

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:)

) CASE NO. 13,555

APPLICATION OF THE NEW MEXICO OIL)
CONSERVATION DIVISION FOR ADOPTION OF)
A NEW RULE CONCERNING INFILL WELLS AND)
COMPULSORY POOLED UNITS)

ORIGINAL

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REPORTER'S TRANSCRIPT OF PROCEEDINGS

COMMISSION HEARING

BEFORE: MARK E. FESMIRE, CHAIRMAN
JAMI BAILEY, COMMISSIONER
FRANK T. CHAVEZ, COMMISSIONER

September 15th, 2005

Santa Fe, New Mexico

This matter came on for hearing before the Oil Conservation Commission, MARK E. FESMIRE, Chairman, on Thursday, September 15th, 2005, at the New Mexico Energy, Minerals and Natural Resources Department, 1220 South Saint Francis Drive, Room 102, Santa Fe, New Mexico, Steven T. Brenner, Certified Court Reporter No. 7 for the State of New Mexico.

* * *

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September 15th, 2005
 Commission Hearing
 CASE NO. 13,555

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* * *

A P P E A R A N C E S

FOR THE COMMISSION:

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* * *

1 WHEREUPON, the following proceedings were had at
2 10:40 a.m.:

3 CHAIRMAN FESMIRE: The next cause before the
4 Commission is Case Number 13,555. It's the Application of
5 the New Mexico Oil Conservation Division for adoption of a
6 new Rule concerning infill wells and compulsory pooled
7 units.

8 At this time is there an appearance of counsel?

9 MS. O'CONNOR: Yes, thank you, Mr. Chairman. My
10 name is Cheryl O'Connor and I'm an attorney for the Oil
11 Conservation Division.

12 CHAIRMAN FESMIRE: Okay. Are there any other
13 appearances in this case?

14 Cheryl, do you have any witnesses?

15 MS. O'CONNOR: I have one, Mr. Chairman. And
16 would it please the Commissioners if I sit instead of
17 standing?

18 CHAIRMAN FESMIRE: Would you introduce your
19 witness and have him sworn, please?

20 MS. O'CONNOR: I will. We call David Brooks.

21 (Thereupon, the witness was sworn.)

22 CHAIRMAN FESMIRE: Ms. O'Connor, would you please
23 proceed?

24 THE WITNESS: Mr. Chairman, could I respectfully
25 request a five-minute recess before we start the

1 proceedings?

2 CHAIRMAN FESMIRE: Surely, we'll take a five-
3 minute break.

4 THE WITNESS: Thank you, Mr. Chairman.

5 (Thereupon, a recess was taken at 10:42 a.m.)

6 (The following proceedings had at 10:55 a.m.)

7 CHAIRMAN FESMIRE: Ms. O'Connor, I believe you're
8 up.

9 MS. O'CONNOR: Yes, thank you.

10 DAVID K. BROOKS, JR.,

11 the witness herein, after having been first duly sworn upon
12 his oath, was examined and testified as follows:

13 DIRECT EXAMINATION

14 BY MS. O'CONNOR:

15 Q. Could you introduce yourself to the Commission
16 and explain to them your occupation?

17 A. Okay, my name is David Brooks and I am Assistant
18 General Counsel for the Energy, Minerals and Natural
19 Resources Department. I work for the General Counsel,
20 however I am more or less permanently assigned to work with
21 the oil and gas -- with the Oil Conservation Division, and
22 I work here in the Santa Fe office.

23 Q. And Mr. Brooks, as you know, we're here today on
24 an application to adopt Rule 36. Were you involved in
25 drafting that Rule?

1 A. Intimately.

2 (Laughter)

3 Q. (By Ms. O'Connor) I'm going to refer you to
4 Exhibit A, and there are two parts of Exhibit A. Could you
5 -- Do you recognize Exhibit A-1?

6 A. I recognize Exhibit A-1.

7 Q. Could you explain what that is?

8 A. Exhibit A-1 is a draft of proposed new Rule 36
9 and a proposed amendment to Rule 7.W.(9) as attached to the
10 Application for rulemaking that I filed to institute this
11 proceeding.

12 Q. Now, behind Exhibit A-1 there is Exhibit A-2. Do
13 you recognize that exhibit?

14 A. Yes.

15 Q. And could you explain to the Commission what the
16 difference is between A-1 and A-2?

17 A. Okay, Exhibit A-2 is what has become inevitable
18 in our rulemaking proceedings. That's the revisions that
19 we're now recommending from what we originally recommended.
20 Do you want me to go ahead and explain what they are and
21 the reasons for them?

22 Q. Not yet. Let me ask you, is Exhibit A-1 the Rule
23 as originally proposed?

24 A. It is.

25 Q. And is Exhibit A-2 a correct and accurate copy of

1 the Rule that's being proposed with some changes?

2 A. That is correct.

3 MS. O'CONNOR: I would move to have, or request
4 to have, Exhibits A-1 and A-2 admitted into evidence at
5 this time.

6 CHAIRMAN FESMIRE: Any objection?

7 COMMISSIONER BAILEY: No.

8 COMMISSIONER CHAVEZ: No.

9 CHAIRMAN FESMIRE: Exhibits A-1 and A-2 are
10 admitted.

11 Q. (By Ms. O'Connor) Mr. Brooks are you familiar
12 with the notice requirements for publication for
13 rulemaking?

14 A. I am.

15 Q. And what are those requirements?

16 A. The notice of rulemaking must be published in the
17 *New Mexico Register* at least 10 days prior to the hearing.
18 It must be published in a newspaper of general circulation
19 in the state at least 20 days prior to the hearing.

20 Q. I would refer you to --

21 A. Well, wait, there's more.

22 Q. I'm sorry. Oh, pardon me.

23 A. It must be published on the Division's website at
24 least 20 days prior to the hearing, and it must be
25 distributed to those persons who have requested to receive

1 copies of the Commission's docket at least 20 days prior to
2 the hearing. Also by virtue of a Legislative enactment at
3 the last session, it must be provided to the Small Business
4 Advisory Council, I believe. I may have the exact name of
5 that agency wrong, but it's something like that, that's
6 attached to the Economic Development Department.

7 Q. I would refer you to Exhibit B.

8 A. Yes, ma'am.

9 Q. Do you have a copy of that --

10 A. I do.

11 Q. -- in front of you? Okay, and could you explain
12 to the Commissioners what Exhibit B is?

13 A. Exhibit B is an affidavit of publication from *The*
14 *Albuquerque Journal*, including a copy of the advertisement
15 that was published concerning this proceeding, and it
16 reflects that it was published one time on the 24th of
17 August, 2005.

18 Q. And therefore does Exhibit B reflect or show that
19 the publication was done as required in *The Albuquerque*
20 *Journal*?

21 A. It does.

22 MS. O'CONNOR: I would request that Exhibit B be
23 admitted into evidence.

24 CHAIRMAN FESMIRE: Any objections?

25 COMMISSIONER BAILEY: No.

1 COMMISSIONER CHAVEZ: No objection.

2 CHAIRMAN FESMIRE: Exhibit B is so admitted.

3 Q. (By Ms. O'Connor) Mr. Brooks, I refer you to
4 Exhibit C.

5 A. Yes, ma'am.

6 Q. Do you recognize that exhibit?

7 A. I do.

8 Q. And could you explain to the Commissioners what
9 that is?

10 A. Exhibit C is an excerpt from the *New Mexico*
11 *Register*, was printed out from the electronic version of
12 the *New Mexico Register* on the Internet.

13 Q. And does this meet the requirements as required
14 by Rule?

15 A. It does. You will note that the caption at the
16 top reflects that this is the *Register* for August 31, 2005.
17 It contains a notice of this hearing on September 15, 2005.
18 Ten days under New Mexico law is 14 days, 14 days from
19 October -- from August 31st, would be September the 13th,
20 so it does reflect compliance with the requirement.

21 MS. O'CONNOR: I would request that Exhibit C be
22 admitted into evidence.

23 CHAIRMAN FESMIRE: Any objection?

24 COMMISSIONER BAILEY: No.

25 COMMISSIONER CHAVEZ: No objection.

1 CHAIRMAN FESMIRE: Exhibit C is so admitted.

2 Q. (By Ms. O'Connor) Now, Mr. Brooks, was any
3 copies of the proposed Rule provided to any other entities?

4 A. Yes, I sent a copy to the general counsel at the
5 Economic Development Department to comply with the
6 requirement for notice to the Small Business Advisory
7 Council. I also sent a copy to the IT -- I don't know, I
8 can't remember for sure what that stands for -- office
9 within this Division, within this Department, to have it
10 posted on the Departments' website -- on the Division's
11 website.

12 Q. And was it so posted on the Division's website?

13 A. It was.

14 Q. And so is it your personal knowledge that it was
15 sent to the Small Business --

16 A. It was --

17 Q. -- agency?

18 A. -- yes.

19 Q. Okay. I would refer you now back to what's now
20 been admitted as Exhibit A-1.

21 A. Yes, ma'am.

22 Q. You said you'd been involved in the drafting of
23 proposed Rule 36; is that correct?

24 A. Yes.

25 Q. Okay. And could you explain to the Commission

1 what your involvement was in the drafting of that Rule?

2 A. Okay, rulemaking has changed around here. We're
3 now on a fast track. But this is the ultimate slow-track
4 Rule. The proposal for -- that eventually resulted in this
5 Rule was initiated by the former OCD Director, Lori
6 Wrotenbery, and the former Division counsel, Lyn Hebert,
7 sometime prior to my coming to the agency in 2001.

