

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

4 IN THE MATTER OF THE HEARING CALLED
5 BY THE OIL CONSERVATION DIVISION FOR
6 THE PURPOSE OF CONSIDERING:

ORIGINAL

CASE 15404

7 APPLICATION OF BURNETT OIL CO., INC.,
8 for a NON-STANDARD OIL SPACING AND
9 PRORATION UNIT AND COMPULSORY POOLING,
10 EDDY COUNTY, NEW MEXICO.

11 REPORTER'S TRANSCRIPT OF PROCEEDINGS

12 EXAMINER HEARING

13 November 12, 2015

14 Santa Fe, New Mexico

15 BEFORE: WILLIAM V. JONES, CHIEF EXAMINER
16 GABRIEL WADE, LEGAL EXAMINER

17 This matter came on for hearing before the
18 New Mexico Oil Conservation Division, William V. Jones,
19 Chief Examiner, and Gabriel Wade, Legal Examiner, on
20 November 12, 2015, at the New Mexico Energy, Minerals,
21 and Natural Resources Department, Wendell Chino
22 Building, 1220 South St. Francis Drive, Porter Hall,
23 Room 102, Santa Fe, New Mexico.

24 REPORTED BY: ELLEN H. ALLANIC
25 NEW MEXICO CCR 100
CALIFORNIA CSR 8670
PAUL BACA COURT REPORTERS
500 Fourth Street, NW
Suite 105
Albuquerque, New Mexico 87102

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A P P E A R A N C E S

For the Applicant:

James G. Bruce, Esq.
P.O. Box 1056
Santa Fe, New Mexico 87504
(505)982-2043
jamesbruc@aol.com

For Ard Oil, Ltd., and Ard Energy Group, Ltd.:

Ernest L. Padilla, Esq.
Padilla Law Firm, P.A.
1512 S. St. Francis Drive
Santa Fe, New Mexico 87505
(505)988-7577
padillalaw@qwestoffice.net

Also Present: William F. Carr, Esq.

I N D E X

CASE NUMBER 15404 CALLED

BURNETT OIL CO., INC.
CASE-IN-CHIEF:

WITNESS COLEY MEANS

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7 ARD OIL, LTD., AND ARD ENERGY, LTD.
CASE-IN-CHIEF

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9 WITNESS HOUSTON KAUFFMAN

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1 (Time noted 10:28 a.m.)

2 EXAMINER JONES: So let's call case 15404,
3 Application of Burnett Oil Co., Inc., for a nonstandard
4 oil spacing and proration unit and compulsory pooling,
5 Eddy County, New Mexico.

6 Call for appearances.

7 MR. BRUCE: Mr. Examiner, Jim Bruce of
8 Santa Fe representing the applicant. I have two
9 witnesses.

10 MR. PADILLA: Mr. Examiner, Ernest L.
11 Padilla for Ard Oil, Ltd., and Ard Energy Group, Ltd. I
12 have one witness.

13 EXAMINER JONES: Any other appearances?

14 (No response.)

15 EXAMINER JONES: Will all witnesses please
16 stand and will the court reporter please swear the
17 witnesses.

18 (WHEREUPON, the presenting witnesses
19 were administered the oath.)

20 MR. WADE: Are there any prehearing motions
21 or procedural matters?

22 MR. BRUCE: The only thing I would say is
23 that due to developments in the last 24 hours,
24 there's -- I mean Mr. Padilla will put on his case, but
25 we think there's a good chance the parties will reach an

1 agreement in this matter.

2 But because of a terminating term assignment
3 coming up, we need to put it on.

4 MR. WADE: For the record, there are no
5 prehearing motions or procedural matters, so we will go
6 ahead and continue.

7 COLEY MEANS
8 having been first duly sworn, was examined and testified
9 as follows:

10 DIRECT EXAMINATION

11 BY MR. BRUCE:

12 Q. Please state your name and city of residence.

13 A. Coley Means, Fort Worth, Texas.

14 Q. Who do you work for and in what capacity?

15 A. I work for Burnett Oil Co. as a landman.

16 Q. Have you previously testified before the
17 Division?

18 A. I have.

19 Q. And were your credentials as an expert petroleum
20 landman accepted as a matter of record?

21 A. Yes, sir.

22 Q. And are you familiar with the land matters
23 involved in this case and the subsequent case?

24 A. Yes, sir.

25 MR. BRUCE: I tender Mr. Means as an expert

1 petroleum landman.

2 MR. PADILLA: No objection.

3 EXAMINER JONES: He is so qualified.

4 Q. Mr. Means, could you identify Exhibit 1 and
5 describe the acreage and the formation involved in the
6 well unit.

7 A. Our Exhibit 1 is -- the first page is the -- a
8 copy of the first page of the approved APD for the well.
9 This is the Nosler 12 Federal DB 4H Well.

10 The unit for the well is going to be the north
11 half, northwest quarter and northwest, northeast quarter
12 of Section 12, Township 17 South, 31 East.

13 The surface location is actually in the adjoining
14 section 11. But the first take point will be 330 inside
15 of section 12, so the entire producing interval will be
16 orthodox.

17 Q. Why is the northeast quarter, northeast quarter
18 of section 12 not included in the well unit?

19 A. Burnett Oil Co. does not own any leasehold in the
20 northeast, northeast. And, in fact, the entire east
21 half, east half of section 12 is COG leasehold. And
22 they have two -- I believe two but at least one
23 horizontal Yeso wells in that 160.

24 Q. Okay. And what formation is being pooled in this
25 well?

1 A. So this is the -- it's a Yeso well, Fren Glorieta
2 Yeso. The Pool Code is on the C-102 -- which is the
3 second page of our Exhibit 1 -- which is 26770.

4 Q. Who is being pooled in this case?

5 A. So we are looking to pool the interest of Ard Oil
6 Company and -- excuse me -- Ard Oil, Ltd., and Ard
7 Energy Group, LTD.

8 Q. And what is Exhibit 2?

9 A. Exhibit 2 is our well proposal sent -- I am just
10 going to refer to Ard Oil and Ard Energy as Ard,
11 collectively -- sent to Ard on September 17th. This is
12 a well proposal letter including an AFE for this, for
13 the DB 4H well and, actually, the subsequent case, the
14 6H well, as well.

15 Q. There are or there were some odd land matters
16 involved in this case; is that fair to say?

17 A. It's a safe statement.

18 Q. What is Exhibit 3?

19 A. Exhibit 3 is a -- kind of a partial copy of the
20 JOA governing this well and -- what's actually copied
21 here is article 16 thereof, which is the other
22 provisions.

23 Q. Let me interrupt for a minute. Although there is
24 a JOA covering this well unit, it does not cover the Ard
25 interest; is that correct?

1 A. That is correct.

2 Q. At one time were the Ard interests covered by the
3 JOA?

4 A. Yes. So I guess you are going to need a little
5 background. The Ard interest was subject to a term
6 assignment in favor of COG Operating. The term
7 assignment expired, let's say, I think effective
8 sometime in October of 2013. Of course, COG Operating
9 is a party to the operating agreement, so when they had
10 the interest, the Ard interest was subject to the
11 operating agreement.

12 Now that the term assignment has expired, as to
13 everything that was not earned thereunder, Ard now has
14 his interest and is not subject to this operating
15 agreement.

16 Q. In looking at the Article 16-E, when this JOA was
17 signed, what did it say with respect to interest owners
18 dealing with the Ards?

19 A. There is this provision, Article 16-E, you
20 reference in the operating agreement. I think, if I
21 can, a little background on it may be helpful for the
22 Commission, for the Examiner and everybody.

23 As I mentioned, the interest of Ard was in a term
24 assignment that expired. They got their interest back.

25 There was -- going back in years past, there

1 arose a disagreement between -- about some well
2 proposals and this area between COG and Burnett.

3 That dispute, disagreement, went on for a
4 prolonged period of time, about a year. And this
5 operating agreement was part of, basically, kind of the
6 resolution of it.

7 And this provision, in a sense, kind of burgeoned
8 out of the resolution of the dispute. And, effectively,
9 it is pretty straightforward in the way it reads. The
10 idea was the interest was subject to a term assignment
11 in favor of Concho, and, if the term assignment expired,
12 the parties to the operating agreement agreed not to go
13 pursue the interest or not to go take a term -- take a
14 term assignment from Ard, that they would allow -- would
15 exclusively give that right to COG. So that was, I
16 think, honestly not something that Burnett bargained
17 for, but you're at the end of a year long dispute and
18 close to settlement, wanting to get it over with.

19 To be honest at the time, too, Burnett was
20 aligned with Hudson, the Hudson family. And there's --
21 I think it is a matter of public knowledge -- that
22 there's not been a great relationship there.

