

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

DOCKET NUMBER 28-15

APPLICATION OF MATADOR PRODUCTION Case 15363
COMPANY FOR A NON-STANDARD
SPACING PRORATION UNIT AND
COMPULSORY POOLING, LEA COUNTY
NEW MEXICO

TRANSCRIPT OF PROCEEDINGS
SPECIAL EXAMINER HEARING

September 29, 2015

Santa Fe, New Mexico

This matter came on for hearing before the New
Mexico Oil Conservation Division, PHILLIP GOETZE,
P.E.;, GABRIEL WADE, Legal Counsel; and WILL JONES,
Chief Engineer, on Tuesday, September 29, 2015, at
the New Mexico Energy, Minerals and Natural
Resources Department, Porter Hall, Santa Fe,
New Mexico.

REPORTED BY: PAUL BACA, CCR #112
PAUL BACA COURT REPORTERS
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| Page 2 | |
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| 23 | INDEX |
| 24 | Opening Statement by Mr. Bruce 6 |
| 25 | Opening Statement by Mr. Gallegos 8 |
| | APPLICANT'S WITNESSES |
| | WITNESSES: PAGE: |
| | RUDY H. SIMS, JR. |
| | Examination by Mr. Bruce 10 |
| | Examination by Mr. Gallegos 31 |
| | Further Examination by Mr. Bruce 53 |
| | JAMES ANDREW JUETT |
| | Examination by Mr. Bruce 68 |
| | Examination by Mr. Gallegos 77 |
| | Further Examination by Mr. Bruce 89 |

| Page 3 | |
|--------|--------------------------------------|
| 1 | INDEX |
| 2 | APPLICANT'S WITNESSES |
| 3 | WITNESSES: PAGE: |
| 4 | AARON MICHAEL BYRD |
| 5 | Examination by Mr. Bruce 101 |
| 6 | Examination by Mr. Gallegos 111 |
| 7 | Further Examination by Mr. Bruce 125 |
| 8 | PROTESTANT'S WITNESS |
| 9 | WITNESS: PAGE: |
| 10 | HARVEY E. YATES, JUNIOR |
| 11 | Examination by Mr. Gallegos 134 |
| 12 | Examination by Ms. Arnold 179 |
| 13 | Examination by Mr. Bruce 206 |
| 14 | APPLICANT'S REBUTTAL WITNESS |
| 15 | WITNESS'S: |
| 16 | AARON MICHAEL BYRD |
| 17 | Examination by Mr. Bruce 222 |
| 18 | Examination by Mr. Gallegos 228 |
| 19 | |
| 20 | Closing Statement by Ms. Arnold 230 |
| 21 | |
| 22 | CERTIFICATE OF COURT REPORTER 233 |
| 23 | |
| 24 | |
| 25 | |

| Page 4 | |
|--------|--------------------------------|
| 1 | APPLICANT'S EXHIBITS ADMITTED |
| 2 | 1 - 11 31 |
| 3 | 12-15 77 |
| 4 | 16 and 18 111 |
| 5 | 17 77 |
| 6 | |
| 7 | PROTESTANT'S EXHIBITS ADMITTED |
| 8 | 1-4 178 |
| 9 | 7-9 178 |
| 10 | 14 178 |
| 11 | |
| 12 | |
| 13 | |
| 14 | |
| 15 | |
| 16 | |
| 17 | |
| 18 | |
| 19 | |
| 20 | |
| 21 | |
| 22 | |
| 23 | |
| 24 | |
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| Page 5 | |
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| 1 | LEAD EXAMINER GOETZE: Good morning, |
| 2 | ladies and gentlemen. |
| 3 | This is the OCD Docket Number 28-15. It's |
| 4 | a special examiner hearing for Tuesday, |
| 5 | September 29th, 2015, in Porter Hall. |
| 6 | We are here to hear the continuance of |
| 7 | Case Number 15363, application of Matador Production |
| 8 | Company for a nonstandard oil spacing and proration |
| 9 | unit and compulsory pooling, Lea County, New Mexico. |
| 10 | I call for appearances, please. |
| 11 | MR. BRUCE: Mr. Examiner, Jim Bruce, of |
| 12 | Santa Fe, in association with Dana Arnold, of |
| 13 | Matador, representing Matador Production Company. |
| 14 | MR. GALLEGOS: Mr. Examiner, Gene |
| 15 | Gallegos, Santa Fe, New Mexico, and I am appearing |
| 16 | for Jalapeno Corporation and Yates Energy. |
| 17 | LEAD EXAMINER GOETZE: We'll introduce the |
| 18 | folks in the front also at this point. |
| 19 | To my right is Will Jones, who has come |
| 20 | along. He is the engineer, chief engineer. |
| 21 | And then Gabriel Wade, to my left, is the |
| 22 | legal counsel. |
| 23 | We also summarize that an application, a |
| 24 | motion for dismissal, was submitted by Jalapeno. |
| 25 | At this point we have made a decision on |

2 (Pages 2 to 5)

| Page 6 | Page 8 |
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| <p>1 that which the director has approved and issued an 2 order denying that dismissal. 3 So at this point we will continue with 4 this case. 5 Witnesses? 6 MR. BRUCE: I have four potential 7 witnesses. 8 LEAD EXAMINER GOETZE: Okay. Four 9 potential witnesses. 10 And you, sir? 11 MR. GALLEGOS: We have one witness, 12 Mr. Examiner. 13 LEAD EXAMINER GOETZE: Okay. Well, at 14 this point we will go ahead and we will have them 15 sworn in as they are called forward. 16 Opening statements? 17 OPENING STATEMENT 18 BY MR. BRUCE: 19 I think the issues are pretty clear in 20 this matter, and one of them was the motion to 21 dismiss that was denied. 22 Another one is good faith efforts to get 23 the parties to voluntarily join in the well. 24 At this point there's about -- 92 percent 25 of the interests have voluntarily joined in the well</p> | <p>1 they don't have to join in it. They don't have to 2 pay any money, and they're not at risk. 3 I think what you're looking at here is 4 what Matador is doing is protecting the correlative 5 rights of the parties. They are preventing waste, 6 and I think in the end you will see that this 7 application should be granted and that the usual 8 200 percent risk charge be assessed against any 9 non-consenting interest owners. 10 Thank you. 11 LEAD EXAMINER GOETZE: Mr. Gallegos? 12 MR. GALLEGOS: Yes, Mr. Examiner. 13 OPENING STATEMENT 14 BY MR. GALLEGOS: 15 Let me just point out the issues. I'm not 16 going to attempt to argue them at this point. 17 But one of the issues is that there has 18 not been a reasonable good faith effort by Matador 19 to secure voluntary participation with Jalapeno, and 20 we will present the evidence on what communications 21 have been between parties, including the efforts to 22 obtain information from Matador critical to 23 decision-making, which has not been supplied. 24 It's also an issue that the AFE put 25 forward by Matador in this case was compiled in</p> |
| Page 7 | Page 9 |
| <p>1 one way or the other. 2 Matador has been trying to get this well 3 put together for six months. I think you will see 4 from the land evidence that the massive number of 5 contacts that Matador has had with the people who 6 own interests in this well will show that good 7 faith, the good faith requirement of pooling, has 8 been met. 9 Another issue that's come up is risk. I 10 think I would rather hold off on that until I get to 11 my drilling witness, for the most part. But there's 12 always risk in drilling a well. 13 Certainly there are drilling risks, 14 geologic risks. At this point, of course, the issue 15 of oil prices come up. That's a risk too. 16 They try to -- Jalapeno and Yates is 17 saying that that risk should be solely on the 18 operator. I think that's a ridiculous position to 19 take, and I've never seen that happen before in my 20 lifetime of dealing with oil and gas poolings and 21 JOAs. 22 If they don't like the well their remedy 23 is to not participate, period. Their rights are not 24 being taken. It's provided for in the statutes, the 25 pooling statutes, that if they don't like the well</p> | <p>1 March, and the AFE increased to \$9 million over a 2 prior AFE involving this well except in the Bone 3 Springs formation, and that the AFE does not reflect 4 the current market for expenses in the Permian 5 Basin, given the oil price reduction and the 6 reduction in expenses by the service companies. 7 We do challenge the allowance of a risk 8 penalty in this case almost of any magnitude, and we 9 will present evidence that demonstrates why a 10 200 percent risk penalty is inappropriate. 11 I do want to just say for the record, 12 these are legal issues more than factual issues, 13 Mr. Examiner. But we do challenge the legal effect 14 of Order R11992, because that is the order for 15 the -- you know, the automatic 200 percent risk 16 penalty. And we think that under the statute under 17 70-2-17 is -- it's basically unlawful, and we 18 continue the challenge that was raised by our motion 19 to dismiss, that there is basically no statutory 20 authority for these nonstandard spacing units which 21 seek to combine already existing 40-acre oil spacing 22 units. 23 Thank you. 24 LEAD EXAMINER GOETZE: Very good. 25 Mr. Bruce, please proceed with your case.</p> |

3 (Pages 6 to 9)