8 There was a work group constituted and they made
9 a report, and some people didn't like the report. I had
10 some objections to it, so did some other people. And
11 Director Wrotenbery directed me to reformulate it, and a
12 new work group was constituted over which I presided. Had
13 a number of meetings over a period of about three years,
14 and finally resulted in the proposal of Exhibit A-1, of
15 which I was the primary draftsman, with the concurrence and
16 assistance of the members of the work group.

17 Q. And who all were members of that work group?

18 A. I have a list here, if I can find it. Myself;
19 William F. Carr, with the law firm of Holland and Hart in
20 Santa Fe; James Bruce, attorney in Santa Fe; Jeff Harvard
21 of the Independent Petroleum Association of New Mexico;
22 Kevin Harwe of Devon Energy; Steven Smith, who was of EOG
23 Resources at the time we started this procedure but is now
24 with Mewbourne; Bob Doty with OXY USA; Randy Patterson of
25 Yates Petroleum; Alan Alexander of Burlington Resources;

1 and with some involvement -- although he wasn't a formal
2 member of the work group, he actually, I think, may have
3 attended more meetings than some of the people that were,
4 Rick Foppiano of OXY.

5 Q. Now, for the proposed Rule, was it a unanimous
6 agreement of the Committee as to the proposed Rule?

7 A. I believe that it eventually was. There was a
8 lot of discussion about many issues, and some people gave
9 on various things, but I believe that that is correct. My
10 understanding was that a unanimous consensus was reached.

11 Q. Okay. Now, when the committee was developing the
12 Rule, were there any opportunities for public input in the
13 development of the Rule?

14 A. Well, after the Rule was developed we conducted a
15 public workshop. That was held in June of this year. We
16 gave notice to the same persons that were noticed for the
17 -- in addition to posting notice on the website, which we
18 did, we also gave mail notice to -- or e-mail notice to
19 those persons who were summoned for the work group -- for
20 the workshop on proposed amendments to Rule 104 that were
21 recently adopted, included representatives of industry
22 associations and also representatives of several
23 environmental groups. The Sierra Club, I know, was one,
24 the New Mexico Citizens for Clean Air and Water, the Oil
25 and Gas Accountability Project. I don't remember if there

1 were any others. I do remember those three.

2 Also we gave notice to the Jicarilla Apache Tribe
3 and the Navajo Nation and the Bureau of Land Management and
4 the State Land Office.

5 Q. Okay. And as the result of the public workshop,
6 were there any changes made to the Rule as originally
7 proposed?

8 A. There were a few. Most of them were very minor.
9 The one I specifically remember was the last sentence of
10 Subsection D, regarding -- no, it's not in Subsection D,
11 I'm sorry, it's in Subsection E, the provisions of
12 Subsection E regarding refund of money advanced with
13 interest were added in response to comments at the
14 workshop.

15 Q. Mr. Brooks, before we go into details of the
16 Rule, could you explain to the committee, just give them a
17 general overview as to what this Rule -- why this Rule is
18 being proposed?

19 A. Okay, there has been long controversy within and
20 outside of OCD about whether compulsory pooling orders in
21 New Mexico are well-specific or pool-specific -- or, not
22 pool-specific, unit-specific. Some people believe that the
23 compulsory pooling order pools the unit only for the
24 purpose of the particular well described in the order.

25 Lori Wrotenbery and I both disagreed with that,

1 but we did recognize that -- I mean, we felt that once it's
2 unitized, because of the terms of the Statute and the terms
3 of the customary order, the -- it was unitized for all --
4 it was pooled for all purposes, for all operations on that
5 unit. However, we did recognize that -- only that the well
6 election and cost-recovery provisions, which are probably
7 the most important part of a compulsory pooling order, as
8 our orders have always been written, are well-specific;
9 they apply only to the first well.

10 If the operator wanted to conduct any other
11 operations on the unit, then the operator would have to do
12 one of two things. He would have to either conduct them
13 under the common law, which would provide him only with
14 100-percent cost-recovery, or he would have to come back to
15 the Division and get an amendment to that order to
16 authorize additional operations.

17 When -- This, I think, was triggered by the
18 amendments in about 1998 -- I say "I think" because I
19 wasn't here then -- but in about 1998 the amendments to
20 Rule 104 that permitted infill wells in deep gas units in
21 the southeast.

22 Of course, subsequently there were amendments to
23 the pool rules for some of the large pools in the northwest
24 which also permitted infill wells, and we had gotten to a
25 situation where most pools -- in most pools, more than one

1 well per spacing unit was permitted. And there existed a
2 belief that it would subserve efficiency to revise our
3 compulsory pooling orders so as to allow the drilling of an
4 infill well on the unit under the same terms as the well
5 that was specifically proposed at the time the pooling
6 order was issued.

7 The original work group geared its efforts toward
8 getting standard language to be put into an order for that
9 purpose. We decided in my work group to change our focus
10 to doing the Rule for the primary reason that there are
11 many of these compulsory pooling orders out there that have
12 already been entered in -- as to units that permit infill
13 wells, and if we adopted an order -- if we adopted language
14 to be put in future orders, it would still be necessary to
15 amend all those other orders, which would require a
16 specific proceeding for each.

17 So it was decided that it could be -- and the
18 work group consensus was, that it could be most efficiently
19 done by a rule change. And the purpose of this Rule is
20 just that, to provide a framework whereby an operator of a
21 compulsory pooled unit can drill an infill well within that
22 unit under the terms of the compulsory pooling order,
23 without the necessity of another application and hearing
24 before the Division to get an amendment to that order.

25 Q. I would refer you to Exhibit A-2. Now, is it

1 correct that this is the Rule as you are proposing it -- as
2 the OCD is proposing it, to the Commission at this time?

3 A. That is correct.

4 Q. Okay. Would you please go through the Rule and
5 explain to the Commission the Rule and the requirements of
6 the Rule?

7 A. Okay. I'm going to start with Rule 36, and I'll
8 go back and conclude with the change of definition that is
9 actually the first item on the Rule.

10 There are some definitions in -- Subsection A
11 includes some definitions. These are being defined solely
12 for the purpose of this Rule and therefore are in the Rule
13 itself, rather than in the definitions Rule.

14 The -- (1) and (3), A.(1) and A.(3), are merely
15 defined for purposes of reference within this Rule, and I
16 do not anticipate -- I do not see any particular
17 substantive significance to the way those definitions are
18 worded, so I won't say any more about them unless there are
19 questions.

20 A.(2) does require some comment. A.(2) says
21 "Infill well shall mean a well in a compulsory pooled unit
22 to be completed in a pool in which an existing well drilled
23 pursuant to the compulsory pooling order has been completed
24 and not abandoned."

25 There are many elements to that definition, but

1 basically what we were doing here was writing around an
2 inherent problem which the work group did not arrive at a
3 consensus as to how to deal with, and that is what I would
4 call the behind-the-pipe issue, in addition to the infill
5 issue, which arises when a well is drilled in a compulsory
6 pooled unit and you want to drill an infill well under the
7 Rules to the same pool. There arises an issue from the
8 multiple-pool nature of most of our compulsory pooling
9 orders.

10 Most of our compulsory pooling orders use what
11 has generally been -- what has often been called the
12 wedding cake approach, where it defines a 320-acre unit for
13 all pools spaced on 320 acres within the horizontal limits,
14 a 160-acre unit for all pools spaced on 160 acres within
15 the horizontal limits, and so on down to the 40-acre oil
16 units.

17 That raises the question, does the operator -- on
18 what terms does the operator of the well -- does the
19 operator of the pooled unit have the right, having once
20 completed the pooled unit in the target formation provided
21 in the order, to plug that well back to a shallower pool or
22 to drill another well on the unit to a shallower pool?

23 The committee did not reach a consensus on that
24 issue and recommended that the Rule leave that issue for
25 another day. As Jane Prouty said one meeting recently on

1 another issue, that we bumble along the way we always have.

2 (Laughter)

3 THE WITNESS: So the infill well definition was
4 carefully written to not treat that issue. Of course you
5 also notice that it says, "in which...a well drilled
6 pursuant to the compulsory pooling order has been completed
7 and not abandoned." If the well drilled pursuant to the
8 compulsory pooling order is abandoned prior to the time
9 that another well is drilled, then under the terms of our
10 typical order, that terminates the unit. So that if
11 somebody comes in later and wants to drill another well,
12 they would have to apply for a new compulsory pooling
13 order.

14 I believe I can take -- as I did in the previous
15 Rule, I will either be happy to answer questions on --
16 subsection by subsection, or go through the whole Rule and
17 then answer questions generally, whichever suits the
18 Commission's pleasure.

19 COMMISSIONER BAILEY: I have questions before we
20 leave the area.

21 THE WITNESS: Okay.

22 COMMISSIONER BAILEY: Okay, since the general
23 public is so involved in the rulemaking now and the terms
24 "compulsory pooling" and "statutory unitization" may seem
25 very close to each other, I have a suggestion that maybe we

1 should have absolute clarity over what we're talking about
2 here, like in A-1, Operator shall mean the division-
3 appointed operator of a compulsory pooled proration or
4 spacing unit, or its successor. So that there's no
5 confusion that we're talking about a larger exploratory or
6 waterflood-type unit.