23 And at the time, because Burnett was aligned with
24 Hudson, Ard really would not even negotiate with
25 Burnett. So you kind of have -- this provision came out

1 of the fact that, one, Burnett didn't think Ard would
2 even deal with Burnett on a term assignment and in order
3 to get the deal settled like the provision was agreed
4 to.

5 So at any rate this provision ended up in the
6 operating agreement. So what has happened here, though,
7 is that -- well, does that answer the question?

8 MR. BRUCE: Mr. Examiner, I can't find a
9 copy of the order. I will e-mail you information on the
10 order which -- it was a lengthy proceeding before the
11 Division, resulting in an order. I will give you that
12 order number. And it will give you some background
13 about what was going on.

14 Q. And, Mr. Means, is it fair to say that in order
15 to settle the disputes after that order came out between
16 Burnett and COG, this JOA was entered into?

17 A. That is correct. It was part of the settlement
18 deal, was entering in this JOA.

19 Q. And if you would look at Article 16-E, item 2,
20 would you just quote that for the Examiner.

21 A. "The parties hereto, other than COG, will not
22 attempt to obtain an assignment of Ard's working
23 interest in the contract area in which such interest has
24 lapsed."

25 Q. So in dealing with the Ards, Burnett was --

1 A. Contractually limited, I would say.

2 Q. Thank you. Before we go into details about
3 conversations between the Ards and Burnett, has that
4 particular contractual issue been resolved?

5 A. Yes, very recently.

6 Q. And if you could refer to Exhibit 14, Mr. Means.
7 What is that?

8 A. Exhibit 14 is a copy of the letter only -- a copy
9 of an agreement to amend this Joint Operating Agreement
10 to delete Article 16-E by COG.

11 Q. And we will present evidence that the other
12 working interest owners in the JOA have also agreed to
13 remove paragraph E from the JOA?

14 A. That is correct. Now all parties to the
15 operating agreement have agreed to amend it to delete
16 that provision.

17 Q. Okay. So this gives Burnett a little more
18 freedom to deal with the Ards?

19 A. Yes.

20 Q. Okay. With that background -- what is Exhibit 4,
21 if you will?

22 A. Exhibit 4 is a summary and timeline format on our
23 dealings -- of Burnett's dealings with Ard on these two
24 well proposals.

25 Q. And since there's been some resolution to this --

1 I am not going to ask you to go through this in some
2 detail -- but could you summarize a few of the key
3 points?

4 A. I can, yes. I think the easiest place to start
5 is back in December of 2014, Mr. Ard actually came over
6 to our offices in Fort Worth to have a discussion. This
7 gets -- there has been a lot of moving parts in this.
8 But at the time there was some questions about the
9 expiration of the term assignment and exactly what was
10 earned and whether or not Mr. Ard had received a
11 reassignment of the interest from COG. And so we
12 discussed those things.

13 We were also at the time pursuing extensions of
14 the term assignments that constitute Burnett's interest.
15 And so we had some discussions with him about that. And
16 said that we have been able to negotiate extensions of
17 those term assignments -- and this was late 2014, so the
18 oil market was what the oil market was. It headed
19 downhill rapidly.

20 So we had secured these extensions and told them,
21 you know, We've got these but we think this is all we
22 can buy. At the expiration at or near the end of these
23 extensions, we will need to develop this acreage, we are
24 going to have to drill a well.

25 So he suggested to us that, you know, we had all

1 these issues in the past but he wanted to move forward
2 and cooperate with Burnett. And we expressed the same
3 desire on a go forward basis.

4 And then things went on down the road. It was
5 roughly early August, we got back in touch with Mr. Ard,
6 Julian Ard and told him we would like to visit with them
7 about our plans, that we were going to propose some
8 wells and needed to start getting on our development
9 program.

10 Roughly into late August, Mr. Ard advised us he
11 had become ill and was contacting a friend of his to
12 help him deal with his interest during the pendency of
13 his illness. And so Houston Kauffman then kind of
14 became his -- whom we had been dealing with -- to his
15 interest.

16 Basically, to kind of glean I think the substance
17 of this for you, at least in my opinion, we began
18 negotiating with Ard and, in effect -- you can go
19 through, there's some e-mails there referencing kind of
20 an idea -- Ard would, hopefully he thought would -- you
21 know, the idea of entering into an operating agreement
22 covering basically the entirety of the contract lands
23 with Burnett, wherein he would go out on an override, as
24 opposed to a nonconsent penalty, and have some
25 optionality. And on a well-by-well basis was something

1 he would be agreeable to.

2 So we kind of, you know, started teeing up those
3 down the road. Had some discussions around term
4 assignments. You know, these were all -- just kind of
5 negotiations, preliminary going back and forth.

6 Kind of during all that, we recalled that there
7 was this limitation in the operating agreement, which,
8 pretty much, when we got back into it and reviewed it
9 with counsel and whatnot, our hands are tied as far as
10 dealing with Mr. Ard.

11 So we advised Ard, Listen. Sorry. We forgot
12 about this provision, but we are contractually limited
13 by virtue of our agreement with Concho not to deal with
14 your interest, can't take an assignment, that we really
15 have two ideas here, one, we are going to go ask
16 everybody to delete the provision, because we think if
17 Concho is not interested in it, maybe they'll waive it,
18 delete it. We can then negotiate. And, then, two, we
19 are happy to suggest some other people we think may be
20 interested in the interest.

21 So we did just that. We sent a letter around to
22 everybody asking them to delete the provision. Everyone
23 with the exception of Concho agreed relatively quickly.
24 And we followed it up with some correspondence with
25 Concho, which is in your exhibit packet. And we asked

1 them again to delete it.

2 We got word that they did delete it yesterday
3 evening, but it was too late in terms of our deal with
4 them. We also put Ard in touch with Chase Oil Company.
5 They were interested in the interest, so we kind of
6 facilitated a contact there.

7 And they did meet. And I am not real sure on the
8 particulars of what came out of that.

9 But we did make those efforts in his regard.
10 And, of course, we proposed the well and asked him to
11 join the existing operating agreement. And that is
12 clearly documented.

13 So what you'll glean from all those exhibits is,
14 basically, we offered the well and offered Ard to join
15 the operating agreement.

16 We attempted to negotiate with them. We realized
17 we were contractually restrained, went about to kind of
18 what we thought were the most logical solutions -- and,
19 one, getting the provision deleted, and, two, trying to
20 help them find somebody else.

21 And that's pretty much the substance of all those
22 exhibits.

23 Q. Okay. And just quickly, let's -- exhibits --
24 let's just run through Exhibit 5. That's simply --
25 David Rhodes is a VP at Burnett?

1 A. He's a VP of Land.

2 Q. And this is some of his contacts with Joe Graf
3 who works for Ard?

4 A. Yes, sir.

5 Q. And then Exhibit 6 is the Burnett offer for Ard
6 to join the existing JOA?

7 A. This is correct. Exhibit 6 is our offer for Ard
8 Oil and Ard Energy to join the existing operating
9 agreement and participate in the well.

10 Q. And is Exhibit 7 simply a request from Ard to
11 resend the JOA; they might have lost their copy?

12 A. Yes.

13 Q. Is Exhibit 8 the September 30th letter request to
14 the various JOA parties to delete Article 16-E from the
15 JOA?

16 A. It is.

17 Q. And all the parties signed this except for COG at
18 the time?

19 A. At the time, correct.

20 Q. And then Exhibit 9, is that a subsequent
21 request to COG?

22 A. A subsequent request to COG when -- we had asked
23 to delete the provision in its entirety, and the
24 substance of that letter is just, If deleting it in its
25 entirety is a problem, how about waiving the right in

1 writing just to these two well proposals.

2 Q. And then you mentioned Mr. Houston Kauffman; is
3 he in this room today?

4 A. Yes, sir.

5 Q. Is he the witness for Ard?

6 A. He is.

7 Q. And you have had -- you or maybe David Rhodes
8 have had extensive e-mail correspondence with
9 Mr. Kauffman; is that correct?

10 A. Yes. And the point here is just to demonstrate
11 that -- in instances, we were asked questions by Ard.
12 We have done our best to be responsive. And I think in
13 all instances we have been responsive and we have been
14 cooperative to the absolute best we could have been
15 considering our contractual limitation through the
16 majority of this time.

17 Q. So that's Exhibit 10. And then you mentioned
18 Chase Oil Corp is Exhibit 11, e-mail correspondence
19 regarding putting Ard in touch with Chase Oil?

20 A. Yes.

21 Q. Have you informed Mr. Kauffman this morning that
22 you did get Exhibit 14, the waiver from COG yesterday
23 afternoon?

24 A. Yes. I did inform Mr. Kauffman about it and told
25 him that we would be happy to continue, basically, where

1 we left off in our negotiations to come to a resolution
2 as kind of a voluntary deal with us. We are more than
3 happy and will work at that, but we have to get this
4 well drilled. We will lose valuable term assignments if
5 we don't spud this well in January, so we have to get
6 the well drilled and need the interest committed one way
7 or the other.