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| <p style="text-align: right;">Page 10</p> <p>1 (The witness was sworn.) 2 THE WITNESS: My name is Rudy H. Sims, Jr. 3 RUDY H. SIMS, JR., 4 after having been first duly sworn under oath, 5 was questioned and testified as follows: 6 EXAMINATION 7 BY MR. BRUCE: 8 Q. Mr. Sims, where do you reside? 9 A. I currently reside in Plano, Texas. 10 Q. And who do you work for and in what 11 capacity? 12 A. I work for MRC Energy Company, an 13 affiliate of Matador Production Company. 14 I am the operations land manager. 15 Q. Does Matador Production Company operate 16 wells for MRC entities? 17 A. Yes. 18 Q. And have you previously testified before 19 the division? 20 A. I have. 21 Q. What are your responsibilities as a 22 landman at Matador? 23 A. I supervise a team of land professionals 24 who are primarily charged with getting wells ready 25 to be drilled.</p> | <p style="text-align: right;">Page 12</p> <p>1 pertaining to the application filed by Matador in 2 this case? 3 A. I am familiar with it. 4 Q. And are you familiar with the status of 5 lands which are the subject of this application? 6 A. Yes, I am. 7 MR. BRUCE: Mr. Examiner, I tender 8 Mr. Sims as an expert petroleum landman. 9 MR. GALLEGOS: No objection. 10 LEAD EXAMINER GOETZE: Very good. He is 11 so qualified. 12 Q. (By Mr. Bruce) Mr. Sims, could you refer 13 to Exhibit 1, which is a two-part exhibit, and 14 explain what Matador seeks in this application? 15 And maybe first turn to page 2 in 16 Exhibit 1. 17 A. Page 2 of Exhibit 1 is a Form C-102 for 18 the well. It is the Airstrip 31, 18 south, 35 east, 19 State Com Number 201H, a horizontal well with a 20 surface location of 50 feet from the south line, 21 330 feet from the west line of Section 31. 22 The producing interval will be orthodox, 23 with the first penetration point 330 feet from the 24 south line and 330 feet from the west line of 25 Section 31. The last perforation 330 feet from the</p> |
| <p style="text-align: right;">Page 11</p> <p>1 Much of our focus is on obtaining run 2 sheets and title opinions, acquisition of oil and 3 gas interests, curing title issues, working with 4 other companies to try to jointly drill wells. 5 Q. Could you describe your educational and 6 employment background for the examiner? 7 A. I can. I have a BA from the University of 8 Southern Mississippi, a JD from Mississippi College 9 School of Law. 10 I've worked in the oil and gas business 11 for an excess of 35 years in various land roles 12 around the country. 13 The companies that I've worked for include 14 Husky Oil Company, Marathon Oil Company, Devon 15 Energy, Chesapeake Energy, Murchison Oil and Gas, 16 and Matador. 17 Q. Do you hold any certifications or belong 18 to any professional associations? 19 A. I'm a member of the Mississippi Bar 20 Association and the American Association of 21 Professional Landmen. 22 Q. Does your area of responsibility at MRC or 23 Matador include this area of Southeast New Mexico? 24 A. It does. 25 Q. And are you familiar with the land matters</p> | <p style="text-align: right;">Page 13</p> <p>1 north line and 710 feet from the west line of 2 Section 31. 3 Matador wishes to form an oil spacing and 4 proration unit comprised of the west half/west half 5 of Section 31, township 18 south, range 35 east, Lea 6 County, New Mexico, in order to drill the horizontal 7 well identified in Exhibit 1. 8 Q. Referring to the first page of Exhibit 1, 9 can you explain a little bit of the permitting 10 history of this well? 11 A. Yes, I can. 12 This well was -- there was a well 13 initially permitted to drill to the Bone Spring 14 formation by HEYCO. 15 Matador purchased HEYCO through a merger, 16 and we elected to -- to drill a different interval 17 in the -- in the Wolfcamp formation. We thought 18 that was more prospective in that interval. 19 Q. And will Matador's other witnesses discuss 20 the reason for the change in formation? 21 A. Absolutely. 22 Q. And what is the acreage of the nonstandard 23 spacing unit? 24 A. It's approximately 154 acres. It's some 25 lots, so they're not an exact 160 that we're</p> |

4 (Pages 10 to 13)

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| <p style="text-align: right;">Page 14</p> <p>1 probably more accustomed to.</p> <p>2 Q. And what pool is the Wolfcamp well in?</p> <p>3 A. It's in the Airstrip Wolfcamp pool, pool</p> <p>4 code 970.</p> <p>5 MR. BRUCE: And, Mr. Examiner, it is --</p> <p>6 it's -- the first page of Exhibit 1 does show the</p> <p>7 lots and their acreage, for the record.</p> <p>8 Q. (By Mr. Bruce) What is the working</p> <p>9 interest ownership of the well unit, and who do you</p> <p>10 seek to pool?</p> <p>11 And I refer you to Exhibit 2.</p> <p>12 A. MRC Permian holds 89.85 percent of the</p> <p>13 working interest. We have voluntary joinders of</p> <p>14 2.83 percent, and we seek to pool 7.32 percent.</p> <p>15 And those parties include Yates Energy</p> <p>16 Corporation, Jalapeno Corporation, Louis Kadane and</p> <p>17 Michael L. Gustafson, trustees of the 4-K Trust, at</p> <p>18 the request of Edward G. Kadane, II, former interest</p> <p>19 of George Kadane.</p> <p>20 In addition, Louis Kadane and Michael L.</p> <p>21 Gustafson, trustees of the 4-K Trust, at the request</p> <p>22 of Matthew D. Kadane, former interest of George</p> <p>23 Kadane.</p> <p>24 And finally, Brent Ray Robertson.</p> <p>25 Q. Is there a chance that you will reach</p> | <p style="text-align: right;">Page 16</p> <p>1 letter that was sent to uncommitted working interest</p> <p>2 owners.</p> <p>3 Q. This letter, in particular, is to Billie</p> <p>4 Kirby.</p> <p>5 Were virtually identical letters sent out</p> <p>6 to all of the originally uncommitted interest</p> <p>7 owners?</p> <p>8 A. They were.</p> <p>9 Q. Have you had any other contacts with the</p> <p>10 parties you seek to pool?</p> <p>11 A. Yes, we have.</p> <p>12 Q. And what is Exhibit 6?</p> <p>13 A. Exhibit 6 is a summary of the</p> <p>14 communication with uncommitted working interest</p> <p>15 owners.</p> <p>16 We also have, as part of Exhibit 6,</p> <p>17 several letters and communications that have</p> <p>18 occurred between various parties.</p> <p>19 Q. How long have you been in touch with the</p> <p>20 working interest owners to try to obtain voluntary</p> <p>21 joinder?</p> <p>22 A. Since March of 2015.</p> <p>23 Q. In your opinion, has MRC or Matador made a</p> <p>24 good faith effort to obtain the voluntary joinder of</p> <p>25 the interest owners in the well?</p> |
| <p style="text-align: right;">Page 15</p> <p>1 agreement with other interest owners regarding</p> <p>2 joinder in the well?</p> <p>3 A. We are hopeful. We -- we think we've made</p> <p>4 some progress with Yates Energy over the last few</p> <p>5 days, and hopefully we can -- we can get that across</p> <p>6 the finish line. And we're always eager to bring</p> <p>7 everyone aboard.</p> <p>8 Q. And if additional parties voluntarily join</p> <p>9 in the well, will you notify the division?</p> <p>10 A. Yes, we will.</p> <p>11 Q. Okay. What is the character of the lands</p> <p>12 involved in this case?</p> <p>13 A. The lands involved are state lands</p> <p>14 encompassing two state leases.</p> <p>15 Q. And is that shown, not only on Exhibit 1,</p> <p>16 but on Exhibit 4?</p> <p>17 A. Yes, it is. It's shown on the Midland map</p> <p>18 and also on a tract map that was prepared by</p> <p>19 Matador.</p> <p>20 Q. Okay. One exhibit we skipped over is</p> <p>21 Exhibit 3. But that is simply a restatement of the</p> <p>22 parties being pooled at this time, is it not?</p> <p>23 A. That is correct.</p> <p>24 Q. Okay. What is Exhibit 5?</p> <p>25 A. Exhibit 5 contains a copy of our proposal</p> | <p style="text-align: right;">Page 17</p> <p>1 A. We have been negotiating in good faith</p> <p>2 since March, to reach a voluntary joinder with the</p> <p>3 uncommitted working interest owners.</p> <p>4 Q. Tell me about some of the different</p> <p>5 alternatives that you have presented to the interest</p> <p>6 owners to get them to join in the well.</p> <p>7 A. In our initial proposal, way back in</p> <p>8 March, we offered the uncommitted working interest</p> <p>9 owners the opportunity to participate in the</p> <p>10 drilling of the well. Some of the parties elected</p> <p>11 to participate at that time.</p> <p>12 We also offered the option of uncommitted</p> <p>13 parties assigning all of their net revenue interest</p> <p>14 in the proposed contract area for the well to</p> <p>15 Matador for \$1,800 an acre.</p> <p>16 We -- we did not have anyone elect under</p> <p>17 that -- under that provision.</p> <p>18 We also offered the parties the option of</p> <p>19 assigning all of their interest to Matador retaining</p> <p>20 a proportionately reduced override equal to the</p> <p>21 positive difference between existing burdens and</p> <p>22 25 percent.</p> <p>23 Bob Kadane actually elected to do that.</p> <p>24 Then we also offered the option of parties</p> <p>25 to sell all of their interest in the governmental</p> |