7 THE WITNESS: That was certainly the intent.
8 There was no --

9 COMMISSIONER BAILEY: The intent, but for people
10 who are not familiar with this type of terminology I think
11 clarity is really important in this Rule. Would you object
12 to having --

13 THE WITNESS: Okay, that's what I was trying --

14 COMMISSIONER BAILEY: -- spacing unit --

15 THE WITNESS: -- to say, was what you were asking
16 me. No, I would not object.

17 COMMISSIONER BAILEY: Okay, I'd like to see it
18 there. Also in A.(2), Infill well shall mean a well in a
19 compulsory pooled proration or spacing unit.

20 And then you just talked about whether in A.(2)
21 the order has been completed and not abandoned. Do we need
22 to be specific as to temporarily or permanently abandoned?
23 Because there are going to be very specific rules on
24 temporary abandonment.

25 THE WITNESS: That is correct. I think actually

1 they are, but they're going to be expanded. That would not
2 -- I would not object to saying plugged and abandoned --

3 COMMISSIONER BAILEY: Okay.

4 MS. O'CONNOR: Does the Commission want to rule
5 on these proposals as we go along, rather than to save
6 them, or how would the Commission like to handle it?

7 CHAIRMAN FESMIRE: I'd rather discuss them, and
8 then I'll mark them and we'll vote on them as we -- when we
9 get to the end.

10 COMMISSIONER BAILEY: That's all I have so far.

11 THE WITNESS: Okay. Are there any other
12 questions?

13 COMMISSIONER CHAVEZ: On that particular Section
14 A.(1) there, "division-appointed operator", is that --
15 could that also include "commission-appointed", should the
16 order come from the Commission hearing?

17 THE WITNESS: I would think that would be
18 implied.

19 COMMISSIONER CHAVEZ: Be implied?

20 THE WITNESS: I think -- There again, I wouldn't
21 object to clarifying if the Commissioners feel there's a
22 need to clarify.

23 COMMISSIONER CHAVEZ: Did any of the operators
24 ever bring that up as an issue?

25 THE WITNESS: No, no one has articulated that

1 prior to you.

2 COMMISSIONER CHAVEZ: Okay, thanks.

3 CHAIRMAN FESMIRE: Go ahead and continue, Mr.
4 Brooks.

5 THE WITNESS: Okay, I will go on to Subsection B
6 then. Subsection B is a general statement of what the Rule
7 is intended to do, which is to allow proposals for infill
8 wells within a compulsory pooled unit.

9 Now, the important thing, I think, about
10 Subsection B is who it allows to propose. We began this
11 inquiry with stating that in a typical compulsory pooled
12 unit there might be -- there would always be at least two
13 different categories of working interest owners, but there
14 might be as many as three, because in many compulsory
15 pooled units there's, one, the operator.

16 And two, there are any people who voluntarily
17 joined in the well. We usually call them -- we called them
18 throughout the discussion the JOA parties, although we
19 recognize that somebody might voluntarily participate
20 without signing a joint operating agreement. But in most
21 cases they would be parties to a joint operating agreement.
22 So we have the JOA nonoperators.

23 And then we have the pooled parties, the pooled
24 working interest owners.

25 There was a lot of debate about this issue, but

1 the decision that was eventually reached was that the Rules
2 should not provide an option for proposals by the JOA
3 nonoperators. The reasons for that were that it was felt
4 that the JOA nonoperators were not parties to the pooling
5 proceeding.

6 For legal and constitutional reasons that I will
7 mention later in the discussion, I believed -- and I think
8 it was generally concurred for fairness issues as well --
9 that the JOA parties should not be made subject to an
10 election on the proposal of a pooled party, a mandatory
11 election on the proposal for a pooled party, basically
12 because the Rules do not provide for notice of a compulsory
13 proceeding to the voluntary joining nonoperators.

14 It was therefore concluded that if the non- --
15 Well, the other reason why it was concluded not -- why we
16 concluded not to give them a right of proposal under this
17 Rule was that we figured that if the JOA nonoperators
18 wanted to institute a drill- -- wanted to initiate a
19 drilling proposal, their remedy would be to propose it to
20 the operator under the terms of the operating agreement.

21 If the operator consented, then it would be the
22 operator's responsibility to put the deal together, which
23 would entail proposing it to the pooled parties. If the
24 operator did not consent, then presumably the JOA parties,
25 their designee rather than the operator, would be drilling

1 the well, and since that would be conduct of operations by
2 a person other than the Division-appointed operator, they
3 would have to come back to the Division anyway to get
4 authority to do that, by amendment to the pooling order.

5 So for that reason we felt like that the JOA
6 parties were not being denied their opportunity to propose
7 it, they just did it under the terms of the joint operating
8 agreement, rather than under the terms of the Rule.

9 Now, this says the operator or -- Subsection B
10 says the operator or a pooled party may propose. And
11 Subsection C deals with proposals by the operator, and
12 Subsection D deals with proposals by a pooled party. The
13 Rules are very different in terms of what they can actually
14 do, although the mechanics are similar. So unless there
15 are questions on the issue of Subsection B, I will proceed
16 then to Subsections C and D.

17 CHAIRMAN FESMIRE: Any questions?

18 COMMISSIONER BAILEY: No.

19 COMMISSIONER CHAVEZ: No.

20 THE WITNESS: Okay, Subsection C provides for
21 proposals by the operator. It is very similar -- it is
22 structured to be very similar to the joint operating
23 agreement in that it provides that the operator will make a
24 proposal. The pooled parties -- the operator is required
25 to propose only to the pooled parties.

1 Now, it would be assumed, of course, that the
2 operator would have a contractual duty to propose the well
3 to the parties to the joint operating agreement, so the
4 Rule doesn't require that. That would be covered by the
5 agreement, presumably.

6 The operator must propose a well to the pooled
7 parties. They have a 30-day period of time to elect to
8 participate or not, just as they would under the terms of
9 either the compulsory pooling order or a joint operating
10 agreement.

11 The distinct feature of this -- of the mechanics
12 of this Rule -- well, actually there are two, but start
13 with the fact of payment. And this is sort of an in-
14 between proceeding.

15 Under joint operating agreement, as you know, the
16 operator has the option of requiring payment in advance of
17 a share of well costs, however the -- whether the payment
18 is separate from the election. So that my understanding of
19 a joint operating agreement has always been that a party
20 elects by notice to participate. And if the party elects
21 by notice to participate and then doesn't pay their share
22 when the operator demands it, then that just creates a
23 contractual liability on which the operator can sue, but it
24 does not affect the validity of the election.

25 On the other hand, under the typical compulsory

1 pooling order the only way you can elect to participate is
2 by paying your share of the costs in advance, because the
3 terms of the order require that. This creates an
4 intermediate procedure that you elect by notice, just as
5 you would under a joint operating agreement, but you must
6 pay your share within 30 days or your notice is voided.

7 The reasons for that were, the committee felt
8 that the compulsory pooling proceeding was right in dealing
9 with parties that didn't have a contractual relationship
10 with each other; because they're forced into this
11 relationship, they haven't made -- they don't have the
12 opportunity to make an assessment of other people's
13 creditworthiness to decide whether or not they want to get
14 into this relationship with them, so it was felt that they
15 should not be allowed to elect to participate and then not
16 put up their money.

17 On the other hand, they didn't want to require
18 the -- this is a strange observation to my way of thinking,
19 but it was the representatives of the majors, didn't want
20 to require the payment within the 30-day election period
21 because they said their companies sometimes couldn't move
22 that fast in terms of getting a check, actually getting a
23 check. So that was the reason that was given in the work
24 group why they had the 60 -- the additional 30 days to make
25 payment.

1 The other difference is with regard to the time
2 for commencement of the well. The joint operating
3 agreement, unless it's modified -- and it sometimes is, but
4 the typical joint operating agreement requires that the
5 well must be started within 90 days, and then there's an
6 additional 30 days for hardship.

7 It was decided here we would give them 120 days
8 up front, and -- rather than try to deal with what is a
9 hardship. But then it was raised that in the present
10 environment particularly -- and this was something that
11 came up in some of the recent meetings, that sometimes you
12 can't even get a rig within 120 days. So the provision was
13 added to allow a party to petition to the Division for an
14 additional 120 days to start the well, and the Division
15 could do without notice or hearing.

16 That's analogous to the way we do things under
17 compulsory pooling orders, because our compulsory pooling
18 orders typically provide basically a 120-day --
19 approximately a 120-day time to start the initial well, and
20 then the Division is allowed to extend it without notice
21 and hearing. The difference being that under the typical
22 compulsory pooling order the Division can extend any number
23 of times it wants to without notice and hearing; under this
24 provision, based on what the operators thought -- way it
25 ought to be, that the Division can extend the 120 days one

1 time without notice and hearing, but if they wanted
2 additional extensions they would have to have notice and
3 hearing.

4 I think -- as a lawyer, I think it's a little
5 unusual that we have procedures for the Division to do
6 things without notice and hearing, however we've been doing
7 it for many, many years in terms of extending compulsory
8 pooling orders, so there's plenty of precedent for it.
9 Otherwise, I believe that the elections work in a way that
10 is very familiar to the industry and not likely to cause
11 any particular problems.