8 Q. In your opinion, has Burnett made a good faith
9 effort to obtain the voluntary joinder of the Ard
10 interest in the well?

11 A. Yes, absolutely.

12 Q. And you said you will continue negotiating with
13 Mr. Kauffman. If you reach agreement with the Ard
14 interest, will you notify the Division that forced
15 pooling is no longer required?

16 A. Yes, absolutely.

17 MR. BRUCE: I would note, Mr. Examiner, that
18 even if joinder is reached, we do need approval for the
19 nonstandard spacing unit since it is only 120 acres.

20 EXAMINER JONES: Nonstandard project area?

21 MR. BRUCE: Nonstandard project area,
22 correct.

23 Q. Referring back to Exhibit 2, Mr. Means, does that
24 contain an AFE for the number 4 well?

25 A. Yes, it does.

1 Q. Could you identify the bottom line cost of that
2 well?

3 A. I believe it is roughly 4.3. Excuse me, 3.4,
4 even better.

5 Q. Is that cost fair and reasonable and in line with
6 the costs of other wells drilled at this depth in this
7 area of New Mexico?

8 A. Yes, sir.

9 Q. Do you have a recommendation as to the overhead
10 rates for the well?

11 A. 6,500, drilling, and 650, producing, is what is
12 in our current operating agreement.

13 Q. And are those rates similar to those used by
14 Burnett and other operators of Yeso horizontal wells in
15 this area?

16 A. They are.

17 Q. And do you request that Burnett Oil Co., Inc., be
18 named operator of the well?

19 A. We do.

20 Q. Was notice of this hearing -- if you do not reach
21 terms with the Ards, do you request the maximum cost
22 plus 200 percent risk charge?

23 A. We would.

24 Q. And would you request that the overhead rates be
25 adjusted as provided by the Copas accounting procedure?

1 A. We would.

2 Q. And was notice given to the Ards of this hearing?

3 A. It was. And that is shown in our Exhibit 12.

4 Q. And who are the only offset operators or working
5 interest owners to Burnett's proposed well unit?

6 A. COG Operating, LLC.

7 Q. And is Apache also an offset working interest
8 owner?

9 A. They are.

10 Q. And were they given notice of this hearing?

11 A. They were. And that is demonstrated in our
12 Exhibit 13.

13 Q. Were Exhibits 1 through 14 prepared by you or
14 under your direction or compiled from company business
15 records?

16 A. They were.

17 Q. And in your opinion is the granting of this
18 application in the interest of conservation and the
19 prevention of waste?

20 A. Yes.

21 MR. BRUCE: Mr. Examiner, I move the
22 admission of Exhibits 1 through 14.

23 EXAMINER JONES: Any objection?

24 MR. PADILLA: No objection.

25 EXAMINER JONES: Any objection?

1 MR. CARR: May it please the Examiner, I'm
2 William F. Carr, Senior Counsel to COG. We reached an
3 agreement last night and we are not participating in
4 this hearing.

5 EXAMINER JONES: Thank you, sir. Which
6 exhibits were you admitting?

7 MR. BRUCE: 1 through 14.

8 EXAMINER JONES: 1 through 14 are admitted.

9 (Burnett Oil Co., Inc., Exhibits 1 through
10 14 were offered and admitted.)

11 CROSS-EXAMINATION

12 BY MR. PADILLA:

13 Q. Mr. Mean -- am I pronouncing your name correctly?

14 A. It's "Means" with an "s."

15 Q. Okay, sir, Means. At what time did you receive
16 Exhibit 14 yesterday?

17 A. I received a phone call about it from my boss at
18 4:00 -- probably between 4:00 and 4:30 p.m. this time.
19 And then received the actual signed copy of it from
20 Mr. Bruce at -- it was probably 6:30 or 7:00 p.m.

21 Q. So before that time, as I understand your
22 testimony, there is no way in the world that you could
23 have made a proposal to the Ard entities; is that right?
24 Is that fair to say?

25 A. Somewhat. We could have made a proposal, but we

1 risked being in breach of our contractual obligation.

2 We risked a breach of contract.

3 Q. What Oil Conservation Division rule or statute,
4 if you know, would prohibit you from making a proposal
5 in view of the operating agreement, paragraph 16 of the
6 operating agreement, that would preclude a proposal from
7 you to the Ard entities?

8 A. I would be unaware of an oil commission rule to
9 that effect.

10 Q. Now, you filed your application for your APD to
11 the BLM on June 27, 2014; is that correct?

12 A. Yes, sir, that's correct.

13 Q. Now, at that time did you know you had the
14 restriction under paragraph 16 of the operating JOA?

15 A. Well, to be honest with you, we've known the
16 provision has been in the operating agreement since it
17 was signed, so, yes, we knew or should have known about
18 it.

19 Q. And what was the date of the operating agreement?

20 A. The date of January 20, 2012.

21 Q. So to go on back even further, since that time,
22 you knew you had a restriction as to any well proposal
23 regarding the Ard interest?

24 A. That is true, except that for a good chunk of
25 that time, the interest was in a term assignment note.

1 Concho's interest, though, wasn't. Concho had that
2 interest by virtue of the term assignment.

3 Q. So in looking at Exhibit 1, on the second page,
4 I'll direct your attention to about a third of the page
5 down, where it says, dedicated acreage, 120, and then
6 there is a block entitled Consolidation Code; what does
7 that mean?

8 A. Sorry. Are you on Exhibit 1?

9 Q. Exhibit 1, the second page.

10 A. Page 2?

11 Q. Yes.

12 A. Consolidation code?

13 Q. Yes.

14 A. I am unsure. And it might have to do with the
15 allowable -- references that no allowable be assigned
16 until interests have been consolidated or nonstandard
17 unit's been approved.

18 Q. Do you think that also applies to whether or not
19 you had a joinder of all parties who had working
20 interests in this proposed well?

21 A. Well, I guess I am not following your question.
22 We have to apply for a nonstandard unit, so this was --
23 I'm not following the question. I am sorry.

24 Q. You don't know whether consolidation code means
25 you had obtained either a communitization agreement or

1 some other agreement, such as the JOA, to proceed with
2 drilling the well where everybody was already locked
3 into drilling the well?

4 A. We -- you're right. We did not have the Ard
5 interest committed to this well when we filed, and --

6 Q. What was it that you disclosed to the Ard
7 representatives or Mr. Ard that you had a problem with
8 under paragraph 16?

9 A. That probably was -- I mean, I would put that
10 sometime in August of this year. You know, we received,
11 actually received from Ard/COG copies of the
12 reassignments, the actual reassignments, in May of this
13 year.

14 And, in fact, to date, to the best of my
15 knowledge, those assignments have not been filed of
16 record. We have not been provided with recorded copies
17 of those assignments. So, you know, there is some
18 element that we had to seek out who -- whether or not
19 the interest was still subject to a term assignment.

20 And that was, in effect -- really our initial
21 conversations with Mr. Ard were to that effect. And
22 back in December was, Do you have the interest or does
23 Concho have the interest because we are going to need
24 the proposed wells.

25 Q. And you sought the reassignments in May of this

1 year, right?

2 A. Correct.

3 Q. And so in May of this year, you knew who had the
4 interest then, right?

5 A. Well, yes and no. We had reassignments that were
6 unrecorded and there was some conversation about,
7 because there is a Nosler 3 Well that's in here that was
8 drilled and never completed and needed to be T&A'd for
9 a number of reasons.

10 We were advised by the Ard group that acceptance
11 of those assignments was pending because they weren't
12 reassigned back to Concho in the same free of liens and
13 incumbrances, and that there was an issue there. So to
14 date, there has been some questions about exactly what
15 was reassigned and whether the assignments were accepted
16 by Ard.

17 But, yes, we did receive at least signed copies
18 from Concho of assignments of interest back into Ard in
19 May.

20 Q. So you have had a lot of communications, judging
21 from the e-mails, at least more than in some cases that
22 I have handled, but at no time did you make any
23 proposals, such as a term assignment that -- or a
24 variation of the term assignment that the Ards have with
25 Concho; is that correct? Hrrrr

1 A. We did not make a formal offer with a term
2 assignment to Ard, no. And that again is because -- and
3 I'll take the blame for it. We were negotiating down
4 the road with them and then kind of came to remember
5 this article 16-E. And at that point in time, we had to
6 tell them, Listen, we're prevented from dealing and now
7 we are seeking a solution to that which we did. And the
8 proof is there.

9 Q. Now, you did make the proposal that Ard sign a
10 joint operating agreement; and that's Exhibit 3, right?

11 A. Yes, sir.

12 Q. And let me direct your attention to paragraph 16
13 again. And there are some forfeiture provisions in
14 there. Does that paragraph 16, in any way, say that if
15 you do not participate in the first well, you would
16 forfeit the entire interest from the prospect area?