5 (Pages 14 to 17)

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| <p style="text-align: right;">Page 18</p> <p>1 section, including the existing wellbores. 2 No one elected to do that. 3 Later, we increased our offer to \$5,000 4 per net acre, delivering a 75 percent net revenue 5 interest. 6 We had a number of parties -- in fact the 7 majority of the outstanding working interest 8 owners -- elected under that offer. 9 As to Jalapeno and Yates Energy, we 10 offered them the option to participate, sell their 11 interest at 5,000 an acre, sell to JV that -- my 12 understanding, that they have either legal or 13 beneficial interest in that JV that Matador also has 14 an interest in. 15 They could, of course, be force pooled as 16 a last resort. 17 And finally, sell down and retain a 18 certain amount of interest, so they would 19 participate for part and sell to Matador a part. 20 Q. In today's economic environment, is \$5,000 21 an acre a fair and reasonable offer? 22 A. Yes, sir, very much so. 23 Q. In your summary of communications, on 24 June 3, there's a listing for a working interest 25 owners' meeting.</p> | <p style="text-align: right;">Page 20</p> <p>1 interest, unfortunately, in what we thought were -- 2 were very good offers to them. And so we were 3 trying to find some way, somehow, to make this thing 4 work. 5 Q. Is it usual and customary to have that 6 sort of meeting with uncommitted working interest 7 owners? 8 A. It's very unusual. It's especially 9 unusual to have a CEO of a public company with over 10 \$2 billion of market cap sit down at a meeting of 11 this type. 12 Q. Now your Exhibit 6, besides the summary, 13 contains the -- some other correspondence. 14 But let's concentrate on maybe the last 15 eight or nine pages of Exhibit 6. 16 There are two letters I would like to have 17 you discuss. 18 The first letter is a letter dated 19 August 17, 2015. That's from Jalapeno Corporation 20 to Matador. 21 And then there's a letter dated August 26, 22 2015, from MRC to Mr. Harvey Yates at Jalapeno 23 Corporation. 24 MR. GALLEGOS: I'm sorry, Mr. Bruce. 25 You're on Exhibit 6?</p> |
| <p style="text-align: right;">Page 19</p> <p>1 Could you describe that meeting in Dallas 2 with -- and who was present? 3 A. Yes, I would be happy to. 4 On June 3, in our offices in Dallas, Fred 5 Yates, Becky Pemberton, and Mike Stewart represented 6 Yates Energy. 7 Emmons Yates represented Jalapeno. 8 Including -- representing Matador were Joe 9 Foran, our CEO, and much of our executive 10 management, much of our technical and land teams 11 that work this particular area of New Mexico, and 12 specifically, those that are entrusted with getting 13 this particular well ready. 14 Approximately 20 people met with -- with 15 the representatives of these two companies. And we 16 were there probably a couple of hours discussing 17 this particular well. 18 Q. And what was discussed? 19 A. Well, the various options that we were 20 offering them to participate. In fact, there were 21 even some discussions on additional options, where 22 the buy-down and they participate for half, were 23 kind of viewed as an elegant solution to the issue 24 that we were facing. 25 We were not seeing a whole lot of</p> | <p style="text-align: right;">Page 21</p> <p>1 MR. BRUCE: Exhibit 6, towards the end of 2 it. 3 MR. GALLEGOS: Oh, okay. 4 MR. BRUCE: The last eight or nine pages. 5 MR. GALLEGOS: Okay. 6 Q. (By Mr. Bruce) Without going into detail, 7 can you tell me your takeaway from the letter that 8 Jalapeno sent on August 17 from Mr. Yates? 9 When you read it, what was your 10 impression? 11 A. I personally was shocked by the tenor of 12 the letter, the allegations that -- that Matador did 13 not make a good faith effort to negotiate. It just 14 simply didn't comport with the facts. 15 Q. If you were not related to -- not employed 16 by Matador, not involved in this situation, and you 17 had no knowledge of the surrounding circumstances 18 regarding this well and this proceeding, what would 19 you think if you read this letter? 20 MR. GALLEGOS: I object to the relevancy 21 of that. 22 LEAD EXAMINER GOETZE: Are you trying to 23 give an opinion with regard to -- let's clarify 24 that. 25 What are you after?</p> |

6 (Pages 18 to 21)

Page 22

1 MR. BRUCE: Well, that's a very short
2 answer.

3 Q. (By Mr. Bruce) But, Mr. Sims, if you --
4 reading this letter, if you had no knowledge of
5 prior discussions between the parties, what would
6 you think had occurred between Jalapeno and Matador
7 up to that point?

8 A. From this letter, you would think that we
9 had not made any contact at all and had not made
10 anything -- any reasonable effort to work out a deal
11 with these two companies.

12 Q. Then if you would move forward to the
13 Matador letter, the final letter in the Exhibit 6
14 package.

15 A. (Witness complies.)

16 Q. Could you -- does this letter summarize
17 the efforts the people at Matador made to get a deal
18 done with Jalapeno?

19 A. Yes, it does.

20 Q. And again, in the last six months, has
21 Matador made a good faith effort to reach voluntary
22 agreement with not only Jalapeno, but with all of
23 the interest owners in the well?

24 A. We have made Herculean efforts to reach an
25 agreement with every uncommitted working interest

Page 23

1 owner.

2 Q. And again, other parties have accepted the
3 terms offered by Matador related to the well, have
4 they not?

5 A. Yes, indeed, they have.

6 Q. Does MRC or Matador request the maximum
7 cost plus 200 percent risk charge if a working
8 interest owner goes nonconsent in the well?

9 A. Yes, we do.

10 Q. Mr. Sims, how long have you been -- you
11 said you've been in the business now 35 years?

12 A. Over 35 years, yes, sir.

13 Q. And as part of your work for the various
14 companies, have you been negotiating JOAs?

15 A. Yes, I have.

16 Q. And over the course of that time, how many
17 JOAs have you negotiated?

18 A. Well over 2,000.

19 Q. Were those JOAs for horizontal
20 development?

21 A. They were for both.

22 Q. Vertical and horizontal wells?

23 A. Correct.

24 Q. Have those JOAs ever been in areas where
25 there was existing production?

Page 24

1 A. Yes, indeed.

2 Q. And were you -- in your negotiations with
3 JOAs, were you both an operator and a non-operator?

4 A. Yes, I was.

5 Q. And what nonconsent penalty is common in
6 those JOAs?

7 A. We typically see 100/300 percent
8 nonconsent penalty. I think that's probably the
9 most prevalent.

10 But you also -- you also see a number of
11 different versions of that.

12 In fact, as I -- I was sitting on the
13 other side of the table from -- from Matador back in
14 2008 working for Chesapeake. And the play of the
15 day back then was the Haynesville Shale in and
16 around Shreveport.

17 Chesapeake acquired a 75 percent interest
18 in a fairly sizable position that Matador had.

19 The JOA in that case had a
20 200 percent/400 percent nonconsent penalty.

21 So we do see a lot of different versions
22 of that.

23 Q. If Matador was a non-operator in this
24 well, would it sign a JOA with a 300 percent
25 nonconsent penalty, cost plus 200 percent?

Page 25

1 A. We would.

2 Q. From a land standpoint, is a risk charge
3 of cost plus 200 percent justified in this case?

4 A. It is.

5 Q. In your experience of over 35 years
6 working in the oil and gas business, has the price
7 of oil and gas been constant?

8 A. No, it has not.

9 Q. You've been in the business about the same
10 length of time as me. There's been at least a half
11 a dozen major downturns in the industry over that
12 period?

13 A. There have been a number of downturns.
14 Price -- I remember \$9 oil a couple of times. So
15 yes, there's -- there's a lot of variability with
16 respect to the price of oil and gas.

17 Q. In negotiating JOAs have you ever seen a
18 provision in the JOA, where prices are low, all the
19 risk is on the operator?

20 A. Could you repeat that?

21 Q. Have you ever seen a JOA provision where,
22 if oil prices when you start drilling are \$9 a
23 barrel, that any risk involved in drilling the well
24 is only on the operator and not on the
25 non-operators?

7 (Pages 22 to 25)

Page 26

1 A. No, sir. I've never heard of such.
 2 Q. Okay. Have you ever seen a provision in a
 3 JOA where, if prices decline, the participating
 4 working interest owners would get a new election in
 5 oil?
 6 A. No, sir. I haven't seen that either.
 7 Q. And vice versa. What about if prices go
 8 up? Should non-consenting working interest owners
 9 get a new election in the well?
 10 A. I don't think so, sir.
 11 Q. You said you've worked in several states,
 12 correct?
 13 A. I have.
 14 Q. What sort of risk charges have you seen in
 15 compulsory pooling cases in other states?
 16 A. Well, in those states that have a risk
 17 premium mechanism like New Mexico, you typically do
 18 see cost plus 200 percent.
 19 And that's the -- that's the case in
 20 North Dakota, Colorado, Louisiana.
 21 You'll find some states, like Wyoming, it
 22 can be up to 300 percent there, and even higher in
 23 Idaho.
 24 Mississippi has an alternative election
 25 that you can wipe at 250 percent.

