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 MACK ENERGY CORPORATION FOR COMPULSORY POOLING, LEA COUNTY, NEW MEXICO.

Case No. 14,763 (*de novo*)

PRE-HEARING STATEMENT
OF
MACK ENERGY CORPORATION

This pre-hearing statement is submitted by applicant Mack Energy Corporation as required by the Oil Conservation Division.

APPEARANCES

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OPPONENT
Tom M. Ragsdale

OPPONENT'S ATTORNEY
J. Scott Hall

STATEMENT OF THE CASE

APPLICANT

Facts.

Mack Energy Corporation ("Mack") is operator of the Cockburn A State Well No. 5 (the "well"), an existing well completed in the Abo formation, located in the SE¼NW¼ of Section 32, Township 17 South, Range 33 East, N.M.P.M. Mack desires to re-enter and frac the well to increase production.

Siana Operating, LLC ("Siana") acquired the well, and the related lease, from OXY USA WTP Limited Partnership ("OXY") in 2004. It then assigned all of its interest to Caza Energy, LLC (a Mack-affiliated entity), which subsequently assigned 6.25% to Tom. M. Ragsdale, a principal of Siana ("Mr. Ragsdale"). The remaining 93.75% is owned by a Mack-affiliated entity. Mack operates wells for Chase Oil Corporation and, prior to its dissolution, operated wells for Caza Energy, LLC.

Mack successfully re-completed the well from the Morrow formation to the Abo formation in 2004. Mr. Ragsdale contributed to the re-completion, and began receiving joint interest billings and payments on the well (payments were made by Navajo Refining Company until March 2006, and by Mack thereafter). Mr. Ragsdale never complained about them.

A modern frac has never been performed on the well. In 2011 Mack began considering fracing the well, and employed Michael McCoy, a registered professional engineer and partner of Ely & Associates, to examine the potential results of a frac. Ely & Associates is the world leader in fracture stimulation design. Mr. McCoy testified at the Division, and will testify before the Commission, that the proposed frac will increase ultimate recovery from the well.

Title information on the well was received by Mack from Siana when the well was acquired.[1] While reviewing title information on the well in 2010, Mack could not locate a joint operating agreement. A subsequent review of the county records turned up an instrument entitled "Operating Agreement." However, upon closer review this instrument was determined to be an assignment, and not a joint operating agreement. It turns out that the prior operator of the well, OXY, owned 100% of the working interest, so there was no need for an operating agreement.

Mack sent Mr. Ragsdale a re-entry proposal, with an AFE, by letter dated August 30, 2011. Mack's engineer, Lee Livingston, and Siana's operations manager, Matt Doffer (acting on Mr. Ragsdale's behalf), had at least three telephone discussions during September and October 2011 discussing the proposal. Mr. Ragsdale never signed the AFE. Because there was no joint operating agreement, Mack then filed an application with the Division seeking an order pooling the uncommitted mineral interest owner from the surface to the base of the Abo formation underlying the SE¼NW¼ of Section 32. Mr. Ragsdale's Texas attorney, Tom Zabel, subsequently called Mack's landman, Staci Sanders, and requested that Mack send his client a joint operating agreement. A proposed joint operating agreement was sent by Mack to Mr. Ragsdale by letter dated December 7, 2011. Mack has sent follow-up letters to Mr. Ragsdale, but he has never sent Mack any comments on the proposed joint operating agreement.

Before the Division, Mr. Ragsdale opposed the pooling, asserting (among other reasons) that (a) Mack did not make a good faith effort to voluntarily pool the acreage, and (b) the proposed frac is too risky and unnecessary. He also requested that no risk charge be assessed.

[1] Interestingly, Mr. Ragsdale complained before the Division that Mack refused to provide him title and other information regarding the well. As Mack proved before the Division and will again prove if the Commission deems necessary, this information was provided to Mr. Ragsdale on at least three occasions.

However, Order No. R-13519 granted Mack's application to pool Mr. Ragsdale into the well. Mr. Ragsdale subsequently filed an application for a hearing *de novo*.

Issues.

Mr. Ragsdale raised several issues before the Division, and Mack anticipates that they will also be raised before the Commission. They are discussed briefly below.

(1) Mr. Ragsdale claimed that Mack is not in compliance with the pooling statutes because it did not enter into an operating agreement with Mr. Ragsdale after assuming operations in 2004. However, under the case of *Bellet v. Grynberg*, 114 N.M. 690, 845 P.2d 784 (S. Ct. 1992), Mack was entitled to operate the well without an operating agreement, and recover operating costs. The Court in *Bellet* found that, in a situation identical to the present case, the working interest owners were co-tenants, and the law implies a contract for the non-operator to pay its proportionate share of reasonable and necessary operating expenses to the operator of a well. The evidence to be presented at the hearing will demonstrate that Mr. Ragsdale acted in accordance with this well established principle by paying his joint interest billings for many years.

In addition, Mr. Ragsdale, at any time over the last 7-8 years, could have requested an operating agreement or could have force pooled all interests into the well unit. He did not do so, although he was fully aware of the land matters affecting the well. In fact, the pooling statute expressly permits compulsory pooling after a well is drilled. NMSA 1978 §70-2-17.C.

(2) Mr. Ragsdale also asserted that the Division should not grant Mack's pooling request because it did not make a good faith effort to obtain Mr. Ragsdale's voluntary joinder in the proposed frac. However, the facts stated above show Mack made a good faith effort to

obtain Mr. Ragsdale's voluntary agreement to re-complete the well. The Division, in its order, found that Mack had made a good faith effort.