17 A. I can't remember. It may. Are you looking in
18 Article B or C?

19 It may have -- it may have a provision to that
20 effect. Those seem to be common these days. I'm not
21 seeing it here. If you could point it out to me, I will
22 confirm it, though.

23 It does say -- here you go, if you nonconsent to
24 first well, then you are out of any well in that spacing
25 unit.

1 MR. WADE: Can you point that out?

2 THE WITNESS: 16-B-2.

3 Q. So, in effect, what that is saying is you cannot
4 go nonconsent on the first well, right?

5 A. You can go nonconsent but you are just going to
6 be out of the spacing unit.

7 Q. But you lose your interest forever as I
8 understand this paragraph, right?

9 A. As to that spacing unit, yes.

10 The idea is just to incentivize people not to get
11 a free look at the first well; right? Because if you
12 nonconsent to the first well in the spacing unit and you
13 know there's going to be two wells -- or however many
14 wells -- just let them go take all the risk on the
15 first well, and, then, if it's good, we will participate
16 after.

17 Q. Let me ask you. Why did you propose two wells?
18 You have this and the second proposal in the other case.

19 A. We proposed two wells simply because those -- we
20 are going to have to drill a well in January to hold our
21 term assignments and then we have to spud a well 180
22 days from the RID release of that first well to hold
23 those term assignments.

24 And as a practical matter, getting APDs from the
25 BLM takes some time. There's -- we have all this

1 process and compulsory pooling. And it's just easier,
2 as a practical matter, to do two at a time, because then
3 we know next year our drilling set, our budget we can
4 handle, we know what we're going to do, we are going to
5 drill these two wells. And, then, if we have an issue
6 with one well, we can move over and drill the next well
7 and not have to worry about losing term assignments.

8 It's really just to manage our term assignment
9 risk, if you will.

10 Q. So you are looking out solely -- as I understand
11 that testimony, you're looking out solely for your
12 interest, not for Ard's interest, and here you are
13 pointing a gun at Ard --

14 MR. BRUCE: I object to that, Mr. Examiner.
15 That is inflammatory. You are not pointing a gun at
16 anyone.

17 MR. WADE: Rephrase the question.

18 Q. You're forcing Ard to accept only one proposal,
19 to join in this JOA?

20 A. That is the only proposal we made him. We asked
21 him to join the JOA, as everybody else has, and
22 participate in the well. I don't think it's fair to say
23 that's his only option. He could go out on the
24 Street -- there's only five or six parties to that
25 operating agreement of everybody in the universe.

1 That is a valuable interest. He could sell it on
2 the Street. There's a million non-op buyers out there
3 that would take the interest. And we tried to put him
4 in touch with one. We did our best there.

5 I think it's -- I think it's not my opinion -- in
6 my opinion, it is not the case that his only option is
7 to get forced pooled or participate in the well. Those
8 are two options in a sense.

9 Q. When you put him in touch with a third party, you
10 were essentially forcing him -- let me back up. You put
11 him in touch with Chase after you filed your application
12 for compulsory pooling, right?

13 A. It may have been after. I think it was at or
14 about the same time. Let me look at my timeline. The
15 timeline will likely say that.

16 MR. WADE: And the timeline is exhibit
17 number --

18 THE WITNESS: It's Exhibit 4.

19 A. So the e-mail from David Rhodes to Brad Bartek or
20 to Houston is dated September 25, and we filed these
21 applications on October the 13th, I believe -- yes. So
22 I think we gave them -- put them in touch prior to
23 filing the applications.

24 Q. Is Chase a party to the operating agreement?

25 A. They are now. At the time, they were not. In

1 September they were not, but as of October 1; now
2 they are. Chase did buy an interest in this area and is
3 now a party to the operating agreement, which did
4 create a problem with them pursuing the interest
5 further.

6 Q. Ultimately, they had the same problem you did,
7 right?

8 A. Well, ultimately, yes. After they signed, they
9 did. But prior to signing, I don't think they were
10 subject to it.

11 Q. So once they signed, this was not a viable
12 option?

13 A. That's true. I would say that's true. It wasn't
14 a viable option, but it was an effort, which seems to be
15 what's required.

16 Q. Well, you still didn't have -- you still had the
17 contractual restriction, correct?

18 A. That's correct.

19 Q. So all the talk in the world wouldn't have made
20 any difference unless you got the waiver like you got it
21 yesterday?

22 A. That's correct. And we endeavored pretty hard to
23 get that. I think if you look at the letter and the
24 subsequent letter we sent Concho, we made a very
25 diligent effort to get that.

1 Q. But you agree with me that has nothing to do with
2 Ard?

3 A. Well --

4 Q. The contractual agreement between Burnett and COG
5 had nothing to do with Ard, realistically, because
6 they're not a party to the JOA, correct?

7 A. In a sense, yes. I mean, it doesn't affect Ard
8 in a sense, yes, as they are not a party to the
9 operating agreement. But it limits our ability to deal
10 with Ard, because we have this provision and it exists.

11 Q. And it also limits Ard's ability to go to any of
12 the interest owners other than COG and make a deal with
13 them, right?

14 A. That's correct. Just the five or six other
15 parties to that operating agreement, it limits their
16 ability. It doesn't limit it with respect to COG or
17 anybody else.

18 Q. Would somebody else be compelled to then sign the
19 joint operating agreement?

20 A. Well, no one would be compelled to if they bought
21 the working interest. Yes, it's likely that we would
22 send them the operating agreement, saying, Here's the
23 operating agreement -- I mean, in the normal course of
24 things someone may buy an interest and say, I am not
25 going to join that operating agreement, but I will join

1 something else. And, you know, it's a negotiation with
2 the deal.

3 But, very likely, yes, if someone bought the
4 interest from Ard, they would be asked to sign that
5 operating agreement. And that's -- we can't compel them
6 to sign it, but, yes, they would probably be asked to
7 sign it. Because it just makes life easier when
8 everybody is under an operating agreement.

9 Q. Would Ard be able to renegotiate the terms of
10 paragraph 16 if they joined this well?

11 A. Well, there would be no need to now. Now that
12 everybody in the operating agreement has agreed to
13 delete it, what we intend to do next week is basically
14 send an amended operating agreement out with the
15 provision to delete it.

16 So I think if Ard -- we'd love for him to join
17 this operating agreement. There'd be no need to
18 renegotiate it. It's gone.

19 Q. Before yesterday, would Ard have been able to
20 renegotiate the terms of paragraph 16?

21 A. Yes. If we never -- we sent the operating
22 agreement to Ard and asked them to join it; we never
23 received any communication back with respect to it at
24 all. We didn't call back and say, I won't sign this but
25 I will sign this. Will you do this? Here's my

1 suggested red line. Nothing to that effect.

2 As a matter of course, we propose operating
3 agreements all the time and take suggestions and people
4 have issues with any number of things. And we, as a
5 practical matter, will always entertain those offers
6 because, like I say, at the end of the day, if he just
7 has a couple of issues with it, we might do a side
8 letter agreement, saying, With regard to Ard, provision
9 A, B, C, and D do not apply; signed, sealed, and
10 delivered and we have a deal.

11 So I would say, yes, he would have been able to
12 renegotiate 16-E. However, as that party has pointed
13 out before this, I don't know how that provision applies
14 with respect to Ard itself.

15 So as far as Ard finding it in that provision, it
16 seems like that that provision as to Ard is a moot
17 point.

18 Q. You are telling us here today that you negotiated
19 in good faith. And the fact is that you could not
20 negotiate at all other than having Ard sign this JOA,
21 correct?

22 A. No. It would have been hard to get around that
23 provision, because it says no one can take an
24 assignment. So the fact of the idea that we enter into
25 an operating agreement where Ard goes out in the

1 override was Ard's idea.

2 And we went down that road with them and said
3 that's definitely something we'd entertain, which is a
4 sweet deal for them. And we were going to entertain
5 that. And then we had to check the horse on that
6 because we had this provision. There is no way to get
7 around that at some point in time, in that arrangement,
8 the interest has to transfer.

9 Q. Wouldn't COG have had to be a signatory party to
10 any amendment regarding the provisions of paragraph
11 16-E?

12 A. Yes.

13 Q. And you didn't get that until yesterday, correct?

14 A. That's correct.

15 MR. PADILLA: That's all I have.

16 EXAMINER JONES: Okay. Do you want to say
17 anything else?

18 MR. BRUCE: Yes. I would like to ask a
19 couple of questions.

20 REDIRECT EXAMINATION

21 BY MR. BRUCE:

22 Q. Mr. Means, Mr. Padilla said you made no proposal.
23 You sent a well proposal with an AFE regarding this well
24 to the Ards?