12 If there are any questions on operator proposals,
13 I'll entertain them. Otherwise, I'll move on to Subsection
14 D.

15 COMMISSIONER CHAVEZ: Just one on the -- I'm
16 sorry.

17 CHAIRMAN FESMIRE: Commissioner?

18 COMMISSIONER CHAVEZ: Yes, Mr. Brooks, if the
19 pooled order, the compulsory pooling order, comes out of
20 the Commission, would the extension still be -- the
21 Division Director could extend the time under the
22 Commission --

23 THE WITNESS: I think it should be, because --
24 and I think that's the way this reads, because Commission
25 orders are only dealt with impliedly, but I think that

1 should be the case because the Commission acting on things
2 is much more unworkable than the Director.

3 COMMISSIONER CHAVEZ: Okay. when it says
4 Division, that implies the Division Director?

5 THE WITNESS: Yeah, it has been our -- I would
6 have no objection to substituting "Director" in this
7 context. It's generally been our philosophy in rulemaking
8 to say "Division" instead of "Division Director", but then
9 that is generally -- that is in a generic sense. If
10 there's something that specifically needs to be done by the
11 Director -- and this probably does -- then it's appropriate
12 to say Director.

13 COMMISSIONER CHAVEZ: Okay. And then extension,
14 say if an operator wants more than one extension, which
15 goes to -- would require notice of hearing, that would be
16 an Examiner hearing, not a Commission hearing, even if the
17 order, the original order, came out of the Commission?

18 THE WITNESS: It would be. This does not provide
19 for it specifically at all in the Rule, but then you'd go
20 back to the general procedural rules, which are, you file
21 an application and it goes to an Examiner.

22 COMMISSIONER CHAVEZ: Okay, that's all I have.

23 CHAIRMAN FESMIRE: Commissioner Bailey?

24 COMMISSIONER BAILEY: No questions.

25 CHAIRMAN FESMIRE: I have no questions on this.

1 THE WITNESS: Okay. D deals with proposals by
2 pooled parties, and the consensus that we came to is a
3 little bit odd in that it provides for proposals by pooled
4 parties, but it doesn't really give them a right to force
5 an election. What they have the right to do is to propose
6 the infill well to the operator. Then the operator can
7 decide whether it wants to propose the well as an operator
8 proposal or whether it wants to decline to propose it.

9 If the operator decides to propose the well as an
10 operator proposal, then the rest of the procedure goes
11 under Subsection C. If the operator decides not to propose
12 it as an operator proposal, then the Rule provides that the
13 proposing party may apply to the Division for an amendment
14 of the pooling order to authorize the drilling of the well.

15 There was a lot of discussion of this issue,
16 again, and our original proposal had been to require an
17 operator -- to allow a pooled party to -- or -- through
18 several drafts, we worked on trying to develop a procedure
19 to allow a pooled party to propose an infill well and force
20 an election without the involvement of the Division. The
21 stumbling block that we couldn't get over on that was the
22 presence in many force pooled units of voluntarily joining
23 parties who were not noticed or given an opportunity to
24 participate in the original compulsory pooling proceeding.

25 It would seem that there are fairness and perhaps

1 even Constitutional due-process -- likely even,
2 Constitutional due-process arguments to placing a JOA
3 nonoperator in the position where it has to make an
4 election on the basis of a proposal by a pooled party,
5 which will have the consequence of either requiring it to
6 participate, which requires it to put up money, or putting
7 it in a nonconsent position, which I think in the market
8 certainly an interest in a potential prospect that's not
9 subject to a mandatory election is worth a lot more than
10 one that is.

11 And I think that there is a property interest
12 there by the JOA nonoperators. They're not participants in
13 the original compulsory pooling order, so it would seem
14 that they're entitled to some notice and hearing before
15 they're placed in that position. And I think there was a
16 feeling among the participants that fairness sort of
17 indicated the same thing.

18 In this scenario, the pooled party proposes to
19 the operator, the operator is given 60 days in which to
20 decide whether it wants to propose, the idea there being
21 that that would give the operator time to propose the well
22 to its JOA partners and find out whether their elections --
23 what their elections are, so it can know what its own
24 position is going to be before it has to decide whether to
25 go along with the proposal or whether to oppose it.

1 The only other thing I think is worthy of comment
2 is that there is a provision in here which, if the operator
3 proposes -- if the operator does elect to propose it and
4 there's one pooled party who has proposed it and therefore
5 is in the deal, but there are other pooled parties who are
6 out of it, and the operator wants to join -- wants to
7 abandon the proposal after having made it because of the
8 elections not to participate by the other pooled parties,
9 then the pooled party who proposed it can keep the proposal
10 alive by electing to take up the interest of the nonjoining
11 or nonconsenting pooled parties.

12 I think that's as -- When we got away from the
13 mandatory election, I think that ends up not probably being
14 a real important provision. It was a very vital issue when
15 we were talking about allowing a pooled party a mandatory
16 proposal -- a proposal that would result in a mandatory
17 election by the operator. But at this point it's probably
18 not all that important. However, it seems that --
19 reasonable to me that if the pooled party is going to
20 propose the well and say, I want the operator to propose
21 it, he should be willing to cover the nonconsents of the
22 other pooled parties if that's necessary to make the deal
23 work.

24 That's all I have to say about C and D.

25 COMMISSIONER BAILEY: The third line from the

1 bottom of paragraph D --

2 THE WITNESS: Yes, ma'am.

3 COMMISSIONER BAILEY: -- that begins with
4 "including those whose interests in the..." Would you
5 object to putting in "proration or spacing"?

6 THE WITNESS: No. No problem.

7 COMMISSIONER BAILEY: Okay.

8 THE WITNESS: Your question reminds me of
9 something I should have commented on that I did not.

10 That last sentence serves a specific purpose.
11 That is dealing with the situation where the operator
12 refuses to accept a -- or refuses to advance a proposal
13 that a pooled party has made. The pooled party then
14 applies to the Division. Because that involves all
15 interests -- because all interests in the unit will be
16 involved in that situation, the pooled party must give
17 notice to all owners and not merely to the people who are
18 force pooled, including the voluntarily joining parties,
19 because they were not notified of the original pooling
20 proceeding.

21 Any other questions?

22 COMMISSIONER BAILEY: No.

23 COMMISSIONER CHAVEZ: Yes, where the operator
24 wants an extension after the 120 days that it received
25 notice, you say that the Division may extend the time for

1 commencement of drilling. That would be, in a sense, the
2 operator submitting a letter to the Director saying, I need
3 an extension of the 120 days provided by this Rule in order
4 to commence drilling of the well. Something along those
5 lines?

6 THE WITNESS: That was the idea. That's the way
7 it's always been -- or that's the way it has been done
8 since I've been familiar with it under the present
9 compulsory pooling orders.

10 COMMISSIONER CHAVEZ: And the Division's
11 extension, would that be considered an order, as part of
12 the original compulsory pooling order, an amendment to it
13 like an A, B, or C, or is it -- and this purpose, would you
14 still be having a letter from the Director, just a
15 letter --

16 THE WITNESS: My assumption was, and I think
17 everybody else on the work group believed, that it would
18 operate just like it does under the compulsory pooling
19 order, and it would just be an informal letter from the
20 Director. The Rule does not address that.

21 COMMISSIONER CHAVEZ: On the very first line
22 after it says D, it says "Proposal by pooled owner."
23 Elsewhere the phrase "pooled working interest owner" is
24 used. Do you object if that was expanded to say "Proposal
25 by pooled working interest owner"?

1 THE WITNESS: No, I think that's a good idea.

2 COMMISSIONER CHAVEZ: Now, is it possible -- and
3 maybe I missed your testimony here -- that a proportion of
4 the pooled working interest owners may elect to participate
5 and some may not, who otherwise didn't want to participate
6 in the original well?

7 THE WITNESS: That is correct.

8 COMMISSIONER CHAVEZ: Well, never mind, I think
9 I've answered it. Thank you.

10 THE WITNESS: My understanding is, if there's any
11 doubt about it, this is a proposal of a new well, and
12 regardless of the election a person has made on the initial
13 well, they get the right to make a separate election on the
14 infill well.

15 COMMISSIONER CHAVEZ: Thank you.

16 CHAIRMAN FESMIRE: I have no questions, Mr.
17 Brooks.

18 THE WITNESS: Very good, then I will go on to E.
19 Subsection E is the refund of money provision,
20 and this was proposed by some of the operators at the work
21 group. I don't -- at the workshop; the workshop was the
22 meeting we had in June.

23 Now, I mentioned who was given -- who we gave
24 notice to at the workshop. I don't believe I said who
25 appeared. The only person that appeared, other than -- We

1 had a number of representatives of operators who were not
2 represented in the work group, that appeared at the
3 workshop. We did not have any parties other than
4 representatives of operators appear, except for
5 representatives of the State Land Office. There were no
6 other -- the environmental community and the tribes and BLM
7 and, I believe also, the cattle growers association was
8 noticed. None of those people sent a representative.

9 Okay. The E portion, Subsection E was proposed
10 and debated at the workshop. This provision with the rate
11 that was put in it was evolved at that -- by that -- by the
12 workshop. I won't say everybody agreed to it, but it
13 seemed to be generally acceptable. It is a departure from
14 anything that is in either the joint operating agreement or
15 -- the AAPL joint operating agreement or the compulsory
16 pooling orders that we've been issuing. So there's really
17 not any direct precedent for that type of provision, but it
18 seemed to be acceptable to -- desired by some and
19 acceptable to pretty much everybody.

20 F. is something that is added in the A-2 version
21 versus the A-1 version. So before I go into F., I will go
22 back through the other things that are changed in the A-2
23 version from the A-1 version. There may be a little bit of
24 difficulty in following this because we do not have color-
25 printed copies, in which case -- where these would show up

1 in red. So they're just in slightly less bold type.