Page 27

1 I think Alabama you can have a percentage
 2 that's a little higher than 250, or around the 300
 3 range.
 4 So 200 plus cost is very common, and a
 5 higher number of cases as well.
 6 Q. Does -- moving forward a little bit.
 7 What is Exhibit 11, Mr. Sims?
 8 A. Exhibit 11 is the AFE for the well.
 9 Q. And what are the costs set forth in that
 10 AFE?
 11 A. The dry hole costs are 5.376 million.
 12 And the completed well cost is 9,099,000.
 13 Those are approximations.
 14 Q. Are those costs in line with the cost of
 15 other horizontal wells drilled to this depth in this
 16 area of New Mexico?
 17 A. Yes, they are.
 18 Q. Have these costs come down since the
 19 March proposal?
 20 A. Yes.
 21 Q. Will a subsequent witness discuss the well
 22 costs?
 23 A. Yes.
 24 Q. Have other parties agreed to participate
 25 in the well based on the -- this AFE and the

Page 28

1 March proposal letter?
 2 A. Yes.
 3 Q. And once that pooling order is issued,
 4 will an updated AFE be provided to all of the
 5 non-con- -- the working interest owners who have not
 6 yet consented to the well?
 7 A. Absolutely.
 8 Q. Who do you request be appointed the
 9 operator of the well?
 10 A. Matador Production Company.
 11 Q. And do you have a recommendation for the
 12 amounts which Matador should be paid for supervision
 13 and administrative expenses?
 14 A. I do.
 15 Q. What are they?
 16 A. 7,000 per month for a drilling well, and
 17 700 per month for a producing well.
 18 Q. And are those amounts equivalent to those
 19 normally charged by Matador and other operators in
 20 this area for horizontal wells of this depth?
 21 A. Yes, they are.
 22 Q. Are those the rates that is -- that are in
 23 the JOA for the well?
 24 A. Yes.
 25 Q. Do you request that the overhead rates be

Page 29

1 adjusted periodically as provided by the COPAS
 2 accounting procedure?
 3 A. We do.
 4 Q. Were the parties being pooled notified of
 5 this hearing?
 6 A. Yes, they were.
 7 Q. And is that reflected in my affidavit of
 8 notice marked as Exhibit 7?
 9 A. It is.
 10 Q. And what is Exhibit 8?
 11 A. Exhibit 8 is a list of offset operators,
 12 or working interest owners, to the unit.
 13 Q. And were those persons notified of this
 14 hearing?
 15 A. Yes, they were.
 16 Q. And is that reflected in my affidavit of
 17 notice marked as Exhibit 9?
 18 A. It is.
 19 Q. And was notice of this application
 20 published as to certain interest owners to be sure
 21 that they received notice?
 22 A. Yes.
 23 Q. And is that marked Exhibit 10?
 24 A. Yes, it is.
 25 MR. BRUCE: Mr. Examiner, two things, both

8 (Pages 26 to 29)

Page 30

1 with respect to -- let's go to Exhibit 7.
 2 The very last page of Exhibit 7, with
 3 respect to Edward Kadane and Matthew Kadane, the
 4 postal service website shows this was delivered.
 5 But in two months I've never gotten the green card
 6 back.
 7 And in Exhibit 9, which is the notice to
 8 offsets, the same thing with respect to one of the
 9 offsets, KC Resources.
 10 The postal service shows it was delivered,
 11 but they never delivered the green card back to me,
 12 the third page from the back of Exhibit 9.
 13 But notice was published as to those
 14 parties, and that is shown on Exhibit 10. I believe
 15 they received actual notice, but they did also --
 16 notice was published as against them.
 17 I don't know how to disgorge those green
 18 cards from the postal service.
 19 **Q. (By Mr. Bruce) Mr. Sims, were Exhibits 1**
 20 **through 11 prepared by you or under your supervision**
 21 **or compiled from company business records?**
 22 **A. They are.**
 23 **Q. And in your opinion, is the granting of**
 24 **this application in the interest of conservation and**
 25 **the prevention of waste?**

Page 31

1 **A. Yes, it is.**
 2 **MR. BRUCE:** Mr. Examiner, I would move the
 3 admission of Matador Exhibits 1 through 11.
 4 **MR. GALLEGOS:** No objection.
 5 **LEAD EXAMINER GOETZE:** No objections?
 6 Very good.
 7 Exhibits 1 through 11 are so entered.
 8 **MR. BRUCE:** I pass witness.
 9 **LEAD EXAMINER GOETZE:** Your witness,
 10 Mr. Gallegos.
 11 **EXAMINATION**
 12 **BY MR. GALLEGOS:**
 13 **Q. Mr. Sims, let's just take one moment for**
 14 **Exhibit 11. That's the AFE.**
 15 **A. Yes, sir.**
 16 **Q. Is it your testimony that in respect to**
 17 **any details concerning the -- this AFE and any**
 18 **modifications of it, you are not the witness to**
 19 **address that?**
 20 **A. That is correct.**
 21 **Q. Okay. And that will be who? Who will be**
 22 **the witness?**
 23 **A. One of the subsequent witnesses of Matador**
 24 **will address that.**
 25 **Q. All right.**

Page 32

1 **MR. BRUCE:** Mr. Gallegos, his name is
 2 Aaron Byrd.
 3 **MR. GALLEGOS:** Okay. Thank you.
 4 **Q. (By Mr. Gallegos) On the matter of the**
 5 **risk penalty, Mr. Sims, do I understand your**
 6 **testimony that you have stated that the 200 percent**
 7 **risk penalty is common in the industry, and that you**
 8 **frequently see a 300 percent risk penalty in JOAs in**
 9 **the industry?**
 10 **A. I did not say a 200 percent risk penalty**
 11 **is common in a JOA.**
 12 **Q. Okay. Well, what is your testimony in**
 13 **that regard?**
 14 **A. My testimony is a 100/300 percent**
 15 **nonconsent penalty is common in JOAs.**
 16 **Q. Okay. Meaning what, then? The cost of**
 17 **the well is the 100 percent, and then three times**
 18 **the cost of the well would be the 300 percent risk**
 19 **penalty?**
 20 **A. Well, the -- the 100 percent covers some**
 21 **of the tangible costs. The 300 percent covers the**
 22 **intangible costs. The vast majority of the costs**
 23 **are going to come in under 300.**
 24 **So basically, you're getting**
 25 **100 percent -- you're getting your cost back and**

Page 33

1 200 percent.
 2 **Q. So when you refer to a 300 percent**
 3 **penalty, as far as the intangible costs are**
 4 **concerned, the nonconsent party would pay three**
 5 **times that cost?**
 6 **A. Repeat your question, please.**
 7 **Q. Well, I'm trying to clarify what you're**
 8 **telling -- what you're telling the division.**
 9 **A. I'm telling --**
 10 **Q. What happens in terms of recovery of cost**
 11 **by the operator of a non-consenting working interest**
 12 **owner when there is a 300 percent penalty?**
 13 **A. Okay. In the case of a JOA with a**
 14 **nonconsent 300 percent penalty, the -- the operator**
 15 **recovers its cost plus 200 percent.**
 16 **Q. Okay. Recovers its cost three times?**
 17 **A. Correct.**
 18 **Q. All right. And you -- you agree, do you**
 19 **not, that the terms of JOAs are matters of**
 20 **negotiation, like any other contract? In other**
 21 **words, if the parties are addressing the terms of a**
 22 **JOA, they can negotiate the terms including the risk**
 23 **penalty.**
 24 **Do you agree?**
 25 **A. My experience, in having been responsible**

9 (Pages 30 to 33)

Page 34

1 for negotiations of over 2,000 in my career, I have
 2 not seen a single instance where the nonconsent
 3 penalty was less than the 100/300.
 4 To answer your question, it is a voluntary
 5 document between parties, and it can be negotiated.
 6 But we operate in this business under custom and
 7 practice. And the custom and practice is not what
 8 you're saying.
 9 **Q. The custom and practice is not to**
 10 **negotiate?**
 11 A. The custom and practice is not to
 12 negotiate below 100/300. That is not custom and
 13 practice.
 14 **Q. And if an operator such as Matador can**
 15 **come before the division with a forced pooling**
 16 **application, there is no need to agree to anything**
 17 **less than a 200 percent -- 100 percent/200 percent**
 18 **penalty, because that's going to be imposed by order**
 19 **of the commission.**
 20 Isn't that the circumstance?
 21 A. The commission does set the penalty cost
 22 plus 200 percent, or whatever they -- they set.
 23 If that's -- I hope I answered your
 24 question.
 25 **Q. Okay. Well, I would say in the case of**

Page 35

1 communications with a potential non-consenting
 2 party, Matador knows that if it comes before the
 3 commission it's going to receive the 200 percent
 4 risk penalty?
 5 A. We don't necessarily know that until they
 6 grant that.
 7 **Q. Okay. All right.**
 8 So the -- the other factor that you
 9 testified to is that you've seen that there are some
 10 other states, and they -- their law, their statutes,
 11 allow for up to a 200 percent risk penalty?
 12 A. Yes.
 13 **Q. Is that your testimony?**
 14 A. That is my testimony.
 15 **Q. And then the other subject matter you**
 16 **addressed on the question of risk penalty was price**
 17 **risk.**
 18 Could you explain what you mean by that?
 19 A. That I mean by price risk?
 20 **Q. Yes. I mean, I assume your testimony**
 21 **about price risk had something to do with assessment**
 22 **of a risk penalty for non-consenting owners, or am I**
 23 **mistaken?**
 24 It had nothing to do with that?
 25 A. Well, obviously, a change in the price of