25 A. We did.

1 Q. That's a proposal?

2 A. That's a proposal; we asked them to join in the
3 well.

4 Q. Under the current situation or the situation as
5 it existed before yesterday, did you do everything you
6 could to try to get the Ards committed to this well?

7 A. I think the evidence says absolutely.

8 Q. And when Burnett is drilling a well, is it under
9 any obligation -- let's say, Burnett -- forget the Ards
10 -- Burnett is contacting Apache or Cimarex or any other
11 company that operates out here, are you under an
12 obligation to take a farmout from someone or to take a
13 term assignment from someone?

14 A. No.

15 Q. You could just say, Send a letter, a well
16 proposal, an AFE, please join in the well?

17 A. Yes.

18 Q. And if they didn't want to join in, you could
19 force pool them?

20 A. Exactly.

21 Q. Do you believe that Burnett went far and above
22 that in order to get the Ards committed to this well?

23 A. We did. We made a hard effort at it and did all
24 we could.

25 Q. Mr. Padilla also mentioned renegotiating the

1 JOA -- the Ard interest is a working interest under a
2 federal lease; is that correct?

3 A. Yes, it is.

4 Q. Once the term assignment ended as to this.
5 particular well unit, they could have contacted all the
6 working interest owners under the JOA and negotiated
7 changes, could they?

8 A. They could have. They could have -- in fact,
9 they could have contacted COG of their own accord and
10 asked them to delete the provision.

11 Q. Do you know if they did?

12 A. I do not.

13 Q. And one final thing, as far as filing the APD,
14 does Burnett own an interest in every quarter, quarter
15 section in the well unit?

16 A. We do. It does.

17 Q. Thank you.

18 MR. BRUCE: That's all.

19 EXAMINATION BY EXAMINER JONES

20 EXAMINER JONES: I was going to ask about
21 that also. The tract ownership in the 120, Burnett owns
22 an interest in each of the 40s, but is it a standard
23 section?

24 THE WITNESS: It is. So for the 4H only,
25 the northwest, northwest 40 was earned in the term

1 assignment between -- Concho earned that. So COG has
2 the -- Ard has a 10.83438 percent interest. So Concho
3 earned that in the 40. So Ard's interest in this well
4 is going to be 80 over 120 of 10.83438 percent. So they
5 have two thirds of the unit.

6 EXAMINER JONES: Okay. And what about the
7 other 40s? Who owns those? This is all federal -- is
8 that correct? -- one federal lease?

9 THE WITNESS: This is one federal lease,
10 correct.

11 EXAMINER JONES: So the ownership of the --

12 THE WITNESS: The ownership is common in the
13 three 40s with the exception of -- there's the 10.8
14 percent that Ard owns in two 40s and then Concho owns in
15 one 40. Outside of that, the ownership is common.

16 EXAMINER JONES: Oh, I see. So Concho still
17 owns the northwest, northwest.

18 THE WITNESS: Yes. And Concho has
19 non-consented this well. But they are under the
20 operating agreement for the interest they have in the
21 northwest, northwest quarter.

22 EXAMINER JONES: They have non-consented
23 this well?

24 THE WITNESS: Yes.

25 EXAMINER JONES: But they are under an

1 operating agreement?

2 THE WITNESS: Yes.

3 EXAMINER JONES: So they signed a JOA, but
4 they still need to be pooled?

5 THE WITNESS: No. Their interest is subject
6 to the operating agreement.

7 EXAMINER JONES: So you are not asking them
8 to pool their interest?

9 THE WITNESS: No. They will just go out on
10 the non-consent penalty.

11 EXAMINER JONES: That makes sense. And so
12 the JOA is similar; it's sixty-five-hundred, six-fifty?

13 THE WITNESS: Yes, sir.

14 EXAMINER JONES: And Ard Oil versus Ard
15 Energy Group, Ltd., is that two different entities or is
16 it one entity?

17 THE WITNESS: That is two different
18 entities -- and it is two different entities. And there
19 is actually an e-mail in here that has the breakdown.
20 One them owns a bigger piece than the other.

21 EXAMINER JONES: But both of them need to be
22 pooled?

23 THE WITNESS: Yes.

24 EXAMINER JONES: If it goes that far?

25 THE WITNESS: Yes. They are distinct

1 entities with different percentages, but both need to be
2 pooled.

3 EXAMINER JONES: And the notice for the
4 nonstandard project area, as far as noticing that
5 northeast, northeast, COG owns that; is that correct?

6 THE WITNESS: Yes, sir, the northeast,
7 northeast is COG.

8 EXAMINER JONES: And you said they have two
9 horizontal wells; did they already drill there?

10 THE WITNESS: They have two horizontal Yeso
11 wells in the east half, east half of --

12 EXAMINER JONES: North, southwest?

13 THE WITNESS: North, south --

14 EXAMINER JONES: But you guys are drilling
15 east, west.

16 THE WITNESS: Yes, sir.

17 EXAMINER JONES: And you got another witness
18 for that?

19 THE WITNESS: I would be happy to answer
20 that, but he is going to do a lot better job.

21 EXAMINER JONES: Okay. And the COG/Ard
22 relationship, when did it fall apart and why did it fall
23 apart?

24 THE WITNESS: Well, I would not say that
25 their relationship fell apart. The term assignment fell

1 apart. And that happened -- if I recall the effective
2 date of the assignment from COG back to Ard is
3 October 13, 2013.

4 And that's probably based on the day of the
5 continuous development provision in that lapsed in the
6 term assignment lapse. And this is a lot of moving
7 parts.

8 But there were -- they could receive
9 credit -- because the term assignment was predispute,
10 they could receive credit for anything Burnett drilled
11 and Burnett could receive credit under its term
12 assignment for anything that Concho drilled.

13 So I believe that term assignment expired in
14 October of 2013. And then there was a very extended
15 delay in the reassignments coming out of that. Like I
16 say, we didn't see them until May of this year.

17 EXAMINER JONES: Okay. So May until now is
18 when you tried to get participation from Ard; is that
19 correct?

20 THE WITNESS: That's correct. I mean, we
21 really began discussing this with Ard -- our first
22 meeting about Maljamar needing to deal with his interest
23 and we are going to drill wells was in January of last
24 year, January 9th.

25 And in that timeline, there are some

1 different things. I mean, we really started discussing
2 with Houston in August of this year.

3 EXAMINER JONES: Do you have any questions?

4 MR. WADE: I don't.

5 EXAMINER JONES: Thank you very much.

6 THE WITNESS: Thank you.

7 RAFAEL ZELAYA

8 having been first duly sworn, was examined and testified
9 as follows:

10 DIRECT EXAMINATION

11 BY MR. BRUCE:

12 Q. Would you please state your name for the record?

13 A. My name is Rafael Zelaya.

14 Q. And where do you reside?

15 A. Fort Worth, Texas.

16 Q. Who do you work for and in what capacity?

17 A. I work for Burnett Oil Co., Inc., and I am a
18 geological manager.

19 Q. Have you previously testified before the
20 Division?

21 A. No, sir.

22 Q. Could you describe for the Examiner your
23 educational and employment background.

24 A. I graduated from TCU, Texas Christian University,
25 with a bachelor's of science in geology. And I went on

1 to work for XTL Energy as a staff geologist in Fort
2 Worth.

3 And then moved to Houston to work for Gas Star
4 Exploration as a senior geologist. And I moved back to
5 Fort Worth to work with Terrace Energy as a VP of
6 geology.

7 And then I have been with Burnett as a geologist
8 for two years.

9 Q. When did you graduate from TCU?

10 A. In 2003.

11 Q. Does your area of responsibility at Burnett
12 include this portion of southeast New Mexico?

13 A. Yes, it does.

14 Q. And are you familiar with the geology involved in
15 this application?

16 A. Very familiar.

17 MR. BRUCE: Mr. Examiner, I tender
18 Mr. Zelaya as an expert petroleum geologist.

19 EXAMINER JONES: Any objections?

20 MR. PADILLA: No. I don't want to
21 mispronounce your name. How do you spell it?

22 THE WITNESS: Zelaya, Z-e-l-a-y-a.

23 MR. PADILLA: Thank you.

24 EXAMINER JONES: Mr. Zelaya is qualified in
25 geology.

1 Q. Could you identify Exhibit A for the Examiner?

2 A. Mr. Examiner, Exhibit A is a topo map showing the
3 Nosler 12 Federal DD 4H location, highlighted in the top
4 part of this page. In essence, this is just showing any
5 surface expressions or any risks that may show up on the
6 surface.

7 As you can see towards the toe of the well,
8 towards section B, there is the Taylor Draw on there.
9 But other than that, there is really not much going on
10 in the area.

11 Q. And what is Exhibit B?

12 A. Exhibit B is to just clarify some of those
13 habitat and exclusion areas. The highlighted section in
14 the brown are sand dune, lizard habitats. And then the
15 buffered blue is the buffer around that Taylor Draw.