2 The first change is in the first line of
3 Subsection B. The words "are authorized, pursuant to" we
4 propose to delete. This is an editorial correction.

5 The second change is in the fifth line from the
6 bottom of page 1 in Subsection C, "share of well costs",
7 and after "costs" we propose to add "as defined in
8 19.15.1.35 NMAC". The reason for that addition is that the
9 definition of well costs which the Commission adopted when
10 it adopted Rule 35 is specifically applicable only to that
11 Rule. Therefore if we're to make the same definition
12 applicable to this Rule, we need to cross-reference it.

13 The next change I'm having trouble finding here.
14 I remember what it is, but I -- oh, in Subsection D, eighth
15 line in Subsection D -- the line begins with "county" -- as
16 proposed in Exhibit A-1 it says "county where the proposed
17 well will is be located". We propose to change that to
18 "will be located". No, wait, it says "will is located",
19 and we propose to change "will is located" to "will be
20 located". That again is an editorial correction.

21 The only change of a substantive nature is
22 Subsection F. Subsection F in its entirety is a new
23 proposal. That is, it was not discussed in the work group,
24 and it was not included in the Rule as originally proposed.

25 The reason for Subsection F is to incorporate the

1 determination of reasonable well costs -- the procedure for
2 determining reasonable well costs as it is set out in the
3 compulsory pooling order, and it always is -- into this
4 structure so that the eventual cost that will be borne by
5 the pooled parties will be their share of reasonable well
6 costs, if those should be different from actual well costs.

7 This was not included in the original Rule,
8 frankly, because I didn't think about it and nobody else in
9 the work group did. But when I got to reviewing this Rule
10 it occurred to me that the Statute, Compulsory Pooling
11 Statute, Section 70-2-17, has a mandatory requirement that
12 OCD establish a procedure for determining reasonable well
13 costs in a compulsory pooling order. And it seems to me
14 that one of two results would occur from not having a
15 provision like F in here.

16 The most probable one would be that a court would
17 hold, if the issue were presented, that the procedure
18 prescribed in the original compulsory pooling order would
19 apply even though it wasn't specifically made applicable.
20 But if they didn't so hold, then it would seem to be
21 probable that the entire Rule would be invalid because it
22 violates the Statute. So I thought that it was a wise
23 precaution to put that provision in here.

24 The only other thing to comment on is what I left
25 for last, changing the definition of "working interest

1 owner".

2 When we got to crafting this Rule, we used the
3 term "working interest owners" in a lot of contexts, and we
4 got to thinking about the problem of, does "working
5 interest owner" include an unleased mineral owner? And so
6 we looked to see what the current definition of "working
7 interest owner" was.

8 And we found that the current definition of
9 "working interest owner" does not include an unleased
10 mineral interest owner. And my feeling is that it should,
11 not just for this rule but for all purposes, subject to the
12 qualification about the royalty that's allowed -- the one-
13 eighth royalty that's allowed in the compulsory pooling
14 context to an unleased mineral interest owner. In all
15 other contexts I believe that an unleased mineral interest
16 owner is, in effect, a working interest owner. And the
17 definitional change that I propose would make that the case
18 for all purposes in the OCD Rules, subject to the
19 qualification about the compulsory pooled working interest
20 owner -- unleased owner's royalty.

21 Q. (By Ms. O'Connor) And Mr. Brooks, your
22 definitional change is in what Rule?

23 A. Rule 7, Subsection W, paragraph (9).

24 CHAIRMAN FESMIRE: Okay.

25 THE WITNESS: That concludes my testimony --

1 well, my -- that concludes my answer to the question you
2 asked me quite a while back.

3 COMMISSIONER BAILEY: I have a question, though.
4 In this definition for working interest owners --

5 THE WITNESS: Yes.

6 COMMISSIONER BAILEY: -- if the Land Office has
7 an unleased tract within a compulsorily pooled --

8 THE WITNESS: -- unit.

9 COMMISSIONER BAILEY: -- proration unit, does
10 this definition put the Land Office as a working interest
11 owner? That can't happen.

12 THE WITNESS: Well, I know that it's not
13 authorized to be, but it seems to me it in effect is a
14 working interest owner by virtue of its ownership, unless
15 and until it leases. I assume what would happen if you got
16 in that situation is that you would lease it.

17 But I don't see, you know, how we escape from the
18 fact that -- I guess the Land Office could appear at the
19 compulsory pooling hearing and point that out, and maybe
20 that would be ground for denying the compulsory pooling
21 order.

22 COMMISSIONER BAILEY: Admittedly, this is way out
23 there. But it's a potential -- I guess I'm curious if this
24 unleased interest has to apply to governmental agencies
25 such as the BLM or the Land Office or the Jicarilla

1 Apaches, or any governmental owner of unleased interests.

2 THE WITNESS: Well, the Rule could be made to
3 exclude that. I'm not sure what consequences that would
4 have in context, other than our Rules, nor am I totally
5 sure how it would work under our Rules. If the Land Office
6 had an unleased interest and there were an application to
7 pool that unit, I don't know what the consequences would be
8 exactly. I don't know that it's ever --

9 COMMISSIONER BAILEY: I don't know that it's ever
10 come up --

11 THE WITNESS: I've never heard of it coming up.

12 COMMISSIONER BAILEY: -- but I just hate blanket
13 things that automatically include governmental agencies
14 without --

15 THE WITNESS: Well, we could say except
16 governmental agencies.

17 CHAIRMAN FESMIRE: Add another sentence, the
18 working interest --

19 THE WITNESS: Or perhaps we may want to say
20 "except the State Land Office and the Bureau of Land
21 Management". I would assume that if a State agency owned
22 land and had a mineral interest in that land and it was not
23 trust land, that the State agency would have the right to
24 become a working interest owner if it chose to do so.

25 COMMISSIONER BAILEY: But that entails some

1 obligations that the agency may not be prepared to accept.

2 Q. (By Ms. O'Connor) Would the agency -- Mr.
3 Brooks, would the agency be able -- those governmental
4 agencies be able to move quickly enough to respond to the
5 time limits?

6 A. I don't know the answer to that. I think the
7 concern is that there would be obligations, and I don't
8 know -- I don't believe the compulsory pooling scenario
9 imposes any, and perhaps that's the reason it doesn't.
10 Except that it would be subject to the election. That is,
11 if they elected not to participate, which would essentially
12 be the only election they could make, then their interest
13 would be -- then the operator would have the right to
14 recover costs out of their interest.

15 COMMISSIONER BAILEY: But as a royalty owner they
16 can't be compromised for their royalties.

17 THE WITNESS: And the royalty would be one-eighth
18 by statute. You know, I -- that's provided in the Oil and
19 Gas Act, that any unleased mineral interest owner gets the
20 one-eighth royalty.

21 COMMISSIONER BAILEY: Right. No, I understand
22 that. But I know State Parks has oil and gas leases.
23 Highway Department, I believe, does.

24 THE WITNESS: Well, I think this is a decision
25 the Commission will have to make on such wisdom as it has.

1 I don't really have any advice to offer on it, because it
2 seems to me that as a matter of common law the governmental
3 agency is going to be placed in that position unless their
4 position is changed by some other statute, which I'm not
5 aware of any, really.

6 I know that they're prohibited from becoming
7 working interest owners in the usual sense, but it seems to
8 me that by -- the ownership of an unleased mineral interest
9 has the incidence that it has under the common law and that
10 they're put in that position not by the OCD but by the fact
11 -- the nature of their tenure. How we deal with it in our
12 regulations, I don't really have any wisdom to offer the
13 Commission at this point on that subject.

14 CHAIRMAN FESMIRE: Well, they would become a one-
15 eighth royalty -- in essence, a one-eighth royalty interest
16 owner until the 200-percent payback --

17 THE WITNESS: That's correct.

18 CHAIRMAN FESMIRE: -- at which point they become
19 a working interest owner, and --

20 THE WITNESS: That's correct.

21 CHAIRMAN FESMIRE: -- you guys can't --

22 COMMISSIONER BAILEY: Yeah.

23 CHAIRMAN FESMIRE: -- be working interest owners.

24 COMMISSIONER BAILEY: And we can't have any
25 withholding of our royalty under the 200 percent.

1 THE WITNESS: Well, there would be no withholding
2 of the royalty under the --

3 CHAIRMAN FESMIRE: You'll still --

4 THE WITNESS: -- Oil and Gas --

5 CHAIRMAN FESMIRE: -- a one-eighth royalty owner.

6 COMMISSIONER BAILEY: But we can't be a working
7 interest.

8 CHAIRMAN FESMIRE: You'd have 200 percent payout
9 to find somebody who was interested in leasing the
10 property.

11 COMMISSIONER BAILEY: And I don't think State
12 Parks would be able to assume the responsibilities either.

13 THE WITNESS: Well, I think under the Oil and Gas
14 Act the responsibility is purely passive, because what in
15 effect you have, since you wouldn't be able to elect to
16 participate, as Mark says, you would -- your interest would
17 be withheld until the 200-percent payout, and at that
18 point, then, you would receive your working interest share
19 of the revenues. But the compulsory pooling order
20 authorizes the operator to withhold costs out of revenues.
21 It does not require the pooled party to pay revenues -- to
22 pay costs if they exceed revenues. So it would be a purely
23 passive role as a working interest.