Page 36

1 the commodity of oil or gas does have an effect
 2 on -- in a component of risk.
 3 **Q. Well, that's what I'm asking you to**
 4 **explain.**
 5 And maybe -- again, if -- if oil prices
 6 are \$90 a barrel as opposed to \$40 a barrel, then is
 7 that the price risk that you're talking about?
 8 A. Well, I think no matter where you are in
 9 the -- in the continuum of what the price is, if
 10 price goes down it affects your economics. If price
 11 goes up it, arguably, enhances your economics.
 12 **Q. What does that have to do with the risk**
 13 **penalty for a non-consenting owner?**
 14 A. I'm trying to answer your question, sir.
 15 **Q. No, but I'm asking you.**
 16 What does that have to do with the risk
 17 penalty for a non-consenting owner?
 18 A. There is a risk component related to the
 19 price of crude. That is my answer.
 20 **Q. And if prices of oil are \$40 a barrel and**
 21 **it's not economic, then the operator doesn't drill**
 22 **the well, does it?**
 23 A. I think every operator has a risk profile
 24 that they've got to deal with. And I would -- I
 25 would say that in -- that's probably -- as a

Page 37

1 generality, that's probably true. We would not
 2 drill the well if it is uneconomic to you unless
 3 there are other circumstances.
 4 **Q. Does it make a difference if the operator**
 5 **has financial arrangements, hedges, so that it's**
 6 **receiving \$70 a barrel, but the parties who it's**
 7 **seeking to have participate are going to receive \$40**
 8 **a barrel?**
 9 A. Is this a hypothetical that you're asking?
 10 **Q. Yes. I'm trying to understand how --**
 11 **how -- if price risks fit into the risk penalty, if**
 12 **it does.**
 13 A. Obviously, if there's a -- an operator
 14 that's hedged crude, then that would be a factor
 15 that would affect the economics of the project as to
 16 that operator.
 17 **Q. Well, does it also affect the economics of**
 18 **the other working interest owners who might wish to**
 19 **participate or decline to participate?**
 20 A. Well, it would be -- other working
 21 interest owners would likewise have had the same
 22 opportunity to hedge production.
 23 **Q. And you think that's common, that the**
 24 **working interest owners, like -- you know, like**
 25 **these Gustafson trusts, for example, you don't**

10 (Pages 34 to 37)

Page 38

1 really -- you don't really contend, Mr. Sims, that
 2 they're -- that they're hedging their oil prices,
 3 are you?
 4 A. I don't even know who they are, other than
 5 their names.
 6 Q. Well, is there -- besides what you've told
 7 us now, is there anything else that you present to
 8 the division in support of the applications -- in
 9 support of the applicant's request for a 200 percent
 10 risk penalty?
 11 A. I think the support of the risk penalty
 12 will come in witnesses that follow me.
 13 Q. I see. So that -- that covers what you
 14 have to say about it?
 15 A. It does.
 16 Q. Okay. You were asked if you would present
 17 to the examiner the well permitting history.
 18 Do you remember that question?
 19 A. Why don't you ask me specifically.
 20 Q. Well, are you -- are you the witness for
 21 Matador to tell the examiner about the well
 22 permitting history of the -- of this Airstrip well?
 23 A. Well, I can tell you that there was a well
 24 permitted by HEYCO for Bone Springs, a Bone Spring
 25 well.

Page 39

1 And once the merger occurred, I can tell
 2 you that Matador chose not to drill that well.
 3 And then we subsequently permitted the
 4 Airstrip Wolfcamp well that we're talking about
 5 today.
 6 Q. I didn't see in your exhibits a permit for
 7 the Airstrip Wolfcamp well.
 8 Why don't you -- do you have -- can you
 9 provide the APD for -- for a Wolfcamp 201H well?
 10 MS. ARNOLD: If I may, Commissioner. The
 11 permit that he's discussing is of public record.
 12 It's filed with the OCD.
 13 Typically we only include the C-102, but
 14 we would be happy to provide the permit that he's
 15 discussing.
 16 Q. (By Mr. Gallegos) Okay. Well, Mr. Sims,
 17 there's a white notebook -- it should be on the
 18 exhibit stand there.
 19 Would you flip to Exhibit 14?
 20 A. (Witness complies.)
 21 LEAD EXAMINER GOETZE: And for the record,
 22 this is exhibits of Jalapeno and Yates Energy
 23 Corporation?
 24 MR. GALLEGOS: Yes, Mr. Examiner. Thank
 25 you.

Page 40

1 Q. (By Mr. Gallegos) Is the first page,
 2 Mr. Sims, a Form C-101 application for permit to
 3 drill?
 4 A. Yes.
 5 Q. Okay. And is this a permit for drilling a
 6 Bone Springs well?
 7 A. It is a permit to drill a third Bone
 8 Spring well.
 9 Q. Okay. And if you will flip through here,
 10 does it -- does the form include information on the
 11 point of diversion that -- the TVD for the well?
 12 A. What page are you on, sir?
 13 Q. It's the third page.
 14 A. And your question again?
 15 Q. Does this give information on the point of
 16 diversion, the TVD, where you go from vertical to
 17 horizontal?
 18 A. It appears to.
 19 Q. Okay. Does it look like that's at --
 20 10,510 would be the depth we're talking about?
 21 MR. BRUCE: I'd object to this. I mean,
 22 the permit says what it is. It's for a well that's
 23 not being drilled. I fail to see the relevance.
 24 LEAD EXAMINER GOETZE: Where are we going
 25 with this line of questioning?

Page 41

1 MR. GALLEGOS: Well, the line of
 2 questioning is the absence of a permit for the
 3 Wolfcamp well.
 4 All we have is a permit and the
 5 information well plan and other information
 6 necessary to present to the division for the
 7 Wolfcamp well.
 8 Q. (By Mr. Gallegos) Let me ask you to flip
 9 through these pages, Mr. Sims, and see if you can
 10 find, at the next-to-the-last page, a C-103 which is
 11 approved by the division on May 21, 2015.
 12 A. (Witness complies.)
 13 Q. Do you find that? Do you find that page
 14 of Exhibit 14?
 15 A. Yes, I do.
 16 Q. All right. And are you familiar with the
 17 form which is called -- referred to as the sundry
 18 notice?
 19 A. Yes.
 20 Q. And does that have, in print sort of in
 21 the open space there:
 22 "Note: Change of formation being
 23 Airstrip; Wolfcamp 970, see attached C-102."
 24 A. I see those words.
 25 Q. All right. Do you know if there is

11 (Pages 38 to 41)

Page 42

1 anything else provided to the division other than
 2 this, such as a directional plan for this Wolfcamp
 3 well?
 4 A. I'm not the right witness for that. I do
 5 not know.
 6 Q. Well, you were asked whether you would be
 7 able to provide the permitting history, and that's
 8 what I'm asking you about.
 9 What has been presented to the division
 10 other than what we have here?
 11 A. My understanding is we have a permit to
 12 drill this Wolfcamp well.
 13 Q. And it's a permit other than the permit
 14 for what was a Bone Springs well?
 15 A. It is a different permit, yes, sir.
 16 Q. Okay. And that will be provided by some
 17 other witness.
 18 Is that your understanding?
 19 A. They will be prepared to discuss the
 20 permit.
 21 Q. I see. Okay.
 22 Let's go back to your exhibits.
 23 And Exhibit 2, is this your exhibit that
 24 shows the 7.3 percent ownerships, various ownerships
 25 of parties that you are asking the division to force

Page 43

1 pool?
 2 A. Yes. Exhibit 2 of Matador's exhibits sets
 3 out 7.32 percent that we are asking the division to
 4 compulsory pool.
 5 Q. What has Matador done in regard to these
 6 Gustafason trustees, other than send them a well
 7 proposal and an AFE?
 8 A. We -- you may recall that we had one
 9 party, that was a Kadane, who did elect under one of
 10 our options. We had discussions with that
 11 individual about the family members.
 12 And I believe also, we did send either an
 13 e-mail or make additional contact, and these people
 14 would not communicate with us.
 15 Q. What would be their share, in dollar
 16 amount, of this \$9 million well?
 17 A. Are you referring to all of these parties
 18 below?
 19 Q. I'm referring to the two trusts.
 20 A. The two trusts?
 21 It looks like it's about -- it's a very
 22 small percentage, sir. I --
 23 Q. I was asking about dollar amount, what it
 24 would mean to these people, trustees, if they
 25 were...

Page 44

1 A. I don't know. I am not familiar with the
 2 trust.
 3 Q. No. You're familiar with \$9 million and
 4 their percentage of interest, are you not?
 5 A. Yes, I am.
 6 Q. So that's the question.
 7 A. I do not follow your question.
 8 Q. The question is: In dollar amount, what
 9 would it be required of these parties to participate
 10 in this well?
 11 A. They would have to pay their pro rata
 12 part, whatever the amount is, of the percentage of
 13 that well.
 14 Q. Or --
 15 A. Or they would --
 16 Q. Or engage an attorney to protest the
 17 proceeding?
 18 A. Or engage with us so we can try to do a
 19 deal with them.
 20 Q. I probably missed it, but if you will turn
 21 to your Exhibit 9.
 22 A. (Witness complies.)
 23 Q. I didn't see anything there that referred
 24 to attempts to work out a deal with the Gustafason
 25 trusts.

