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May 19, 2005

HAND-DELIVERED

Ms. Florene Davidson
New Mexico Oil Conservation Division
1220 South St. Francis
Santa Fe, New Mexico 87505

Case 13533

2005 MAY 19 PM 2 38

Re: In the Matter of the Application of Energen Resources Corporation to Amend Compulsory Pooling Order No. R-10154 to Include Provisions for an Infill Well and to Address Excess Royalty Burdens, San Juan County, New Mexico

Dear Florene:

Please schedule the hearing before the Division for the above-referenced matter on August 11, 2005.

Thank you for your assistance.

Very truly yours,

MILLER STRATVERT P.A.

J. Scott Hall

J. Scott Hall

JSH/glb

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

**IN THE MATTER OF THE APPLICATION OF
ENERGEN RESOURCES CORPORATION TO AMEND
COMPULSORY POOLING ORDER NO. R-10154
TO INCLUDE PROVISIONS FOR AN INFILL WELL
AND TO ADDRESS EXCESS ROYALTY BURDENS,
SAN JUAN COUNTY, NEW MEXICO**

CASE NO. 13533

APPLICATION

Energen Resources Corporation, by its undersigned attorneys, Miller Stratvert P.A. (J. Scott Hall) hereby makes application pursuant to NMSA 1978 § 70-2-17 (1995) for an Order Amending Compulsory Pooling Order No. R-10154 which pooled all interests in the Fruitland Coal formation, (Basin-Fruitland Coal Gas Pool) underlying the S/2 of Section 19, Township 30 North, Range 11 West, NMPM, San Juan County, New Mexico, forming a standard 326.26 acre spacing and proration unit. In support thereof, Applicant would show the Division:

1. Applicant is the current operator of the Flora Vista "19" Well No. 2 drilled to the Fruitland Coal formation (Basin-Fruitland Coal Gas Pool) in 1994 by SG Interests I, Ltd. The Flora Vista "19" Well No. 2 is located at a standard coal gas well location 833 feet from the south line and 1465 feet from the west line (N) of said Section 19.

2. Applicant also operates the Flora Vista "19" Well No. 3 which it drilled as a Fruitland Coal formation infill well in 2004, at a standard location 675 feet from the south line and 1025 feet from the east line (P) of Section 19. The S/2 of Section 19 is dedicated to both the No. 2 and the No. 3 wells.

3. Previously, on July 19, 1994, pursuant to a hearing held on June 23, 1994, the Division issued Order No. R-10154 pooling certain uncommitted interests in the S/2 of Section

19 preparatory to the drilling of the Flora Vista "19" Well No. 2 by SG Interests I, Ltd., as contract operator for Maralex Resources, Inc. (Case No. 11007; Application of Maralex Resources, Inc. for Compulsory Pooling, San Juan County, New Mexico).

4. The evidence at the hearing established that the applicant in that case owned or controlled the majority of the working interests in the S/2 of Section 19 and that the applicant sought to pool the remaining interests of those owners who did not agree to participate in the drilling of the well. The quantum of the non-participating interests constituted a relatively large percentage of the interest in the unit. The Division accordingly granted the applicant's request and issued Order No. R-10154 pooling the interests of Norman L. Gilbreath and Loretta E. Gilbreath, husband and wife, the owners of the leasehold in the SE/4 of Section 19 that comprised approximately 48.60% of the working interests in the S/2 unit dedicated to the Flora Vista "19" Well No. 2.

5. The Gilbreaths entered their appearances *pro-se* at the June 23, 1994 Division hearing on the Maralex application in Case No. 11007. The Gilbreaths were allowed to cross-examine the applicant's witnesses and provide their own brief testimony.

6. On June 21, 1994, two days before the Division hearing in Case No. 11007, the Gilbreaths executed an overriding royalty assignment conveying to themselves a "16-2/3rds% of 8/8ths overriding royalty interest in the lease assigned to them by Calvin Petroleum Corporation, et al.". The assignment of their overriding royalty was not filed of record with the San Juan County Clerk's office at the time Maralex Resources, Inc. filed the application for compulsory pooling in the case on May 27, 1994. The transcript and exhibits from the June 23, 1994 hearing contain no evidence of the existence of the assignment and the Gilbreaths made no other effort to apprise the hearing examiner or the Division of the interest. On information and belief, at no

time subsequent to the June 23, 1994 hearing did the Gilbreaths inform Maralex, SG or Energen of the existence of the overriding royalty interest.

