

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

**APPLICATION OF ARD ENERGY, LLC TO REOPEN CASE NO. 15185 PURSUANT
TO THE PROVISIONS OF ORDER NO. R-13913 FOR THE PURPOSE OF
DETERMINING REASONABLE WELL COSTS, LEA COUNTY, NEW MEXICO.**

CASE NO. 15185 (re-opened)

COG's PROPOSED FINDINGS AND CONCLUSIONS

1. Under Division Orders R-13913, COG Operating LLC ("COG") is the designated operator of a pooled non-standard 160-acre spacing and proration unit in the West Maljamar-Yeso Pool underlying the W/2 W/2 of Section 15, Township 17 South, Range 32 East, NMPM, Lea County, New Mexico (the "Unit").

2. Under Order R-13913-A, the Unit was dedicated to the Ivar the Boneless Federal Well No. 11H Well (API No. 30-025-42514).

3. Ard Energy LLC ("Ard Energy") is an interest owner subject to Orders R-13913 and R-13913-A. Under the terms of these pooling orders, Ard Energy elected to participate in the Ivar the Boneless Federal Well No. 11H well and submitted "its share of the estimated drilling costs in the amount of \$180,784.38" based on the AFE submitted by COG. See Application at ¶4; COG Exs. 3 and 4.

4. Division records reflect the Ivar the Boneless Federal Well No. 11H was drilled, completed and declared ready to produce by August 26, 2015.

5. Three additional infill wells have been or are being drilled and completed in the Unit: The Ivar the Boneless 12H (API No. 30-025-42997), the Ivar the Boneless 21H (API No. 30-025-43406) and the Ivar the Boneless 22H (API No. 30-025-42998). See COG Ex. 2; Tr. 179 (Scott)

6. Under the terms of the pooling orders, Ard Energy elected to participate in the first infill well (the Ivar the Boneless 22H) but elected not to participate in the remaining two infill wells in the Unit. See Tr. 193 (Scott).

7. On February 19, 2016, COG provided Ard Energy with an itemized schedule of actual well costs for the initial well in the Unit, the Ivar the Boneless 11H well. See Ard Ex. 2.

8. On March 30, 2016, Ard Energy filed an Application with the Division seeking a determination on the "reasonable well costs for drilling the Ivar The Boneless Federal Well No. 11H." See Application at p. 2. No other relief is requested in the Application. See Tr. 105-106 (Attorney discussion).

9. Despite requests from COG, Ard Energy refused to identify the disputed costs prior to the Division hearing in this matter. *See* Ard Exhibit 7; Tr. 81-85 (Grappe).

10. At the hearing, Ard Energy identified the following lines items as disputed costs in the schedule of actual well costs COG provided Ard Energy in February of 2016:

- 332: Stimulation/Treating
- 337: Trucking/Forklift/Rig Mob
- 201: Title/Permits
- 209: Daywork Contract
- 225: Contract Labor
- 237: Trucking/Forklift/Rig Mob
- 242: Miscellaneous
- 510: Tanks
- 511: Flowlines/Pipelines
- 512: Htr Ttr/Seprtr
- 513: Electrical System/Equipment
- 515: Couplings/Fittings/Valves
- 519: Miscellaneous Other Equip
- 521: Pumps-Surface
- 522: Instrumentation/SCADA Equi
- 401: Surface Casing

See Ard Exhibit 2; TR. 164-168 (Morris).

11. While Ard Energy disputes the total amount under the line items identified in the preceding paragraph, it presented no testimony on the amount it considers reasonable under each of these line items. *See* Tr. 76-78, 80, 122-125 (Grappe); Ard Exhibit 10.

12. Ard Energy presented no alternative AFE for the subject well or any cost comparisons with similar wells. *See* Tr. 170, 174 (Morris); Tr. 94 (Grappe).

13. Ard Energy's witness agreed the drilling and completion costs contained in the AFE executed by Ard Energy on May 21, 2015, are reasonable. *See* COG Exhibit 4; TR. 144-145 (Morris).

14. Ard Energy's witness testified that a 5%-10% variance from the AFE executed by Ard Energy on May 21, 2015, would not be unusual. *See* TR. 163 (Morris).

15. Line items 332 (Stimulation and Treating) and 209 (Daywork contract) reflect increases within six percent of the anticipated costs reflected on the AFE executed by Ard Energy on May 21, 2015. *Compare* COG Exhibit 4 *with* COG Exhibit 5.