Page 45

1 MR. BRUCE: Excuse me.
 2 Do you mean Exhibit 6?
 3 MR. GALLEGOS: Did I say 9? I was upside
 4 down. 6. I was looking at the back side of the
 5 tab.
 6 Q. (By Mr. Gallegos) I'm sorry, Mr. Sims. I
 7 meant to refer to Exhibit 6.
 8 A. So you're in Exhibit 6 now?
 9 Q. Yes, sir.
 10 A. Okay.
 11 Q. So in March of 2015, you sent out the
 12 proposal?
 13 A. That is correct.
 14 Q. And then as I understand, the rest of this
 15 summary was presented for purposes of informing the
 16 division of what had gone on in terms of seeking
 17 voluntary agreement with these working interest
 18 owners?
 19 A. Correct.
 20 Q. I -- do we understand that you did nothing
 21 in terms of those trusts, other than send out the
 22 proposal? Because I see nothing on here that refers
 23 to that, unless I missed it.
 24 A. We had discussions with Mr. Bob Kadane.
 25 Q. Okay. And what -- can you tell us, what

12 (Pages 42 to 45)

1 was the contents of those discussions?
 2 A. To encourage him to get the trust to
 3 respond to our letter.
 4 Q. And what happened?
 5 A. We received no response.
 6 Q. Now, let's turn to Jalapeno.
 7 Again in our exhibit book -- it's the
 8 white notebook, Mr. Sims.
 9 Turn your attention to Exhibit 4, please.
 10 A. I'm ready.
 11 Q. Okay. This is a letter from Harvey Yates,
 12 Junior, to Melissa Randall, land manager.
 13 Is she part of your division or group at
 14 Matador?
 15 A. She is an employee of Matador, correct.
 16 Q. Okay. And did Mr. Yates present an
 17 alternative or a counterproposal to the proposal
 18 that was sent out in March to all the working
 19 interest owners?
 20 A. Mr. Yates did send a letter where he
 21 suggested various options on how to proceed.
 22 Q. Okay. And he closed the letter by saying:
 23 "We would agree to sell MRC a one-year
 24 term lease covering our interest in the Wolfcamp
 25 underlying the spacing unit for \$5,000 per net acre.

1 We would receive an ORR equal to the difference
 2 between 25 percent in the existing burdens.
 3 "If you are interested in this, please let
 4 us know."
 5 Wasn't that a fair and reasonable
 6 proposal, Mr. Sims?
 7 A. It is not the entire entirety of the
 8 offer.
 9 Q. Well, did the offer also complain about
 10 the risk penalty in the proposed joint operating
 11 agreement?
 12 A. That is correct.
 13 Q. Okay. And Matador was not willing to
 14 budge 1 percent on the risk penalty, was it?
 15 A. We are not, and were not, willing to
 16 accept something that does not represent custom and
 17 practice in our industry.
 18 Q. Okay.
 19 A. So we would not go below a 100/300 percent
 20 nonconsent penalty in the JOA.
 21 Q. And that's because it's custom and
 22 practice in the industry?
 23 A. It is absolutely custom and practice.
 24 Q. Thank you, sir.
 25 Did Mr. Yates also raise some questions

1 about why the well cost had moved from 7 million to
 2 9 million?
 3 A. Yes, he did.
 4 Q. Was he provided any information in that
 5 regard?
 6 A. I think the \$7 million cost was for a Bone
 7 Spring well. And obviously, when you're going
 8 deeper and you may need another string of pipe or
 9 something -- and our other witnesses can testify to
 10 this better than I can. Clearly, costs will
 11 increase as you drill deeper.
 12 Q. How much deeper -- and that's why I was
 13 asking before about the -- about the deviation.
 14 What was the difference in deviation depth
 15 between the Bone Springs and this Wolfcamp well?
 16 A. I'm not your right witness.
 17 Q. Well, let's say -- let's say it's
 18 300 feet. Do you think that's -- that adds
 19 \$1.8 million to the well cost?
 20 A. I'm not going to speculate. I have no
 21 knowledge.
 22 Q. All right. So in terms of Mr. Yates'
 23 proposal of 5,000 an acre, the proportionately
 24 reduced override, Matador was not willing to give
 25 one inch or one percent concerning the risk penalty.

1 Isn't that the circumstance?
 2 A. Well, the circumstance is that Jalapeno
 3 was not willing to give one inch.
 4 Q. By not accepting what Matador requires as
 5 the risk penalty?
 6 A. Superimposed in every communication is, I
 7 will not do this. I -- how many times -- and I can
 8 point to it in various letters -- where Mr. Yates
 9 indicates, I'm not going to accept anything with a
 10 risk -- to any JOA with a risk penalty of 100/300.
 11 Q. Is it accurate to say that was the single
 12 condition that stood in the way of reaching
 13 voluntary agreement?
 14 A. Well, there were a lot of various side
 15 issues. But clearly, this was a major stumbling
 16 block between the two parties.
 17 Q. Now, you referred to a -- I think you said
 18 a June 3, 2015, meeting.
 19 A. I did.
 20 Q. Was not this forced pooling application
 21 proceeding already underway?
 22 A. I don't recall exactly when we started
 23 that process. I -- to my knowledge, it was not. We
 24 had not filed anything by that point.
 25 Q. Was it -- was it said by Mr. Foran, or

1 anybody else who was representing Matador at that
2 meeting, that we are -- we expect to or plan to file
3 an application with the New Mexico Oil Conservation
4 Division to force pool your interests?

5 A. As I've mentioned, there were I believe,
6 like, five different options made available to them,
7 and one of those options was a forced pool. It is
8 one of the tools that we use in this industry to get
9 wells drilled when we can't get voluntary joinder.

10 And so Mr. Foran would have listed the
11 five or so options made available.

12 And I don't recall precisely the wording
13 that he would have used, but I would agree that the
14 words of forced pool were probably used in some
15 context.

16 Q. And I -- and I appreciate that your answer
17 might be an estimate, not specific.

18 But how many horizontal wells has Matador
19 drilled in the Permian Basin of Southeast
20 New Mexico?

21 A. Well, you know, I don't want to guess.
22 I've been an employee for about six months, and
23 there were a number of wells drilled before I
24 started with Matador, so I really wouldn't be aware
25 of that number.

1 So I'm not going to give you some
2 inaccurate information.

3 Q. Well, to your knowledge, in any of those
4 wells has there been a voluntary agreement between
5 Matador's operator and nonoperating working interest
6 owners in regard to a negotiated percent of a risk
7 penalty?

8 A. A negotiated percent of a risk penalty?

9 Now, explain. Are you referring to a risk
10 penalty under a forced pooling or under a JOA
11 nonconsent?

12 Q. I'm starting with a JOA and just asking
13 you: Has there been a situation where Matador said,
14 Okay. We want to work with you so we'll -- we'll
15 give, and we won't require the
16 100 percent/300 percent in order to have agreement.

17 Has there been any instance of that sort
18 that you can tell us?

19 A. And as I said, custom and practice in our
20 industry is for a 100/300 percent nonconsent
21 penalty.

22 That is the penalty that Devon uses.
23 That's the penalty that Cimarex uses. That's the
24 penalty that virtually all oil and gas companies
25 use.

1 If not that, it is more.

2 Q. I guess I'm not making my question clear.
3 You've told us that.

4 I understand you're -- you're land
5 manager?

6 A. Operations land manager.

7 Q. Operations land manager. Which means, I
8 guess, several other landmen work under your
9 supervision?

10 A. That would be correct.

11 Q. You head the department. Is that the
12 status?

13 A. I have a vice president of land that I
14 report to.

15 Q. Okay. So, Mr. Sims, to make my question
16 as clear as possible, I'm not asking about custom
17 and practice.

18 I am asking if you can tell us if there
19 has been any occasion in which Matador has agreed to
20 a lesser nonconsent risk penalty with a nonoperating
21 working interest owner in order to arrive at
22 agreement?

23 A. I don't recall, other than this particular
24 instance here, where anyone has asked for something
25 less than what is custom and practice.

1 Q. And in the case of any forced pooling
2 applications, do you know of any instance in which
3 Matador has achieved other than the 200 percent risk
4 penalty -- other than the 200 percent risk penalty?

5 A. Not to my knowledge. I'm not aware of
6 that.

7 Q. Okay.

8 MR. GALLEGOS: That's all the questions
9 that I have. Thank you, Mr. Sims.

10 FURTHER EXAMINATION

11 BY MR. BRUCE:

12 Q. First to clarify, so that there's no
13 question, when you're talking about forced pooling,
14 you're talking about cost plus 200 percent --

15 A. Correct.

16 Q. -- on the risk charge.

17 That is equivalent to a JOA 300 percent
18 nonconsent?

19 A. Roughly, it would.

20 Q. And Mr. Gallegos asked you about the
21 Kadane trust.

22 I think your answer was they never
23 responded to you.

24 A. That is correct.

25 Q. It's hard to negotiate with someone who

Page 54

1 won't respond to you?