24 CHAIRMAN FESMIRE: But they're still a passive
25 working interest owner because their share of the proceeds

1 is being docked for the share of the operating cost after
2 the payout, and they can't by statute do that.

3 THE WITNESS: Well, you know, like I say, having
4 never thought about this problem, I don't know how one
5 deals with the tension between the Statute, the common law
6 and the Oil and Gas Act. So I just don't have any wisdom
7 to offer the Commission at this point.

8 CHAIRMAN FESMIRE: Could we add another section,
9 say, C.(1), or in between C and D? But how would you --
10 even if we did have a special section, how could we deal
11 with it?

12 COMMISSIONER BAILEY: Yeah, I'm thinking it
13 should just go to the definitions by just exempting
14 governmental agencies in the definitions of working
15 interest owners.

16 CHAIRMAN FESMIRE: But then you're exempting
17 governmental agencies from force pooling, from compulsory
18 pooling, wouldn't it?

19 THE WITNESS: Except --

20 COMMISSIONER BAILEY: If it's put in --

21 THE WITNESS: -- royalty interests.

22 COMMISSIONER BAILEY: -- 36, you would be. But
23 not if it's put in 7.

24 CHAIRMAN FESMIRE: So your proposal is to make...

25 MS. BADA: Does it only apply if it's released?

1 Could you just say, or except those interests government
2 agencies own of unleased interest in oil and gas?

3 CHAIRMAN FESMIRE: Well, that would -- that's the
4 only time the problem would come up, because if it's leased
5 you're going to have a working interest owner to go
6 against.

7 THE WITNESS: My concern with it would be -- and
8 I'm not sure how this definition works with -- the Statute
9 does not exclude working interests owned by -- or unleased
10 mineral interests owned by -- The Oil and Gas Act does not
11 exclude unleased mineral interests owned by governmental
12 agencies from the provisions of the compulsory pooling
13 statute. It really arises only with state agencies,
14 because by federal law, an interest owned by the federal
15 government cannot be compulsory pooled without their
16 consent.

17 CHAIRMAN FESMIRE: David, this is purely a
18 theoretical problem, because if an operator proposes a
19 well, finds an unleased interest in the tract they're
20 trying to acquire or trying to pool, they're going to
21 acquire that unleased interest. I mean, if the well is
22 worth drilling at, you know --

23 THE WITNESS: Yeah.

24 CHAIRMAN FESMIRE: -- 319/320, it's certainly
25 worth drilling at 320/320.

1 THE WITNESS: I would assume that would be the
2 case, but I -- and that's probably the reason the question
3 has never arisen. I'm just unsure, you know, having been
4 confronted with this seemingly -- somewhat intractable
5 problem for the first time this morning, I can't think
6 through immediately what the consequences of putting any
7 particular provision in any particular place would be,
8 without some more time to investigate or think through it.
9 That's the reason I'm not able to really offer any advice
10 on what you should do.

11 COMMISSIONER BAILEY: What we could do is insert,
12 in that phrase, "or of unleased interests in oil and gas",
13 how would it work to put, "or of unleased non-state
14 interests in oil and gas"? "Non-state"...

15 CHAIRMAN FESMIRE: Why don't we take an hour
16 break for lunch and come back, and --

17 COMMISSIONER BAILEY: Okay.

18 CHAIRMAN FESMIRE: -- after we've thought about
19 it over lunch --

20 THE WITNESS: Okay.

21 CHAIRMAN FESMIRE: -- come back and discuss it.

22 COMMISSIONER BAILEY: Admittedly, this is very
23 theoretical but, you know, it could be that State Parks is
24 not going to be able to get a lease out there.

25 CHAIRMAN FESMIRE: Well, it could have come up in

1 Otero Mesa.

2 COMMISSIONER BAILEY: Well, it could, I guess.

3 CHAIRMAN FESMIRE: It could have, with that 1600-
4 acre tract.

5 So why don't we break for one hour, come back at
6 one o'clock, and we'll start with that problem.

7 (Thereupon, a recess was taken at 12:00 noon.)

8 (The following proceedings had at 1:05 p.m.)

9 CHAIRMAN FESMIRE: Let the record reflect that
10 it's 1:05 p.m. on September 15th, and this is a
11 continuation of the hearing of the New Mexico Oil
12 Conservation Commission, and we were addressing Cause
13 Number 13,555.

14 We had just finished going through the proposed
15 Rules, and we've come upon a problem, and Mr. Brooks was
16 going to think about it and propose a solution after lunch.

17 Let the record reflect there's a long pause while
18 Mr. Brooks --

19 (Laughter)

20 THE WITNESS: Okay. Well, I think that without
21 word-searching the entire OCD Rules, we don't know exactly
22 what the effect of changing a definition is.

23 So my proposal at this point would be to leave
24 the definition -- to withdraw the change in the definition
25 of working interest in 19.15.1.7.W, and instead to change

1 the definition of pooled working interest in proposed
2 19.15.1.36.A.(3), and state there that pooled working
3 interest, for purposes of 19.15.1.36 only, shall mean a
4 working interest or unleased mineral interest that is
5 pooled by order of the Division and not voluntary agreement
6 of the owner thereof, except for any unleased interest
7 owned by any governmental -- any government or governmental
8 agency, I guess is the way -- any governmental agency or --
9 well, there are so many ways to say that. I think we would
10 want to exclude state, federal and tribal land that was
11 unleased.

12 MS. BADA: Can we just say except an unleased
13 interest on state, tribal or federal land?

14 THE WITNESS: Yeah, I think that would cover it.

15 CHAIRMAN FESMIRE: So we are going to essentially
16 eliminate the ability to compulsory pool any interest that
17 has a state, federal or tribal -- unleased state, federal
18 or tribal component to it?

19 THE WITNESS: No, I think that would not be the
20 effect, since that -- since I said for purposes of Rule 36
21 only. All that it would eliminate would be that if there
22 is a force-pooled unit, however it arose, that has unleased
23 federal, state or tribal land in it, then this automatic
24 election procedure would not apply. And everything else
25 with regard to both compulsory pooling and any other

1 context in which "working interest owner" is used would be
2 as it now is, whatever that may be.

3 CHAIRMAN FESMIRE: Okay. Any discussion?

4 COMMISSIONER BAILEY: I'll go along with what
5 David said.

6 COMMISSIONER CHAVEZ: I think that's an excellent
7 solution there.

8 One other thing too, I noticed that the OCD Rules
9 do define mineral interest owners under a separate
10 definition, which does reference also oil and gas leases
11 and interest owners who have not signed an oil and gas
12 lease --

13 CHAIRMAN FESMIRE: Yeah.

14 COMMISSIONER CHAVEZ: -- and I didn't know if
15 that -- to me it looked like the proposal for the
16 definition of W.(9) there was going to be very, very
17 similar to the definition of mineral interest owner, the
18 way it was proposed.

19 THE WITNESS: Well, the difficulty, always, of
20 changing a definition is that when one changes a definition
21 one must do a thorough analysis of the entire body of Rules
22 to find out what effect that change of definition may have,
23 and I have not done that.

24 CHAIRMAN FESMIRE: David, do you think that
25 withdrawing the recommended change in the definition of

1 working interest owner would be necessary if we make that
2 change to 36.A.(3)?

3 THE WITNESS: Would be necessary? No, it would
4 not be necessary, but it could be done.

5 CHAIRMAN FESMIRE: I mean, if we make that change
6 in 36.A.(3), can we not still make this change in the
7 definition of working interest owner?

8 THE WITNESS: We could. I thought the whole
9 purpose of changing it -- of revising the language, though,
10 was to avoid crafting how we were going to make that change
11 in the definition of working interest owner.

12 CHAIRMAN FESMIRE: Okay, so we would make no
13 change in Rule 7?

14 THE WITNESS: That would be my recommendation at
15 present, because I have not word-searched the Rules to be
16 sure how "working interest owner" is used in every place,
17 and so I cannot advise you as to what the effect of making
18 that change would be.

19 CHAIRMAN FESMIRE: Okay. Ms. O'Connor, is there
20 anything else?

21 MS. O'CONNOR: No, Mr. Chairman, that concludes
22 OCD's presentation.

23 COMMISSIONER CHAVEZ: I'm sorry, I do have one
24 more question here.

25 One of the -- it looks like the important parts

1 of your proposed change is significant change talking about
2 how the interest will be considered, and it was put into
3 the definitions. Is that important enough to perhaps
4 include somewhere else in the -- under 36?

5 CHAIRMAN FESMIRE: It is clear in other parts of
6 the Statute, isn't it?

7 THE WITNESS: What? I'm not sure what Frank is
8 talking about.

9 COMMISSIONER CHAVEZ: The portion that starts,
10 "provided that if any unleased mineral interest is pooled
11 by order of the division, seven-eighths of such interest
12 shall be considered a working interest and one-eighth shall
13 be considered a royalty interest."

14 THE WITNESS: That clause is a direct quote from
15 the Oil and Gas Act.

16 COMMISSIONER CHAVEZ: I understand that, and I
17 didn't know why it was significant to put that into a
18 definition. If it was significant to include that
19 somewhere in the Rules --

20 THE WITNESS: The reason that got in there was
21 because I had submitted a definition of working interest
22 owners that would include unleased mineral interest owners,
23 and another member of the work group suggested that that
24 definition would be contrary to the Statute if it didn't
25 include that qualification.