16. COG's witness testified that the cost increases in Line 201 (Title/Permits) was due to complicated and unexpected title issues presented by the acreage in the W/2 of Section 15. *See* Tr. 187-190 (Scott).

a. The subject acreage is a 1930s era federal lease covering the W/2 of Section 15. *See* Tr. 187 (Scott).

b. Ownership in the subject acreage is fragmented by surface and depth, suffers from gaps in title, and is complicated by a waterflood project. *See* Tr. 187-189, 199-200, 222 (Scott).

c. COG's witness testified that it was necessary in this case to examine title for the entire lease to obtain a reasonably secure title opinion. *See* Tr. 220-221 (Scott).

d. The title opinion for this acreage was in excess of 200 pages (*see* Tr. 186) and was "one of the largest abstracts the broker ever provided." *See* Tr. 187 (Scott).

e. Ard Energy presented no witness with the qualifications or information to dispute the complexity of the title opinion for this acreage, or to opine on the reasonableness of the land and legal costs. *See* Tr. 100 (Grappe); Tr. 165:4-17 (Morris).

17. Of the remaining cost increases between the AFE executed by Ard Energy on May 21, 2015, and the final report of well costs provided to Ard in February of 2016, roughly \$668,664 are contained under the following line items:

225/325: Contract Labor - \$145,000 increase
242: Miscellaneous - \$79,525 increase
510: Tanks - \$66,515 increase
512: Htr Ttr/Seprtr - \$146,182 increase
515: Couplings/Fittings/Valves - \$182,934 increase
519: Miscellaneous Other Equip - \$48,728 increase

Compare COG Ex. 4 with COG Ex. 5.

18. COG's witnesses testified the costs increases under these line items result from installation of surface facilities to accommodate not only the initial well in the Unit, but three additional infill wells. *See* Tr. 182; 190-191, 214-215 (Scott); Tr. 227 (Hinshaw).

a. The surface facilities only accommodate the wells in the Unit and therefore have identical interest owners. Tr. 192 (Scott)

b. The additional surface facilities included the installation of five tanks and dual flow lines. *See* Tr. 231-232 (Hinshaw)

19. The AFE executed by Ard Energy on May 21, 2015, only included the anticipated costs to drill and complete the initial well; it did not include costs to install the surface facilities necessary to accommodate four wells in the Unit. *See* Tr. 193, 214 (Scott); Tr. 229; 233 (Hinshaw); COG Ex. 4.

20. COG has chosen to bill the title and surface facility costs to the initial well in the Unit in which all of the working interest owners agreed to participate. *See* Tr. 183; 193; 202 (Scott). Accordingly, these additional costs are not currently subject to any risk penalty imposed by the pooling order. *See* Tr. 193-194 (Scott); Tr. 230 (Hinshaw).

21. COG has offered to allocate the surface facility costs among the four wells in the Unit, but Ard Energy has refused to state whether that allocation is acceptable. *See* Tr. 235-36 (Hinshaw); Tr. 82-85 (Grappe); Ard Ex. 7.

22. COG is responsible for 68% of the costs at issue, ConocoPhillips is responsible for 25% of the costs at issue, and Lynx Petroleum is responsible for just over 1% of the costs at issue. *See* Tr. 196 (Scott); COG Ex. 7.

23. None of the other cost-bearing interest owners (which account for 95% of the working interest) have raised any concerns with the costs to drill and complete the Ivar the Boneless 11H well or to install the surface facilities necessary to accommodate the four wells drilled in the Unit. *See* Tr. 196-197 (Scott).

24. COG's witnesses testified that the costs incurred to drill and complete the Ivar the Boneless 11H well, and the costs incurred to install the surface facilities for the four wells in the Unit, are consistent with the costs incurred by the company to develop similar properties. *See* Tr. 197-198 (Scott); Tr. 229-230 (Hinshaw).

25. The concerns raised by Ard Energy about the amount of the lease operating expenses for the Ivar the Boneless 11H well, the offsetting of well costs with revenues from other wells, a desire for an audit or an accounting of the well costs were not raised by the Applicant until the hearing and are not before the Division under the filed Application. *See* Tr. 113 (Brooks observation).

26. As the applicant challenging the reasonableness of the well costs, Ard Energy has the burden to establish that specific costs are unreasonable. *See* Tr. 102:19-25 (Brooks comment).

27. The Division concludes Ard Energy has failed to meet its burden of establishing that any specific costs are unreasonable.

Respectfully submitted,

HOLLAND & HART, LLP



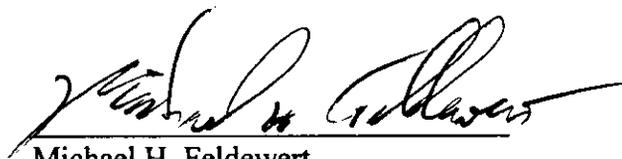
Michael H. Feldewert
Jordan L. Kessler
Post Office Box 2208
Santa Fe, New Mexico 87504-2208
(505) 988-4421
mfeldewert@hollandhart.com
jlkessler@hollandhart.com

ATTORNEYS FOR COG OPERATING LLC

CERTIFICATE OF SERVICE

I hereby certify that on November 7, 2016, I served a copy of the foregoing document to the following via electronic mail to:

Ernest L. Padilla
Padilla Law Firm
Post Office Box 2523
Santa Fe, New Mexico 87504
(505) 988-7577
padillalaw@qwestoffice.net



Michael H. Feldewert
Jordan L. Kessler