7. The oil and gas lease owned by the Gilbreaths and covering the lands in the SE/4 of Section 19 provides for a 12-1/2% royalty interest. Together with the 16-2/3rds% overriding royalty interest claimed by the Gilbreaths, the total royalty burden on the lease in the SE/4 of Section 19 is approximately 29.166%.

8. Subsequent to the hearing and the issuance of Order No. R-10154, SG Interests I, Ltd. drilled and successfully completed the Flora Vista "19" Well No. 2 in the Fruitland Coal formation. SG Interests I, Ltd. continued to act as designated operator of the Flora Vista "19" Well No. 2 until approximately August 1, 2004 when Energen Resources Corporation acquired ownership of the property. On August 3, 2004, the Division approved the Change of Operator for the Flora Vista "19" Well No. 2 from SG to Energen.

9. On November 21 2004, applicant Energen Resources Corporation spudded the Flora Vista "19" Well No. 3 infill well. The well reached total depth in the Fruitland Coal formation on December 4, 2004 and first production from the Flora Vista "19" Well No. 3 occurred on January 10, 2005.

10. Although the Gilbreaths' interest in the S/2 spacing and proration unit were previously pooled under Order No. R-10154, Energen did not solicit the voluntary participation of the Gilbreaths in the drilling of the infill well until after the well was completed. Applicant has since been unable to obtain the voluntary agreement of the Gilbreaths for their participation in the drilling of the Flora Vista 19 Well No. 3.

11. Order No. R-10154 made no provisions for the drilling, completion and operation or the recovery of costs for an infill well. Energen, by this application seeks the amendment of Order No. R-10154 to provide for the drilling of the infill well.

12. The amendment of Order No. R-10154 will afford the Applicant the opportunity to produce its just and equitable share of hydrocarbons underlying the spacing unit, will avoid the drilling of unnecessary wells, will prevent waste and will protect correlative rights.

13. Applicant seeks an order amending Order No. R-10154 that will allow Applicant to recover its costs of drilling, equipping and completing the Flora Vista "19" Well No. 3 infill well and the allocation of the costs thereof, its costs of supervision while drilling and after completion, including overhead charges and providing for adjustments to such rates in accordance with accepted COPAS accounting procedures, and imposing a 200% risk penalty for the risks assumed by the Applicant in drilling, completing and equipping the well, and making such other and further provisions as may be proper.

14. The conveyance by Norman L. Gilbreath and Loretta E. Gilbreath unto themselves of the 16-2/3rds% of 8/8ths overriding royalty referenced in paragraph 6 above is not the result of an arms-length transaction and was undertaken to circumvent the Division's authority under the New Mexico Oil and Gas Act to promote the interests of conservation and to prevent waste. Further, the imposition of the additional excess royalty burden on the SE/4 of Section 19 dedicated to the 326.26 acre unit causes the operator and the other interest owners in the spacing unit to bear a disproportionate and unreasonable share of costs.

15. Applicant further seeks the issuance of an order authorizing the recovery of costs and the risk penalty out of the full working interest in the lease owned by the Gilbreaths, or their

successors or assigns, without recognition of the 16-2/3rds overriding royalty interest claimed by them pursuant to the transaction referenced in paragraph 6 above.

WHEREFORE, Energen Resources Corporation, as Applicant, requests that this application be set for hearing before a duly appointed examiner of the Oil Conservation Division on August 11, 2005 and that after notice and hearing as required by law, the Division enter its order amending Order No. R-10154 as follows:

1. Naming Applicant as operator of the Flora Vista "19" Well No. 3 infill well;
2. Providing for the Applicant and all working interest owners with the opportunity to participate in the costs of drilling, completing, equipping and operating the infill well;
3. Providing for Applicant to recover out of production its costs of drilling, equipping, completing and operating the Flora Vista 19 Well No. 3 infill well, and the allocation of the costs thereof, its costs of supervision while drilling and after completion, including overhead charges and providing for adjustments to such rates in accordance with accepted COPAS accounting procedures and imposing a 200% risk penalty factor against the interests of those owners electing not to participate in the drilling, equipping and completing of the well;
4. Authorizing Applicant to recover the non-participating parties' share of costs for the infill well out of their full working interest without recognition of the 16-2/3rds% overriding royalty interests claimed by the Gilbreaths;
5. Further authorizing Applicant to recover the non-participating parties' share of costs of supervision and operations for the Flora Vista 19 Well No. 2 parent well out of their full working interest without recognition of the 16-2/3% overriding royalty interest claimed by the Gilbreaths;
6. And including such other and further provisions as may be proper.

Respectfully submitted,

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