1 COMMISSIONER CHAVEZ: Okay, okay.

2 COMMISSIONER BAILEY: I have one question too.

3 CHAIRMAN FESMIRE: Sure.

4 COMMISSIONER BAILEY: Were there no comments made
5 on these proposed Rules outside of the working group
6 committee meeting and the work group that you mentioned?

7 THE WITNESS: Not to my knowledge. Those would
8 be received by the Commission secretary.

9 MS. DAVIDSON: No, we received none.

10 COMMISSIONER BAILEY: Okay, good. I needed to
11 verify that.

12 CHAIRMAN FESMIRE: There being no other
13 presentation, I think we can step through these Rules.

14 Let's start with the changes from the proposed
15 Rule to the Exhibit A-2, the changes between Exhibit A-1
16 and A-2, and I guess we can step through these and vote on
17 them individually.

18 The first one I have is under 36.A.(1) to include
19 the phrase "proration or spacing unit" after the word
20 "pooled" so that the sentence reads, "Operator shall mean
21 the division-appointed operator of a compulsory pooled
22 proration or spacing unit, or its successor."

23 Any comment on that?

24 COMMISSIONER BAILEY: I move we accept that
25 change.

1 COMMISSIONER CHAVEZ: I would like to add
2 "division- or commission-appointed operator".

3 CHAIRMAN FESMIRE: Mr. Brooks, would you have any
4 comment on that?

5 THE WITNESS: No objection.

6 CHAIRMAN FESMIRE: So that the sentence will
7 read, "Operator shall mean the division- or commission-
8 appointed operator of a compulsory pooled proration or
9 spacing unit, or its successor."

10 Since we have a motion, do you want to withdraw
11 your original motion?

12 COMMISSIONER BAILEY: I'll withdraw the original
13 and make it for this one.

14 CHAIRMAN FESMIRE: Okay.

15 COMMISSIONER CHAVEZ: Second.

16 CHAIRMAN FESMIRE: All those in favor?

17 COMMISSIONER BAILEY: Aye.

18 COMMISSIONER CHAVEZ: Aye.

19 CHAIRMAN FESMIRE: Opposed? So sentence one
20 shall read, "Operator shall mean the division- or
21 commission-appointed operator of a compulsory pooled
22 proration or spacing unit, or its successor."

23 The second difference between A-1 and A-2 that I
24 have is in 36.B, the first line, "Whenever are authorized
25 pursuant to..." --

1 COMMISSIONER BAILEY: You skipped some.

2 CHAIRMAN FESMIRE: Oh, I'm sorry, I did. Let me
3 retract that. The next change is in 36.A.(2). The
4 sentence reads, "Infill well shall mean a well in a
5 compulsory pooled unit to be completed in a pool..." --

6 COMMISSIONER BAILEY: -- "...in a compulsory
7 pooled proration or spacing unit..."

8 CHAIRMAN FESMIRE: -- "...in a compulsory pooled
9 proration or spacing unit to be completed in a pool in
10 which an existing well drilled pursuant to the compulsory
11 pooling order has been completed and not plugged and
12 abandoned."

13 There are two changes there. Do I have a motion
14 on --

15 COMMISSIONER CHAVEZ: I move we accept the
16 changes as you read them.

17 COMMISSIONER BAILEY: Second.

18 CHAIRMAN FESMIRE: All those in favor?

19 COMMISSIONER CHAVEZ: Aye.

20 COMMISSIONER BAILEY: Aye.

21 CHAIRMAN FESMIRE: Opposed?

22 A.(2) should read, "Infill well shall mean a well
23 in a compulsory pooled proration or spacing unit to be
24 completed in a pool in which an existing well drilled
25 pursuant to the compulsory pooling order has been completed

1 and not plugged and abandoned."

2 The next one is 36.(3) [sic], and that was a
3 rather extensive change. I'm going to ask Mr. Brooks to
4 read his change in that.

5 THE WITNESS: Did you copy down when I --

6 MS. BADA: I didn't catch all of that --

7 THE WITNESS: Okay.

8 MS. BADA: -- I just got the last part. If
9 somebody caught the middle, then I think --

10 THE WITNESS: Okay, I will attempt to restate it
11 again. I did not write it down.

12 "Pooled working interest, for purposes of
13 19.15.1.36 only..." --

14 MS. BADA: I don't know that you need to say
15 that, because you say it right above in A.

16 THE WITNESS: Okay. Yeah, okay, probably I
17 don't. You're probably right. "Pooled working interest
18 shall mean a working interest..." comma -- no, "...shall
19 mean a working interest or unleased mineral interest that
20 is pooled by order of the Division and not by voluntary
21 agreement of the owner thereof, except for an unleased
22 interest owned by..." -- or I believe you --

23 MS. BADA: I think -- what did we say?

24 THE WITNESS: -- had some suggested language.

25 MS. BADA: I think we said "except an unleased

1 interest on federal, state or tribal lands".

2 THE WITNESS: Okay, that sounds good to me.

3 CHAIRMAN FESMIRE: Okay.

4 MS. BADA: I had one question, and I just wanted
5 to be clear on it. Are working interests ever pooled by
6 the Commission?

7 THE WITNESS: They might be.

8 CHAIRMAN FESMIRE: Yes, could be.

9 COMMISSIONER CHAVEZ: Yes, it would have to be
10 Division or Commission, it should say.

11 CHAIRMAN FESMIRE: Okay, is there a motion on
12 36.A.(3) as amended?

13 COMMISSIONER CHAVEZ: I'd like to hear the whole
14 thing read now, with all of those --

15 CHAIRMAN FESMIRE: Okay --

16 COMMISSIONER CHAVEZ: -- additions.

17 CHAIRMAN FESMIRE: -- that's what I was trying to
18 avoid.

19 COMMISSIONER CHAVEZ: I know, but I --

20 CHAIRMAN FESMIRE: Please.

21 MS. BADA: Okay, "Pooled working interest shall
22 mean a working interest or unleased mineral interest that
23 is pooled by order of the Division or Commission and not by
24 voluntary agreement of the owner thereof, except for an
25 unleased interest on federal, state or tribal lands."

1 COMMISSIONER CHAVEZ: I move we accept that
2 language.

3 COMMISSIONER BAILEY: Second.

4 CHAIRMAN FESMIRE: All those in favor?

5 COMMISSIONER CHAVEZ: Aye.

6 COMMISSIONER BAILEY: Aye.

7 CHAIRMAN FESMIRE: Opposed?

8 Okay, 36.A.(3) shall read as previously read.

9 The next one is 36.B. In the first line the
10 phrase "are authorized, pursuant to" was stricken, so that
11 the new sentence should read, "Subsequent operations.
12 Whenever 19.15.3.104 NMAC or any applicable pool rule
13 authorizes one or more infill wells within a spacing unit
14 pooled by the order of the division or the commission
15 pursuant to 70-2-17 NMSA 1978..."

16 Is there any discussion about striking the phrase
17 "are authorized, pursuant to"?

18 COMMISSIONER CHAVEZ: I move we accept that,
19 striking "are authorized, pursuant to".

20 COMMISSIONER BAILEY: Second.

21 CHAIRMAN FESMIRE: All those in favor?

22 COMMISSIONER BAILEY: Aye.

23 COMMISSIONER CHAVEZ: Aye.

24 CHAIRMAN FESMIRE: Opposed? The motion carries.

25 36.B shall read as previously --

1 MS. BADA: Before you go on, in A you use
2 "proration or spacing". Do you need to do that again in B
3 also, where it says "within a spacing unit".

4 CHAIRMAN FESMIRE: "within a proration or spacing
5 unit".

6 COMMISSIONER CHAVEZ: Wait just a second. I
7 think the language may be appropriate there --

8 MS. BADA: Okay.

9 COMMISSIONER CHAVEZ: -- "infill wells within a
10 spacing unit", because the infill wells are within spacing
11 units now.

12 MS. BADA: Okay, not within proration.

13 COMMISSIONER CHAVEZ: Okay, 104. 104 refers to
14 spacing units, number of wells per spacing unit
15 consistently the language in 104. So I think that that's
16 probably the language that we should use there.

17 MS. BADA: So then would you want an infill well
18 defined to include a proration unit, as you have in A?

19 COMMISSIONER CHAVEZ: Oh, I see the point you're
20 making, yeah. A separate order may use the language for
21 proration unit, though, for an individual pool.

22 MS. BADA: Okay.

23 COMMISSIONER CHAVEZ: So we probably should allow
24 both that language --

25 MS. BADA: -- in the definition.

1 COMMISSIONER CHAVEZ: Uh-huh.

2 CHAIRMAN FESMIRE: Okay, so there's a separate
3 motion to include the phrase "within a proration" on the
4 second line of B before the word "spacing"; is that
5 correct?

6 COMMISSIONER CHAVEZ: Within this proration or
7 spacing unit, right. I move that we include that
8 language.

9 COMMISSIONER BAILEY: Second.

10 CHAIRMAN FESMIRE: All those in favor?

11 COMMISSIONER BAILEY: Aye.

12 COMMISSIONER CHAVEZ: Aye.

13 CHAIRMAN FESMIRE: Opposed?

14 The phrase shall read, "infill wells within a
15 proration or spacing unit."

16 Okay, the next one I have is the fifth from the
17 bottom line in C, at the bottom of the page, the phrase "as
18 defined in 19.15.1.35 NMAC" has been added. Any
19 discussion?

