, COG filed the application for hearing in Case No. 14,472, seeking cancellation of Yeso's authority as to the Dow B 28 Federal Well No. 1 and termination of spacing units associated with that well.

(22) COG, Yeso, Chica and the Division appeared at the hearing in Case No. 14,472.

(23) At the hearing, COG provided testimony that it intended to use the Dow B 28 Federal No. 1 Well as a salt water disposal well.

(24) On July 13, 2010, the Division issued Order R-13294 in Case No. 14,472. The order provides, in relevant part,

"(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) NMMPM, 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."

(25) Yeso filed a request for de novo review in Case No. 14,472, but did not file a request to stay Order R-13294.

(26) Yeso and Chica as "sellers" entered into a purchase and sale agreement with Judah as "buyer" conveying the sellers' rights to several wells, including the Dow B 28 Federal Well No. 1 and the Dalton Federal No. 001. According to the terms of the purchase and sale agreement, the conveyance became effective August 11, 2010.

(27) Under the terms of the purchase and sale agreement, the sellers received \$10.00 in consideration. The sellers would receive additional consideration if the Dow B 28 Federal No. 1 is permitted as a salt water disposal well: \$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. The agreement also provided that Yeso and Chica would receive additional consideration if Judah sells the Dow "B" 28 Federal No. 1.

(28) If Order R-13294 had not terminated Yeso's authority to operate the Dow "B" 28 Federal No. 1 well, Yeso would still be unable to obtain a permit to inject into the well under its own name, because Yeso is in violation of 19.15.5.9 NMAC and the Division would not be able to approve an injection permit for Yeso. See 19.15.26.8 NMAC.

(29) On August 18, 2010 Judah and Yeso submitted an online application to transfer Yeso wells from Yeso to Judah. The application included the Dow "B" 28 Federal No. 1 and the Dalton Federal No. 001.

(30) The Division did not process the application, because Order R-13294 had terminated the authority of Yeso to act as operator of the Dow "B" 28 Federal No. 1, one of the wells covered by the application for well transfer.

(31) On August 19, 2010, the day after Judah and Yeso submitted the application for well transfer, the Division filed its application for hearing in Case No. 14,547, asking for guidance on determining the appropriate operator of record for the Yeso wells, given the language in Order R-12930-B limiting well transfers to operators not affiliated with Yeso and the language in Order R-13294 terminating the authority of Yeso to act as operator of the well (and allowing COG to apply to use the well for disposal without the necessity of a change of operator).

(32) By application dated August 17, 2010 Judah sought approval from the Division to use the Dow "B" 28 Federal No. 1 as a commercial salt water disposal well. Judah is not the operator of record of the well. The Division has not acted on the application.

(33) By application dated August 31, 2010, COG sought approval from the Division to use the Dow "B" 28 Federal No. 1 as a salt water disposal well. COG is not the operator of record of the well. However, Order R-13294 provides that "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." The Division has not acted on the application.

(34) Judah signed for receipt of the notice of hearing in Case No. 14,547 on August 25, 2010. That notice of hearing included a copy of the application, explaining that the Division was seeking guidance on which operator to recognize as operator of record for the Yeso wells, including the Dalton Federal No. 001.

(35) According to Judah's own regulatory filings, Judah put the Dalton Federal No.001 back on production on October 4, 2010, without becoming operator of record for the well.

(36) Judah was aware that Division rules prohibit operation of a well before becoming operator of record. When Judah registered with the Division as a well operator in 2009, the Division provided Judah with a document describing certain OCC rule requirements, which the manager of Judah signed. That list includes the statement "I understand that if I acquire wells from another operator, the OCD must approve the operator change before I begin operating those wells. See 19.15.9.9.B NMAC."

The same statement appears on the operator change applications signed by the manager of Judah on August 18, 2010.

(37) By letter dated October 6, 2010, Yeso requested to withdraw from both Case 14,472 and Case 14,547.

(38) By letter dated October 7, 2010, Chica stated that it did not want to be a party in either Case 14,472 or Case 14,547.

**The Commission Concludes that:**

(39) Because Yeso, the party that applied for *de novo* review of Case No. 14,472, has now withdrawn from that case, the request for *de novo* review should be denied.