16 Q. And because of these issues, their locations can
17 be difficult to obtain?

18 A. That is correct.

19 Q. Now, Mr. Means said the surface location is in
20 the offsetting section 11. Was that done to maximize
21 the horizontal length -- the producing interval of the
22 horizontal wellbore?

23 A. Yes, sir.

24 Q. If you had located that in the northwest,
25 northwest quarter of section 12, would you have lost a

1 substantial chunk of footage?

2 A. Yes, sir. Approximately, 700 feet of lateral.

3 Q. What is Exhibit C?

4 A. It is the top of Paddock structure map. And if
5 you reference sections B, C, and D, highlighting the
6 lateral for the No. 4H, you can see a gentle dip from
7 subC value 1,300 on average down to 1,270. It is a very
8 gentle dip, not much change going on from west to east.

9 Q. So the structure in this well is relatively
10 unimportant?

11 A. That is correct.

12 Q. And what is Exhibit D?

13 A. Exhibit D is the base of the Paddock porosity.
14 Again, it shows a very gentle dip, not much change. And
15 it shows that there are very little geologic risks in
16 drilling those wells.

17 Q. Are there any faults or anything that would
18 impede the drilling of this well?

19 A. No, sir.

20 Q. What is Exhibit E?

21 A. Exhibit E is the Paddock porosity greater than
22 two to three percent. And that little range there is
23 based off of new and old logs. So we just included a
24 small little range there.

25 And you can see in the lateral, it ranges between

1 150 to almost 200 feet.

2 Q. And can you discuss the cross section, Exhibit F.

3 A. Yes, sir.

4 Mr. Examiner, the cross section in Exhibit F
5 shows that lateral for the 4H with the Partition Federal
6 No. 1 being projected into that lateral.

7 The reason I chose the Partition Federal 1 is
8 because we have an IP within the targeted interval that
9 was about 40 barrels a day.

10 Q. You stated that the target reservoir is fairly
11 uniform in porosity, lateral and for the wellbore?

12 A. That is correct. And the isopach that we
13 previously showed shows that consistency.

14 Q. In your opinion, will each quarter, quarter
15 section in the well unit contribute more or less equally
16 to production?

17 A. Yes, sir.

18 Q. Why are you doing a lay-down well rather than a
19 stand-up well?

20 A. Our engineering department took a closer look at
21 all of the offset operators and has come to a conclusion
22 that the west to east laterals have a higher production.

23 Q. Higher productivity than the stand-ups?

24 A. Yes, sir.

25 Q. And, finally, a last couple of exhibits. What is

1 Exhibit G?

2 A. Exhibit G is the directional plan that we have
3 submitted with the permit showing the plan lateral,
4 kick-off, building the curve, and then drilling this
5 well, toe-up at half a degree.

6 Q. How many completion stages will there be?

7 A. Roughly 13 stages, spaced 250 feet apart.

8 Q. And what will the fracking process consist of,
9 volumes?

10 A. About 5,000 barrels a stage.

11 Q. So, finally, Exhibit H, what does Exhibit H
12 reflect?

13 A. Exhibit H reflects our attempt to negotiate with
14 COG regarding our proposed surface locations. I think
15 initially there was some information saying or relating
16 to COG potentially opposing our surface locations. And
17 this is our attempt to provide them surface locations on
18 our acreage.

19 Q. Were Exhibits A through H prepared by you or
20 under your direction and compiled with company records?

21 A. Yes, sir.

22 Q. And, in your opinion, is the granting of this
23 application in the interests of conservation and the
24 prevention of waste?

25 A. That is correct.

1 MR. BRUCE: Mr. Examiner, I move the
2 admission of Burnett Exhibits A through H.

3 EXAMINER JONES: Any objection?

4 MR. PADILLA: No objection.

5 EXAMINER JONES: Exhibits A through H are
6 admitted.

7 (Burnett Oil Co., Inc., Exhibits A through H
8 were offered and admitted.)

9 MR. BRUCE: I pass the witness.

10 CROSS-EXAMINATION

11 BY MR. PADILLA:

12 Q. Mr. Zelaya, do you know why COG went non-consent
13 on drilling these two wells?

14 A. I do not. That would fall in Mr. Means'
15 category.

16 Q. In your discussions with COG as to the geology,
17 were there any discussions about drilling east, west or
18 north, south?

19 A. Not to my knowledge, no, sir.

20 Q. All of the COG wells shown on Exhibit A are
21 north, south, correct?

22 A. That is correct.

23 Q. And what kind of production do those wells have?

24 A. I do not know the details about those -- about
25 the production in those. But as I mentioned earlier,

1 our engineers have analyzed that and have gone to
2 comparisons versus the east, west and the north, south
3 wells. I believe that orientation was mainly dictated
4 based off the acreage that they had at that point in
5 time.

6 Q. How many wells has Burnett drilled in this area,
7 horizontal wells?

8 A. Horizontal wells? We drilled numerous horizontal
9 wells to the west of Maljamar of this acreage here.

10 Q. The same formation?

11 A. Similar intervals.

12 Q. What is the interval that you are encountering or
13 that you are proposing to encounter in your two wells?

14 A. This would be the Paddock, which is the upper
15 portion of the Yeso formation.

16 Q. Have you drilled any Paddock wells in the
17 immediate area?

18 A. Not in this immediate area, no, sir.

19 Q. How far away would you say are the other wells
20 that you drilled, Paddock wells, how far away are they?

21 A. I do not recall having any Paddock wells.

22 Q. So you haven't drilled any Paddock wells?

23 A. Not in this area, no, sir.

24 Q. Have you performed any stress orientation or
25 modeling studies prior to drilling these wells?

1 A. We have a series of logs. We've looked at FMIs
2 that we have run in some of the vertical wells. And
3 they show very little orientation. It's a non-preferred
4 orientation. It is more like a shattered glass at this
5 point. So there is, from that information, no, nothing
6 that we can glean to orient these wells.

7 Q. What you're telling us here today is that you
8 know how the COG wells are any good?

9 A. We have done the comparisons on the production,
10 yes, sir.

11 Q. How have you made the comparison?

12 A. We have taken the production that has been
13 reported to the state for all the north, south ones and
14 compared the same production for the wells that are
15 drilled to the east and west.

16 Q. What would you say the proportion of north, south
17 wells to east, west wells is in the area?

18 A. I would say that there are more west to east
19 wells than there are north, south wells.

20 Q. Have you met with COG and discussed the geologic
21 features of this area or the engineering aspects that
22 you are relating to?

23 A. I have not, no sir.

24 Q. Do you know whether anyone at Burnett has met
25 with COG to discuss the favorability of drilling east,

1 west or north, south wells here?

2 A. I believe we've discussed with them, but I am not
3 sure if we have gone over the geology with them.

4 Q. When did you -- well, when did you have
5 engineering talks as to the favorability of drilling
6 east, west or north, south?

7 A. Throughout the whole life of this project. I
8 think we have been watching it and just trying to keep a
9 close eye on what offset operators have been doing.

10 Q. But to this point, you haven't drilled any wells?

11 A. Not in this area.

12 MR. PADILLA: That's all I have.

13 EXAMINER JONES: Mr. Bruce.

14 MR. BRUCE: Just a couple of follow-up
15 questions.

16 REDIRECT EXAMINATION.

17 BY MR. BRUCE:

18 Q. Mr. Zelaya, Burnett has drilled a number of
19 vertical Yeso wells in this area, correct?

20 A. That is correct.

21 Q. And has conducted extensive testing on those
22 wells?

23 A. That is correct.

24 Q. Has COG drilled lay-down Yeso wells in this area
25 and outside of this area?

1 A. Yes, sir.

2 Q. There's an area west of here, Loco Hills. Are
3 there some decent lay-down Yeso wells in that area?

4 A. That is correct, yes, sir.

5 Q. About two miles away?

6 A. Yes, sir.

7 Q. And you mentioned engineering studies. The
8 engineers are determining the performance of horizontal
9 wells north, south versus east, west?

10 A. Yes, sir.

11 Q. And Burnett has been in this entire area for
12 decades, has it not?

13 A. That is correct.

14 Q. And drilling a lot of the Yeso wells over the
15 years?

16 A. That is correct.

17 Q. And has substantial experience in this area?

18 A. That is correct.

19 MR. BRUCE: Thank you, Mr. Examiner.

20 EXAMINATION BY EXAMINER JONES

21 EXAMINER JONES: Is the Yeso, the whole Yeso
22 written off except for this Paddock zone? Are there any
23 other wells completed within a mile or so in the Yeso
24 below the Paddock?