20 COMMISSIONER BAILEY: I move we accept that
21 language.

22 COMMISSIONER CHAVEZ: I second.

23 CHAIRMAN FESMIRE: All those in favor?

24 COMMISSIONER BAILEY: Aye.

25 COMMISSIONER CHAVEZ: Aye.

1 CHAIRMAN FESMIRE: Opposed?

2 Okay, it shall read as such.

3 The second one on page 2, "infill well no later
4 than 120 days after the expiration of the initial notice
5 period of 30 days. The division director..." -- add the
6 word "director" -- "...may extend the time for commencement
7 of drilling..."

8 COMMISSIONER CHAVEZ: I move we insert the word
9 "director" after "division".

10 COMMISSIONER BAILEY: Second.

11 CHAIRMAN FESMIRE: All those in favor?

12 COMMISSIONER BAILEY: Aye.

13 COMMISSIONER CHAVEZ: Aye.

14 CHAIRMAN FESMIRE: The motion carries. The word
15 "director" will be inserted so that the sentence reads,
16 "The division director may extend the time for commencement
17 of drilling once for not more than an additional 120
18 days..."

19 The next proposed change is in Section D,
20 "Proposal by pooled working..." -- "Proposal by pooled
21 working interest owner." The suggestion -- suggested
22 change, is to add the words "working interest" between
23 "pooled" and "owner" so that the title -- or that the --
24 Would this be a title?

25 MS. BADA: Yes.

1 CHAIRMAN FESMIRE: So that the section title
2 reads, "Proposal by pooled working interest owner."

3 COMMISSIONER CHAVEZ: I move we accept that.

4 COMMISSIONER BAILEY: Second.

5 CHAIRMAN FESMIRE: All those in favor?

6 COMMISSIONER BAILEY: Aye.

7 COMMISSIONER CHAVEZ: Aye.

8 CHAIRMAN FESMIRE: Motion carries. The section
9 title shall read, "Proposal by pooled working interest
10 owner."

11 The next change that I have is the seventh line
12 down in the middle. It currently reads, "...proposed well
13 will is be located..." The suggestion is that we strike
14 the word -- or "...will is located..." The suggestion is
15 that we strike the word "is" and add the word "be", so that
16 the phrase reads, "...where the proposed well will be
17 located..."

18 Is there a motion --

19 COMMISSIONER CHAVEZ: I move we accept that.

20 COMMISSIONER BAILEY: Second.

21 CHAIRMAN FESMIRE: All those in favor?

22 COMMISSIONER CHAVEZ: Aye.

23 COMMISSIONER BAILEY: Aye.

24 CHAIRMAN FESMIRE: Opposed? The change is
25 accepted.

1 The next change I have is the third from the last
2 line on Section D where the phrase reads, "...all owners of
3 working interests in the unit, including those whose
4 interests in the unit are pooled by agreement..."

5 Should read -- or it is suggested that it read,
6 "...all owners of working interests in the unit, including
7 those whose interests in the proration or spacing unit are
8 pooled by agreement..." Addition of the phrase "proration
9 or spacing".

10 COMMISSIONER BAILEY: The more I look at that
11 sentence, we may want to insert that phrase in the first
12 reference to "unit" at the beginning of that sentence,
13 where it would read, "The owner filing such application
14 shall give notice thereof as provided...to all owners of
15 working interests in the proration or spacing unit..."

16 And then the other references to "unit" within
17 that sentence would carry that same designation.

18 COMMISSIONER CHAVEZ: I agree with that.

19 CHAIRMAN FESMIRE: Okay, do I hear a motion to
20 that effect?

21 MS. BADA: I have one other thing. I didn't know
22 if you wanted -- where -- it's about, oh, halfway down.
23 It's the same sentence that's above in C, and it talks
24 about the Division extending the time for commencement.
25 Did you want that to be "the division director" again?

1 CHAIRMAN FESMIRE: I guess it would have to be to
2 match, wouldn't it?

3 COMMISSIONER CHAVEZ: Yes.

4 COMMISSIONER BAILEY: Uh-huh.

5 COMMISSIONER CHAVEZ: Discussion of two things.
6 I move we accept insertion of "director" after "division"
7 on that referenced line.

8 COMMISSIONER BAILEY: Second.

9 CHAIRMAN FESMIRE: Okay, all those in favor?

10 COMMISSIONER BAILEY: Aye.

11 COMMISSIONER CHAVEZ: Aye.

12 CHAIRMAN FESMIRE: Opposed?

13 COMMISSIONER CHAVEZ: And I move we insert the
14 "proration or spacing" in the -- before the word "unit" at
15 the end of the fifth line from the bottom of Section D.

16 COMMISSIONER BAILEY: Second.

17 CHAIRMAN FESMIRE: Fifth line or the fourth line?

18 COMMISSIONER CHAVEZ: Fourth line, I guess it's
19 the fourth line, excuse me.

20 CHAIRMAN FESMIRE: Okay.

21 COMMISSIONER CHAVEZ: I think we're all referring
22 to the same one.

23 CHAIRMAN FESMIRE: Is there a motion -- Oh,
24 there's been a motion. Is there a second?

25 COMMISSIONER BAILEY: Second.

1 CHAIRMAN FESMIRE: All those in favor?

2 COMMISSIONER BAILEY: Aye.

3 COMMISSIONER CHAVEZ: Aye.

4 CHAIRMAN FESMIRE: The motion passes on both of
5 those changes.

6 The last change I have in the proposed order is
7 Section F, and it's the addition of that entire section.
8 I'll go ahead and read it for the record.

9 "Determination of reasonable well costs. The
10 provisions of the applicable compulsory pooling order
11 regarding reporting of actual well costs to the division
12 and to pooled working interest owners, opportunity for
13 objection thereto, determination of reasonableness of well
14 costs, and adjustment of the amount paid by any
15 participating pooled working interest owner to reflect
16 reasonable well costs, shall apply to any well drilled
17 pursuant to 19.15.1.36 NMAC."

18 COMMISSIONER CHAVEZ: I move we accept that
19 section as proposed.

20 CHAIRMAN FESMIRE: All those in favor?

21 COMMISSIONER BAILEY: Aye.

22 CHAIRMAN FESMIRE: Opposed? The motion carries.
23 Section F will be accepted.

24 The Chair will now entertain a motion to accept
25 the Rules as -- the Rule changes to 19.15.1.36 as amended

1 in its entirety.

2 COMMISSIONER BAILEY: I so move.

3 COMMISSIONER CHAVEZ: I second.

4 CHAIRMAN FESMIRE: All those in favor?

5 COMMISSIONER BAILEY: Aye.

6 COMMISSIONER CHAVEZ: Aye.

7 CHAIRMAN FESMIRE: Opposed?

8 Let the record reflect that those changes will be
9 adopted, and the Rule will be adopted by the Commission.

10 For clarification, we are no longer wishing to
11 amend Rule 7, and that Section 7.W that was originally
12 proposed as change has been stricken. Let's have a vote to
13 make sure that that's clear on the record.

14 Is there a motion to strike the proposed
15 amendment of 19.15.1.7?

16 COMMISSIONER BAILEY: I so move.

17 COMMISSIONER CHAVEZ: I second.

18 CHAIRMAN FESMIRE: All those in favor?

19 COMMISSIONER BAILEY: Aye.

20 COMMISSIONER CHAVEZ: Aye.

21 CHAIRMAN FESMIRE: Opposed?

22 Madame Counsel, is there anything else we have
23 to --

24 MS. BADA: I would appreciate it if each one of
25 you can state briefly your reasons for choosing to adopt

1 the -- those revisions, so when we draft the order I'll
2 have it.

3 CHAIRMAN FESMIRE: Commissioner Bailey?

4 COMMISSIONER BAILEY: I believe they're in the
5 best interests of the Division for clarification to all
6 interested parties that -- what the Rules are and how --
7 what the process should be for compulsory pooling.

8 CHAIRMAN FESMIRE: Commissioner Chavez?

9 COMMISSIONER CHAVEZ: Yes, with the advent of
10 more infill drilling it was unclear to the operators what
11 was important, what needed to be done in the -- for
12 compulsory pooled spacing and proration units that allowed
13 infill wells. So by the addition of Rule 36 they have a
14 much better idea now of how to proceed with further
15 development within such a compulsory pooled unit.

16 CHAIRMAN FESMIRE: And I believe -- my reason for
17 adopting these Rules was that I think it's in the best
18 interests of the State in terms of preventing waste,
19 protecting correlative rights. It also simplifies some of
20 the procedures that have been a little bit awkward in the
21 past. And I believe it provides economic incentive to
22 develop the resources of the State of New Mexico.

23 (Thereupon, these proceedings were concluded at
24 1:35 p.m.)

25

* * *

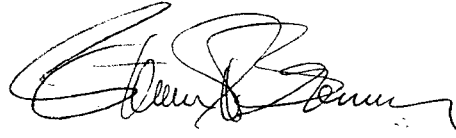
CERTIFICATE OF REPORTER

STATE OF NEW MEXICO)
) ss.
COUNTY OF SANTA FE)

I, Steven T. Brenner, Certified Court Reporter and Notary Public, HEREBY CERTIFY that the foregoing transcript of proceedings before the Oil Conservation Commission was reported by me; that I transcribed my notes; and that the foregoing is a true and accurate record of the proceedings.

I FURTHER CERTIFY that I am not a relative or employee of any of the parties or attorneys involved in this matter and that I have no personal interest in the final disposition of this matter.

WITNESS MY HAND AND SEAL September 17th, 2005.



STEVEN T. BRENNER
CCR No. 7

My commission expires: October 16th, 2006