(40) Order R-13294, issued in Case No. 14,472, was never stayed and remains in effect.

(41) Because Order R-13294 terminated the authority of Yeso to act as operator of the Dow "B" 28 Federal Well No. 1, Yeso has no authority to apply for an operator transfer that would recognize another operator of record for the well.

(42) The intent of Order R-13294 was to allow COG to pursue its intention to obtain the Dow "B" 28 Federal Well No. 1 for use as a salt water disposal well, and gave COG until July 30, 2011 to make its arrangements.

(43) Until July 30, 2011, the OCD should not plug the well or recognize a transfer of the well to any operator other than COG.

(44) By July 30, 2011, COG should apply to become operator of record of the Dow "B" 28 Federal No. 1 Well, following the procedure set out in 19.15.9.9.C NMAC for operator change when the current operator is unavailable. If COG fails to meet the requirements of 19.15.9.9.C NMAC by July 30, 2011, the OCD may plug the well or recognize another operator as operator of record for the well.

(45) Any operator seeking to become operator of record for the Dow "B" 28 Federal No. 1 Well must provide documentary evidence that it has the right to assume operations, as required by 19.15.9.9.C NMAC, and meet any other requirements set by rule or order.

(46) Order R-12930-B's provision allowing Yeso to transfer the Yeso wells "to another operator, not affiliated with Yeso and approved by the Division" not later than March 15, 2010, means that Yeso may not transfer the wells to an "affiliated" entity.

(47) Order R-12930-B provides that after March 15, 2010 the Division has the authority to plug any well covered by the order that Yeso had not properly plugged and abandoned or transferred to another approved operator. Order R-12930-B gives the Division the discretion to refuse to recognize any new operator of record for any of the wells covered by Order R-12930-B.

(48) If the Division chooses to allow a transfer after March 15, 2010, the Division may take into consideration whether the transfer is to an "affiliated" entity, or whether the transfer is designed to avoid the effect of Order R-12930-B.

(49) The purchase and sale agreement between Yeso/Chica and Judah creates an on-going business relationship between Yeso/Chica and Judah, under which Yeso/Chica maintain an income stream from the salt water disposal business. Yeso would not have been able to use the well for salt water disposal under its own name, because it is out of compliance with 19.15.5.9 NMAC.

(50) It is within the discretion of the OCD to deny the well transfers to Judah that would have the effect of circumventing both the language in Order R-12930-B and enforcement rule 19.15.5.9 NMAC, and condone Judah's operation of the Dalton Federal No. 001 without becoming operator of record in violation of 19.15.9.9.B NMAC.

**IT IS THEREFORE ORDERED THAT:**

- (1) The request for *de novo* review of Case No. 14,472 is Denied.
- (2) Until July 30, 2011, the OCD should not plug the Dow "B" 28 Federal Well No. 001 or recognize a transfer of the well to any operator other than COG.
- (3) By July 30, 2011, COG should apply to become operator of record of the Dow "B" 28 Federal Well No. 1, following the procedure set out in 19.15.9.9.C NMAC for operator change when the current operator is unavailable. If COG fails to meet the requirements of 19.15.9.9.C NMAC by July 30, 2011, the OCD may plug the well or recognize another operator as operator of record for the well.
- (4) Any operator seeking to become operator of record for the Dow "B" 28 Federal No. 1 Well must provide documentary evidence that it has the right to assume operations, as required by 19.15.9.9.C NMAC, and meet any other requirements set by rule or order.
- (5) Pursuant to Order R-12930-B, the OCD has the discretion to plug and abandon the Dalton Federal No. 1 and the Morgan Federal No. 1, or may recognize a new operator of record for the wells using the procedure set out in 19.15.9.9.C NMAC for an operator change where the current operator of record is not available.
- (6) It is within the discretion of the OCD to deny the well transfers to Judah, because transferring the wells under the existing purchase and sale agreement would have the effect of circumventing both the language of Order R-12930-B and enforcement rule 19.15.5.9 NMAC, and would condone Judah's operation of the Dalton Federal No. 001 without becoming operator of record in violation of 19.15.9.9.B NMAC.
- (7) 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