The pooling statute states that, where the parties in a well unit have not entered into a voluntary agreement covering a well unit, the Division (and Commission) "shall pool" the interests in the well. NMSA 1978 §70-2-17.C. Thus, compulsory pooling must be affirmed by the Commission.

(3) After the Division hearing, Mr. Ragsdale, for the first time, raised an issue about (i) Mack's authority to operate, and (ii) Mack's right to file a pooling application, because Mack owns no working interest in the well. Mr. Ragsdale's position is incorrect, for the following reasons:

(a) Mack is operator of record of the well in the Division's files.

(b) Mack operates wells for the Mack-related entities which own working interests in the well.

(c) Division rules allow an operator "or other person with standing" to file adjudicatory applications with the Division. NMAC 19.15.4.8.A. Based on the above facts, Mack has standing to file a pooling application.

Mr. Ragsdale has received bills from and made payment to Mack for years without complaint. A person cannot sell a deal, keep a part interest, turn over well files, accept revenue payments, be silent for years, and now claim that Mack is not authorized to operate the well. *Purvis Oil Corp. v. Hillin*, 890 S.W.2d 931 (Tex. Civ. App. 1994) (where a party fails, for a period of years, to object to operations by another party not explicitly authorized to operate an oil and gas lease, the complaining party waives the right to argue that the operating party is not entitled to operate because it does not own an interest in the lease).

(4) Mr. Ragsdale complained that Mack has not complied with NMSA 1978 §70-2-18.B, and that it is entitled to an interest in the well greater than 6.25%. The statute states:

> Any operator failing to obtain voluntary pooling agreements, or failing to apply for an order of the division pooling the lands dedicated to the spacing or proration unit as required by this section, shall nevertheless be liable to account and pay each owner of minerals or leasehold interest, including owners of overriding royalty interests and other payments out of production, either the amount to which each interest would be entitled if pooling had occurred or the amount to which each interest is entitled in the absence of pooling, whichever is greater.

(Emphasis added). Mr. Ragsdale misinterprets this statute. This statute is meant to protect a landowner when a tract of land is not pooled into a larger well unit. For example, assume that the W½ of Section 32 was dedicated to a Morrow well, located on the SE¼NW¼ of Section 32, and the SE¼NW¼ had never been committed to the well by voluntary agreement or compulsory pooling. **In that situation**, the above statute would apply, and Mr. Ragsdale would be entitled to his 6.25% working interest in the well's proceeds until pooling occurred, rather than a 6.25% x 40/320 = 0.78125% working interest if pooling had previously occurred. The case of *Moncrief v. Harvey*, 816 P.2d 97 (Wyo. 1991), is directly on point and confirms Mack's interpretation of the statute. Because the case at hand involves a 40 acre well unit with undivided interests, without other lands involved, and Mr. Ragsdale has always received the proceeds he would be entitled to under any scenario (whether voluntary or compulsory pooling), Mr. Ragsdale is not entitled to any additional interest in the well: His working interest is 6.25% as a tenant in common, and it will be 6.25% under a pooling order or operating agreement.

(5) Mr. Ragsdale has not paid a joint interest billing for two years. Although Mack continued to pay Mr. Ragsdale for one year of that time, Mr. Ragsdale's continued refusal to pay expenses became so abusive and unfair that Mack had no choice but to place him in suspense. Mack has, however, offered on at least two occasions to release the suspended funds if Mr.

Ragsdale will pay his joint interest billings or, in the alternative, authorize Mack to release the funds net of the amount Mr. Ragsdale owes to Mack.

Mr. Ragsdale complained about the suspension of his runs before the Division, and Mack anticipates that issue could arise again before the Commission. These complaints are without merit. First, to the extent Mr. Ragsdale complains that Mack is not paying him in a proper manner, that issue sounds in contract or in tort and is proper before a district court, not the Division or the Commission. Second, even if it were properly heard by the Commission, Mr. Ragsdale's complaint is legally incorrect. It is well-settled that an operator may recover expenses associated with operating oil and gas wells from its cotenant by reimbursement out of production. *Shaw & Estes v. Texas Consolidated Oils*, 299 S.W.2d 307, 314 (Tex. Civ. App. 1957). Finally, on a common sense level, Mr. Ragsdale's refusal to communicate with Mack has precluded him from having his runs released. Mack has offered to release the runs if Mr. Ragsdale will provide written authorization to do so, but he has refused to respond to those offers.

Conclusion

Mack seeks an order pooling all mineral interests from the surface to the base of the Abo formation underlying the SE¼NW¼ of Section 32, Township 17 South, Range 33 East, N.M.P.M., to be dedicated to the Cockburn A State Well No. 5, an existing well to be re-completed (frac'd) in the Abo formation, naming Mack as operator of the well, and granting a 200% charge for the risk involved in re-completing the well.

The Division reduced the risk charge to 100% from the normal 200%, finding that the risk of the frac was not excessive. Mack notes that Mr. Ragsdale himself testified that there was "significant risk" in the re-entry proposal, thus completely undermining his request that no risk

charge be assessed if the pooling application is granted. There is no evidence justifying a reduction in the standard cost + 200% risk charge.

OPPONENT

PROPOSED EVIDENCE

APPLICANT

WITNESSES	EST. TIME	EXHIBITS
Staci D. Sanders (landman)	30 min.	Approx. 12
Michael McCoy (engineer)	20 min.	Approx. 2
Lee Livingston (engineer)	30 min.	Approx. 4

OPPONENT

WITNESSES	EST. TIME	EXHIBITS

PROCEDURAL MATTERS

-None-

Respectfully submitted,

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