2 A. It's difficult.

3 Q. And when you were being questioned

4 about -- about Matador using -- you know, raising

5 the issue of forced pooling, Matador would prefer to

6 have everybody voluntarily join in the well one way

7 or the other, would it not?

8 A. Yes, absolutely.

9 Q. And not pay me?

10 A. Yes. Especially not pay you.

11 Q. But in looking at the proposal letters --

12 (Discussion off the record.)

13 Q. (By Mr. Bruce) But originally, other than

14 the Matador entities there were, it looks like,

15 20-plus uncommitted working interest owners?

16 A. Correct.

17 Q. And now there's five, I believe. So you

18 have --

19 MR. GALLEGOS: I have to object. This is

20 not proper redirect. This is just starting the case

21 over. We've gone through that.

22 LEAD EXAMINER GOETZE: Well, I'll give

23 Mr. Bruce the opportunity to highlight those, and

24 we'll continue to move on.

25 MR. BRUCE: This is the last question.

Page 55

1 Q. (By Mr. Bruce) You went from 20 to over

2 5. It shows that Matador wanted to negotiate with

3 the parties?

4 A. Absolutely. We -- we did everything we

5 could do, reasonably do, with all of these

6 uncommitted owners to get them rounded up and

7 perhaps make some kind of a deal that we could live

8 with.

9 MR. BRUCE: Thank you.

10 That's all I have, Mr. Examiner.

11 LEAD EXAMINER GOETZE: Let's take a break.

12 We'll let you have -- let's come back at 10:30 and

13 we'll start up again.

14 (A recess was taken from 10:14 a.m. to

15 10:31 a.m.)

16 LEAD EXAMINER GOETZE: We are back on the

17 record, and we will continue with the questions for

18 this witness.

19 Mr. Wade?

20 MR. WADE: I do not have any questions at

21 this time.

22 LEAD EXAMINER GOETZE: Very good.

23 Mr. Jones?

24 MR. JONES: Mr. Sims, is there a -- can

25 you explain the relationship between MRC and

Page 56

1 Matador? It was talked about before already.

2 But who's making the application in this

3 case? Is it MRC or is it Matador?

4 THE WITNESS: It's -- Matador Production

5 Company is the operator of the well.

6 MR. JONES: Are they the applicant in the

7 case?

8 MR. BRUCE: They are, Mr. Examiner.

9 MR. JONES: Okay.

10 MR. BRUCE: It's on the application.

11 MR. JONES: Okay. All right.

12 I was kind of brought in late here. I

13 have it in front of me.

14 Do you -- these are two state leases.

15 Is that correct?

16 THE WITNESS: That is correct.

17 MR. JONES: It looks like they are older

18 leases. They are one-eighth royalty?

19 THE WITNESS: Yes. I believe that is the

20 case.

21 MR. JONES: And they've got several

22 assignments. This is like numerous assignments down

23 the line?

24 THE WITNESS: Right.

25 MR. JONES: Do you know the history of

Page 57

1 them?

2 THE WITNESS: I'm not personally familiar

3 with the history of the -- the assignments that have

4 occurred over time.

5 Obviously we have recently acquired some

6 of these interests, as we've tried to get this thing

7 ready for drill.

8 MR. JONES: So you're pooling only working

9 interests, and you're pooling only working interests

10 that can be located, even though you didn't get some

11 green cards back?

12 MR. BRUCE: I think Mr. Sims could answer

13 this, Mr. Examiner.

14 But I think everybody was locateable. As

15 I said with respect to the notice exhibits, I did

16 not get one green card back from one interest owner.

17 But the post office records show that it was

18 delivered. The green card disappeared somewhere

19 along the way.

20 MR. JONES: And as far as notifying the

21 people around them, you didn't get one back from

22 them either?

23 THE WITNESS: Correct.

24 MR. JONES: Okay. So -- but that was

25 posted in the newspaper, those names?

15 (Pages 54 to 57)

| Page 58 | Page 60 |
|---|--|
| <p>1 MR. BRUCE: Those names are in the 2 affidavit of publication. 3 MR. JONES: Okay. 4 So as an attorney, did you do the opinion 5 on this 154-acre -- 6 THE WITNESS: No, sir. 7 MR. JONES: You farm that out -- 8 THE WITNESS: We have outside -- 9 MR. JONES: -- outside -- 10 THE WITNESS: -- attorneys that do that, 11 yes. 12 MR. JONES: And the JOA that -- is that -- 13 you use -- pretty much use the standard JOA for 14 New Mexico or... 15 THE WITNESS: We typically use the 1989 16 version of the form JOA that's put out by the 17 American Association of Professional Landmen. 18 MR. JONES: Okay. It hasn't changed much 19 over the years? 20 THE WITNESS: It -- you know, there have 21 been four or five different versions of the JOA. In 22 fact, I believe they're working on a newer version 23 as we speak. 24 Most companies will also add some changes 25 or modifications to the form to fit circumstances.</p> | <p>1 THE WITNESS: I don't have that -- that 2 information of when the title opinion was finalized. 3 But we do, as a matter of course, wait 4 until we know the working interest owners, based on 5 the title opinion that is rendered by outside 6 counsel. 7 And usual practice after that, is to then 8 make a well proposal based on what we believe is 9 the -- is the ownership confirmed by the opinion of 10 an attorney. 11 MR. JONES: So basically, you don't know 12 exactly when? 13 THE WITNESS: I don't know exactly when. 14 MR. JONES: Okay. But it was relatively 15 soon, or would you like to speculate or not? That's 16 fine if you don't. 17 THE WITNESS: You know, I don't know. I 18 would hate to speculate exactly when it occurred. 19 But I mean, we can -- we can provide that 20 to you at some point if you would like. 21 MR. JONES: It wasn't -- it wasn't a month 22 ago, though? It was further back than that? 23 THE WITNESS: No, this was quite a while 24 back. Yeah. 25 MR. JONES: 75 percent net NRI. That is</p> |
| Page 59 | Page 61 |
| <p>1 For example, with horizontal drilling, a 2 lot of the form doesn't work real well, so we try to 3 make it work a little better. 4 MR. JONES: So this is all happening since 5 March of this year. 6 Is that correct? 7 THE WITNESS: Yes, that is correct. 8 MR. JONES: Because that is when you took 9 it over from HEYCO? 10 THE WITNESS: Right. 11 MR. JONES: And you do intend to get a 12 more -- as far as the application for permit to 13 drill, it -- I see that Paul Kautz signed off on the 14 sundry, but you -- are you going to send him a new 15 C-101, or is that another witness, or is that 16 something you know about or not? 17 THE WITNESS: Well, I do not know the 18 details on that. If we aren't -- if we haven't 19 supplied the OCD or any other agency of the 20 government with something that's required, we will 21 do that. 22 MR. JONES: Okay. As of March of 2015, 23 did you know everybody that -- how soon -- how soon 24 after that did you get your title opinion down for 25 this?</p> | <p>1 low, don't you think? I mean, how can you make any 2 money doing that? 3 THE WITNESS: Well, obviously, we would 4 prefer something a little higher. But... 5 MR. JONES: When you start out with a base 6 lease that has one-eighth royalty and you're willing 7 to go down 75 percent? 8 THE WITNESS: You know there's been a lot 9 of assignments. There's probably overrides and 10 whatnot to other individuals that have capped along 11 the way. 12 I don't know exactly what the -- what the 13 net revenue interest that Yates and Jalapeno has. 14 But you know, we were proposing a deal 15 that would allow them to keep potentially up to 16 25 percent of eight-eighths as well. 17 It -- it's -- sure. We would like 18 something better, but I think we can live with the 19 25 percent of the eight-eighths as outstanding 20 burdens. 21 MR. JONES: Okay. The economics of -- 22 of -- I guess they're -- 23 THE WITNESS: I can -- I can clarify one 24 thing. 25 With the proposal that went out on</p> |

16 (Pages 58 to 61)