25 THE WITNESS: Yes, sir.

1 EXAMINER JONES: What zones?

2 THE WITNESS: That would be the Blinebry,
3 the lower portion of the Yeso.

4 EXAMINER JONES: The top Blinebry?

5 THE WITNESS: Actually, it is a good
6 majority of the Blinebry. It is a fairly thick
7 interval.

8 EXAMINER JONES: Are you looking at that in
9 the future also?

10 THE WITNESS: Yes, sir. And there have been
11 horizontals that have been drilled in the Blinebry.

12 EXAMINER JONES: The control you had for all
13 these nice maps, the wells that you spotted on here, are
14 those the control?

15 THE WITNESS: Yes, sir. The control points
16 are the ones that have the -- it's a green color beneath
17 the well location.

18 EXAMINER JONES: Okay. I don't have any
19 more questions.

20 MR. WADE: No questions.

21 EXAMINER JONES: Thank you very much.

22 MR. BRUCE: I have nothing further in this
23 case, Mr. Examiner.

24 MR. PADILLA: I have one witness. I call
25 Houston Kauffman.

1 HOUSTON KAUFFMAN

2 having been first duly sworn, was examined and testified
3 as follows:

4 DIRECT EXAMINATION

5 BY MR. PADILLA:

6 Q. Please state your full name.

7 A. Houston John Kauffman.

8 Q. Mr. Kauffman, where do you live?

9 A. Fort Worth, Texas.

10 Q. And what is your relationship to the Ard entities
11 involved in this case?

12 A. I am a consulting landman.

13 Q. Have you ever testified before the Oil
14 Conservation Division and had your credentials accepted
15 as a matter of record as a landman?

16 A. No.

17 Q. Tell us when and where you obtained your college
18 degree.

19 A. I have an undergraduate degree in petroleum land
20 management from the University of Texas, 1978; a
21 master's of business administration from Houston Baptist
22 University in 1989.

23 Q. What has been your experience in the oil and gas
24 industry as a landman?

25 A. Twelve and a half years with Amoco Production

1 Company in Houston and Midland. Four years with
2 C and G Producing Company in New Orleans.

3 Eight years with Mercury Exploration and Quick
4 Silver Resources. Since 2003, I've been a part-time
5 consultant.

6 Q. Are you familiar with the land position of the
7 parties in this case?

8 A. I didn't hear you. I'm sorry.

9 Q. Are you familiar with the land position of the
10 parties in this case?

11 A. Yes.

12 MR. PADILLA: I tender Mr. Kauffman as an
13 expert in petroleum land matters.

14 MR. BRUCE: No objection.

15 EXAMINER JONES: He is so qualified.

16 Q. Mr. Kauffman, you have heard the testimony of
17 Mr. Means in this case. And I don't want to belabor
18 this case in trying to refute or somehow appear to want
19 to disprove what Mr. Means said.

20 But in terms of -- I want to ask what your
21 opinion is in terms of whether or not there has been
22 good faith negotiations conducted by Burnett as the
23 operator of this well with regard to the Ard interests?

24 A. Up until September 21st, when I believe it was,
25 of this year, when Mr. Rhodes had sent me an e-mail

1 requesting -- I think that is in the timeline that has
2 been presented -- Mr. Rhodes had sent me an e-mail
3 asking to get on the phone.

4 At that point, I was advised by Mr. Rhodes and
5 Mr. Means that they had this restrictive language in
6 this operating agreement and that as such they had put
7 it in terms of, We're wondering if there is something
8 you could do to help us, either with getting a waiver of
9 that provision from Concho or if there's some other way
10 to work around that.

11 I do believe there's an e-mail in there that
12 indicates that I requested from Mr. Means -- which he
13 complied with that request on September 24th -- he
14 provided me with a copy of that operating agreement,
15 which I read that article 16 language.

16 And the next day I met with Mr. Means and
17 Mr. Rhodes for lunch. And I suggested a number of
18 potential remedies as to how they addressed that
19 provision, starting with my question about whether or
20 not that provision was even enforceable because it was a
21 restriction on trade.

22 I had showed that provision to my wife, who is an
23 oil and gas attorney. That was the first thing she said
24 when she saw it. Both myself and my wife were looking
25 at it, trying to figure out a way to legally circumvent

1 that provision, was there some way we could parse words
2 and make a third-party deal or something to go around
3 that provision.

4 I discussed that with Mr. Rhodes and Mr. Means at
5 lunch, were they willing to go that far. They had
6 indicated that -- as Mr. Means testified earlier --
7 there had been quite contentious relations in this area
8 between Burnett and Concho and that they knew -- they
9 felt fairly certain that Concho would resist any efforts
10 to either waive this provision or allow Burnett -- it
11 was in that meeting that they -- that Mr. Rhodes and
12 Mr. Means suggested that I get in touch with a
13 representative of Chase, which they provided me with
14 that contact information.

15 I did contact that party. I explained to them in
16 general the type of terms that we were trying to -- that
17 I thought that Mr. Ard would be agreeable to. They were
18 not forthcoming with an offer.

19 I contacted some other parties. But I believe
20 that in contacting those other parties, when I tell them
21 that -- the more likely parties to take an interest in
22 this, first and foremost being the operator and,
23 secondarily, parties that are already a party to the
24 agreement, that they had restricted themselves, which I
25 believe puts Mr. Ard at a negotiating disadvantage.

1 And I will further go on and say that insofar as
2 Burnett was restricted, they have certainly been
3 cooperative. They had hoped that they could get this
4 waiver that they eventually got.

5 I think that they intend on proceeding with good
6 faith negotiations. They have just been restricted from
7 doing so up until now. And as such, because they
8 voluntarily restricted themselves from those good faith
9 negotiations by virtue of this agreement, I don't think
10 they should enjoy the benefits of being able to come
11 here and get compulsory pooling relief.

12 Q. When did you learn of the COG waiver of
13 paragraph 16?

14 A. Actually, I received a text message from Chase's
15 representative yesterday evening. It hit my phone about
16 5:40, I believe. And I didn't see it until about an
17 hour later.

18 But they said that Burnett had received this
19 waiver. And the nature of the text said, So now we can
20 talk to you.

21 And, by the way, at least the text offer was for
22 a pay 1 percent override in lieu of participation.

23 Q. Let me ask you, Mr. Kauffman, what options did
24 Ard have? You have already mentioned a couple, to sell
25 to a third party that's not subject to the agreement or

1 to join the well straight up by assigning the joint
2 operating agreement. Is that --

3 A. Correct. The option presented by Burnett was to
4 participate and join in that operating agreement or
5 compelled Mr. Ard that if you didn't want to participate
6 yet, receive some value out of -- out of his 10.8
7 percent ownership and most of this acreage in this area.
8 He'd be compelled to go to a third party and negotiate
9 and then that third party would then be compelled to go
10 and negotiate with the operator.

11 Q. So what is your experience in all the time you
12 have been a landman in participating in negotiations for
13 participation in a well, how do those go about?

14 I take it they happened sort of the way this
15 happened. But at some point, does the operator have the
16 ability to -- the proposed operator to negotiate
17 something?

18 A. Yes. The operator under normal circumstances has
19 the ability, in most states, to offer alternatives that,
20 in my experience, offer similar economic benefits to the
21 co-owner with some consideration given to the fact that
22 if the co-owner is not participating in the well and not
23 taking the geologic risk and not taking the drilling
24 risk, the mechanical risk, that he would not receive as
25 much in a farmout-type scenario as he would receive if

1 he would participate.

2 Q. Did you have a chance to get into any of this
3 kind of negotiation in this case?

4 A. Beginning September 21st, when Burnett advised me
5 that they were quite restricted in that with regard to
6 this operating agreement, no.

7 But as Mr. Means had testified earlier, they
8 had -- in mid-August they had contacted Mr. Ard and
9 wanted to open that discussion and that discussion was
10 going on, as I think the e-mails will indicate, that
11 discussion was going on up until that point, at which
12 point they advised me they needed to truncate those
13 discussions, but they could not, in any form, take an
14 assignment from Mr. Ard and were not willing to
15 challenge the provision, were not willing to try some
16 work-around.

17 Q. In terms of paragraph 16, would you advise
18 Mr. Ard to accept those terms?

19 A. Would I have advised him to accept those terms?

20 Q. Yes.

21 A. Absolutely not. As I mentioned to Mr. Means, I
22 don't know how Mr. Ard could in any way ratify that.

23 MR. PADILLA: That's all I have. I pass the
24 witness.

25 EXAMINER JONES: Mr. Bruce.

1 CROSS-EXAMINATION

2 BY MR. BRUCE:

3 Q. Just a few, Mr. Kauffman.

4 With this provision, if Burnett had made some
5 farmout or term assignment offer, they could have been
6 buying into a lawsuit with COG, correct?

7 A. Burnett could have been, yes.

8 Q. Did the Ards or you on their behalf ever seek to
9 renegotiate the JOA with COG?

10 A. No.

11 Q. As a working interest owner, the Ards could have?

12 A. We do not have standing in that contract, and it
13 didn't -- it had been discussed with them, yes.

14 Q. You could have contacted COG and asked them to
15 waive that provision so that you could negotiate with
16 others?

17 A. Yes.

18 Q. But you didn't?

19 A. But we didn't. Clearly, in my opinion, Concho
20 had that provision in there for their benefit, and I
21 would have presumed that there would have been some quid
22 pro quo on Concho's part. Had I asked them to waive a
23 provision, I would have then expected them to come back
24 and say, Well, we'll waive it if -- if you give us a
25 piece of it, if whatever. I think it is reasonable of

1 me to have expected that would have been the response.

2 Q. But all things considered is there anything else
3 Burnett could have done that it has not done, especially
4 considering the fact it finally has obtained the waiver
5 of that provision?

6 A. Yes. They could have offered Concho
7 consideration to waive that provision. They could have
8 challenged that provision. They could have taken the
9 risk that some type of third party work-around might
10 have worked out.

11 But I will repeat what I said. Insofar as they
12 explained that they were confined and that they could
13 not and would not, for fear of lawsuit from Concho, that
14 they would not go down that path, it left Ard with
15 little option.

16 Q. And the lawsuit would have taken quite some time
17 to resolve, would it not?

18 A. Undoubtedly.

19 Q. So they'd be in limbo till then?

20 A. Yes, it would.

21 Q. And they might lose their other term assignments
22 if that occurred?

23 A. Yes, they would.

24 MR. BRUCE: Thank you. That's all.

25 EXAMINER JONES: Redirect?

1 MR. PADILLA: Yes.

2 REDIRECT EXAMINATION

3 BY MR. PADILLA:

4 Q. Mr. Kauffman, was it up to the operator or to Ard
5 to renegotiate with COG?

6 A. No. And I'll throw out to the Division that in
7 my opinion there is a potential precedent here, in
8 that -- let's say that Apache and Devon are in an area
9 and Mac is a co-owner and Devon is going to operate a
10 well. And Devon and Apache get together and say, We are
11 not going to negotiate with Chase, but we are going to
12 go to the Division and force pooling.

13 They can get together and voluntarily agree that
14 they are not going to negotiate in good faith. I've
15 got -- the Ards nor anyone else has any assurance that
16 parties will not voluntarily enter into those types of
17 agreements, yet come here and plead the benefits of
18 compulsory pooling.

19 MR. PADILLA: Nothing further.

20 EXAMINATION BY EXAMINER JONES

21 EXAMINER JONES: Does Ard want this well to
22 be drilled?

23 THE WITNESS: Yes.

24 EXAMINER JONES: Are you working for both
25 Ard entities here?

1 THE WITNESS: Yes, I am. It's a complicated
2 structure that I am not quite sure I understand for the
3 record.

4 EXAMINER JONES: But they are interested in
5 participating?

6 THE WITNESS: They are interested in
7 participating or working out some type of reasonable
8 farmout arrangement in lieu of participation.

9 And I discussed that, once again, with
10 Mr. Coley first thing this morning in the hallway and
11 told him that I would certainly recommend to Mr. Ard
12 that we try to get together next week and to do that.

13 That having been said, I do believe that if
14 Mr. Ard does have -- if there is a compulsory pooling on
15 this, it puts him at a disadvantage in that negotiation.
16 And he will have a 30-day -- once the order is issued,
17 he will only have 30 days to either negotiate, go find a
18 third party to negotiate what he feels like is a fair
19 deal with Burnett or find a third party and/or gather
20 the money to participate, if he wants to, if he would
21 like to participate, where he has not, up until this
22 morning, has not had the opportunity to negotiate in
23 good faith with Burnett.

24 EXAMINER JONES: He hasn't had the
25 opportunity until this morning to negotiate?

1 THE WITNESS: Excuse me. Burnett made it
2 clear that they could not negotiate with Mr. Ard until
3 this morning.

4 I attempted negotiations. They made it
5 clear that they were restricted by this agreement that
6 they entered into with Concho not to deal with Mr. Ard,
7 which was just waived as Mr. Means said -- was just
8 waived yesterday afternoon around 4:00 or 5:00 or
9 whenever. So up until that point, Burnett did not have
10 the ability to negotiate in good faith with Mr. Ard.

11 EXAMINER JONES: Okay. I don't have any
12 more questions.

13 MR. WADE: I don't think I have questions
14 for the witness. I do have some questions for Mr. Bruce
15 or maybe one of Mr. Bruce's witnesses. Because at the
16 very onset of the hearing, you said the reason you're
17 going to go forward with the compulsory pooling was a
18 time constraint; is that right?

19 MR. BRUCE: Mr. Means testified that term
20 assignment or assignments are expiring in January --

21 MR. WADE: I couldn't recall the exact date,
22 so January --

23 MR. BRUCE: January 23.

24 MR. WADE: All right.

25 EXAMINER JONES: Off the record.

1 (Brief recess.)

2 EXAMINER JONES: Okay. Let's go back on the
3 record.

4 MR. WADE: We feel that based on the
5 evidence that was presented that allowing the
6 opportunity for the parties to have three more weeks of
7 discussion would be beneficial.

8 MR. BRUCE: And I agree, Mr. Examiner. My
9 landman and I were just discussing that, and we have
10 absolutely no objection to that. They intend to meet
11 with Ards or Mr. Kauffman next week. They intend to
12 make an offer. Whether or not they negotiate it
13 successfully is fine, but we have absolutely no
14 objection to that.

15 MR. WADE: And I think it will be
16 worthwhile, for the record, that whatever
17 negotiations -- if they're unsuccessful, to come back
18 and put that on the record again. So be prepared to
19 present more evidence, if needed.

20 MR. PADILLA: We don't have a problem with
21 that.

22 EXAMINER JONES: So case 15404 is continued
23 to December the 3rd.

24 MR. WADE: And then what do you anticipate
25 as far as your next case, how long your direct would

1 last?

2 MR. BRUCE: All I am going to do is put on
3 Mr. Means to identify exhibits -- let me make sure I got
4 the right numbers -- Exhibits 2 through 11 and 14 are
5 common to both cases. And I am going to give another
6 set of those to the court reporter so she has those for
7 the next case file.

8 Mr. Means is just going to testify about the
9 APD for the second well and the notice. And I'll put up
10 Mr. Zelaya. He will submit exhibits, which are
11 virtually identical to the ones submitted before, to
12 confirm his prior testimony and ask that it be
13 incorporated.

14 We do have one additional exhibit, which we
15 would like to submit, just showing the horizontal wells
16 in this area.

17 EXAMINER JONES: You don't want to continue
18 this case for three more weeks also?

19 MR. BRUCE: Both of them is fine. But I
20 would rather put -- I would rather put each witness on
21 briefly just to --

22 MR. WADE: Do you have an objection to the
23 process he just described?

24 MR. PADILLA: I don't have a process. I
25 mean we'll stipulate to the well locations and that kind

1 of thing.

2 MR. BRUCE: If it's okay, I could just
3 present the land stuff myself.

4 MR. PADILLA: That would be fine on the
5 condition that my questions relative to the whole
6 process that I asked in the other case are still
7 applicable to this case.

8 MR. BRUCE: I agree wholeheartedly.

9 MR. WADE: And since we're going to continue
10 this case as well next week, if you come up with any
11 additional questions, you can --

12 MR. BRUCE: I think Mr. Kauffman's testimony
13 in this case could be incorporated by reference into the
14 second case.

15 MR. WADE: Okay.

16

17

18

19

(Time noted 12:07 p.m.)

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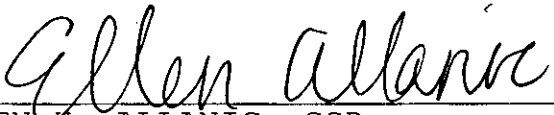
I do hereby certify that the foregoing is
a complete record of the proceedings in
the Examiner hearing of Case No. _____,
heard by me on _____.
_____, Examiner
Oil Conservation Division

1 STATE OF NEW MEXICO)
2) ss.
3 COUNTY OF BERNALILLO)
4
5
6

7 REPORTER'S CERTIFICATE

8
9 I, ELLEN H. ALLANIC, New Mexico Reporter CCR
10 No. 100, DO HEREBY CERTIFY that on Thursday, November
11 12, 2015, the proceedings in the above-captioned matter
12 were taken before me, that I did report in stenographic
13 shorthand the proceedings set forth herein, and the
14 foregoing pages are a true and correct transcription to
15 the best of my ability and control.

16
17 I FURTHER CERTIFY that I am neither employed by
18 nor related to nor contracted with (unless excepted by
19 the rules) any of the parties or attorneys in this case,
20 and that I have no interest whatsoever in the final
21 disposition of this case in any court.

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