| Page 62 | Page 64 |
|--|---|
| <p>1 March 24, that's an indication that we had title 2 before then.</p> <p>3 MR. JONES: Okay. But basically, if you 4 agree to go down to 75 percent with some owners that 5 haven't signed, in order to get them to sign, that 6 penalizes the other owners also, doesn't it, on it, 7 or does it?</p> <p>8 THE WITNESS: Penalize?</p> <p>9 MR. JONES: In other words, that lowers 10 their NRI also, the people that have already joined 11 in the well.</p> <p>12 THE WITNESS: No. A deal that we would do 13 with someone that's not associated with a party 14 that's already elected, their NRI is what it is.</p> <p>15 MR. JONES: Okay.</p> <p>16 THE WITNESS: We're not going to affect 17 that by -- by a -- by an agreement that we enter 18 into with a third party.</p> <p>19 MR. JONES: Okay. But it would penalize 20 Matador's NRI?</p> <p>21 THE WITNESS: Yes, it would. It would 22 lessen our NRI.</p> <p>23 MR. JONES: So it would make your 24 decisions to go forward with drilling -- obviously, 25 you -- you want to drill this well. But even</p> | <p>1 within the bounds of the questions asked by the 2 examiner, please.</p> <p>3 THE WITNESS: Okay.</p> <p>4 MR. JONES: Okay. What do you -- what 5 is -- what do you think the maximum dollars per acre 6 you've offered for any lease in New Mexico so far, 7 MRC, and actually procured the property?</p> <p>8 THE WITNESS: Well, we -- we've paid 9 less -- greater than 10,000 an acre in certain 10 instances.</p> <p>11 MR. JONES: Okay. When we -- obviously, 12 you're not the person to ask about the Wolfcamp 13 formation.</p> <p>14 What about -- which working interest owner 15 would have -- would be the most -- most experienced 16 in -- and have the most facilities in this area?</p> <p>17 Does Matador have any other wells in this 18 area?</p> <p>19 THE WITNESS: It's a fairly new area for 20 us, in terms of drilling Wolfcamp wells. We're in 21 what we call a delineation mode, and so we're kind 22 of stepping out. And this would be an example of a 23 well that would pick that category.</p> <p>24 We do have probably some -- some vertical 25 wells in that neighborhood. And I don't know of</p> |
| Page 63 | Page 65 |
| <p>1 subsequent wells it would make them more difficult?</p> <p>2 THE WITNESS: We -- we, obviously, look at 3 what we could live with from an economic standpoint, 4 and we would not agree to -- to these terms if we 5 couldn't make it work for us.</p> <p>6 I have a point of clarification, if I 7 could, Mr. Examiner.</p> <p>8 I would like to point to the April 28 9 letter that Jalapeno sent to Matador, to Melissa 10 Randall. The last -- effectively the last paragraph 11 was mentioned about Mr. Yates, Mr. Harvey Yates, 12 saying that he's willing to sell his position at 13 5,000 an acre.</p> <p>14 I'm sure you will remember that.</p> <p>15 MR. GALLEGOS: Mr. Examiner, this -- I 16 don't think this is proper, the witness deciding 17 he's going to start his direct again.</p> <p>18 LEAD EXAMINER GOETZE: Let's state 19 comments to what the questions are asked at this 20 point and you have already offered up.</p> <p>21 THE WITNESS: Okay.</p> <p>22 LEAD EXAMINER GOETZE: I mean, we can read 23 the exhibits.</p> <p>24 THE WITNESS: Okay.</p> <p>25 LEAD EXAMINER GOETZE: So let's stay</p> | <p>1 any -- I don't think we have any Wolfcamp wells 2 anywhere near this location.</p> <p>3 But as with every company, you try to 4 build your position from where you are. In most 5 cases you're going to start from zero and try to 6 grow your position.</p> <p>7 MR. JONES: These -- this risk penalty 8 discussion, that -- our order that actually 9 established the uniform risk penalty, the compulsory 10 pooling, is -- have you read that order?</p> <p>11 THE WITNESS: Yes, sir, I have.</p> <p>12 MR. JONES: Okay. Do you -- is there a 13 provision in there to contest the risk penalty?</p> <p>14 THE WITNESS: There's a provision in there 15 that says that the penalty is 200 percent unless 16 somebody -- a party opposes that and argues that a 17 different penalty should -- should prevail.</p> <p>18 MR. JONES: Okay. Thank you. I have no 19 more questions.</p> <p>20 LEAD EXAMINER GOETZE: Very good. I only 21 have one question.</p> <p>22 The application was made on a petition for 23 compulsory pooling, not only to Wolfcamp, but all 24 pools with 40-acre spacing.</p> <p>25 What is the reason behind that form of the</p> |

17 (Pages 62 to 65)

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| <p style="text-align: right;">Page 66</p> <p>1 application? Why are we seeking other than Wolfcamp 2 to compulsory pool? 3 THE WITNESS: I think probably other 4 witnesses can better answer that question, 5 Mr. Examiner. 6 LEAD EXAMINER GOETZE: Okay. So at this 7 point, as far as lands? 8 THE WITNESS: I'm not -- I'm not the best 9 witness on that question. 10 LEAD EXAMINER GOETZE: Very well. Then at 11 this point there are no more questions for this 12 witness. 13 Thank you very much. 14 Your next witness. 15 MR. BRUCE: Okay. I would make -- to your 16 last statement, Mr. Examiner, the application 17 clearly asks only to pool the Wolfcamp formation. 18 LEAD EXAMINER GOETZE: Well... 19 MR. BRUCE: If we go to the wherefore 20 ones... 21 LEAD EXAMINER GOETZE: At that point, 22 let's let the examiner play. 23 And in my application I have oil spacing 24 and proration project area for any formations or 25 pools developed on 40-acre spacing within the</p> | <p style="text-align: right;">Page 68</p> <p>1 JAMES ANDREW JUETT, 2 after having been first duly sworn under oath, 3 was questioned and testified as follows: 4 EXAMINATION 5 BY MR. BRUCE: 6 Q. Mr. Juett, where do you reside? 7 A. Flower Mound, Texas. 8 Q. Who do you work for and in what capacity? 9 A. I am employed by MRC Energy Company, an 10 affiliate of Matador Production Company, as a senior 11 geologist. 12 Q. What are your responsibilities as a 13 geologist for Matador? 14 A. To recommend and evaluate new drill 15 opportunities, workovers, recompletion candidates, 16 evaluate potential acreage acquisitions, and 17 generate new prospect ideas. 18 Q. Have you previously testified before the 19 division and been qualified as an expert geologist? 20 A. Yes, I have. 21 Q. For the record, could you summarize your 22 educational and employment background? 23 A. Yes. I received a bachelor of science 24 degree from West Texas State University in Canyon, 25 Texas, with a math minor.</p> |
| <p style="text-align: right;">Page 67</p> <p>1 vertical extent. 2 MR. BRUCE: And I think if you go to the 3 very first paragraph it says: 4 "Applies for an order approving a 5 nonstandard unit in the Wolfcamp formation and 6 pooling mineral interests in the Wolfcamp 7 formation." 8 LEAD EXAMINER GOETZE: That's true. But 9 then we include everything else in Number 2. So... 10 MR. BRUCE: And at the end it also asks 11 just for the Wolfcamp, and that's all that Matador 12 is asking for. 13 LEAD EXAMINER GOETZE: So it is clearly 14 that, in this application, you're only looking at 15 Wolfcamp? 16 MR. BRUCE: We are only looking at 17 Wolfcamp. 18 LEAD EXAMINER GOETZE: Very good. Thank 19 you very much. 20 Continue. 21 MR. BRUCE: I will call Mr. Juett to the 22 stand. 23 (Witness sworn.) 24 THE WITNESS: I'm James Andrew Juett. 25</p> | <p style="text-align: right;">Page 69</p> <p>1 I began my career as a geologist with Mesa 2 Petroleum in Amarillo, Texas, which is now Pioneer 3 Natural Resources. 4 I left Pioneer in 1998 and joined Prize 5 Energy, who was then bought by Magnum Hunter 6 Resources. 7 And after leaving Magnum Hunter Resources 8 I joined Matador in 2003, where I -- my work 9 concentrated basically on unconventional reservoirs 10 including the Haynesville Shale, the Eagleford 11 Shale, the Phosphoria Shales. In West Texas that 12 included Bone Spring and Wolfcamp formations in the 13 Midland and Delaware Basins. 14 And then in 2013 I went to work for 15 Comstock Resources. And after a brief stay at 16 Comstock, I moved to Laredo Petroleum. 17 And then in February of 2015 I came back, 18 after Laredo closed their office in Dallas. I came 19 back to Matador to work the Delaware Basin. 20 Q. Do you have any certifications or belong 21 to any professional associations? 22 A. Yes. I'm a member of the American 23 Association of Petroleum Geologists, a member of the 24 West Texas Geological Society, and a member of the 25 Dallas Geological Society. And I'm a past treasurer</p> |

18 (Pages 66 to 69)

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| <p style="text-align: right;">Page 70</p> <p>1 of that organization.</p> <p>2 Q. Are you familiar with the geology of the</p> <p>3 land involved in the -- this application?</p> <p>4 A. Yes, I am.</p> <p>5 Q. And have you conducted a geologic study of</p> <p>6 the area embracing the proposed spacing unit for the</p> <p>7 Airstrip State Com 201H well in Section 31?</p> <p>8 A. Yes.</p> <p>9 MR. BRUCE: Mr. Examiner, I tender</p> <p>10 Mr. Juett as an expert petroleum geologist.</p> <p>11 LEAD EXAMINER GOETZE: Mr. Gallegos?</p> <p>12 MR. GALLEGOS: No objection.</p> <p>13 LEAD EXAMINER GOETZE: Very well. He is</p> <p>14 so qualified.</p> <p>15 Q. (By Mr. Bruce) Mr. Juett, could you</p> <p>16 identify Exhibit 12 for the examiner and discuss its</p> <p>17 contents?</p> <p>18 A. Yes. Exhibit 12 is a structure map that</p> <p>19 is made on -- it's a subsea structure map that is</p> <p>20 made on the top of the Wolfcamp formation in the</p> <p>21 subject area.</p> <p>22 And it also shows the different producing</p> <p>23 formations for each of the horizontals that we have</p> <p>24 been able to land from state records, the first,</p> <p>25 second, and third Bone Spring.</p> | <p style="text-align: right;">Page 72</p> <p>1 to drilling this well to the Wolfcamp formation?</p> <p>2 A. There are none that I can see by the</p> <p>3 mapping that I've done.</p> <p>4 Q. And did you prepare a cross-section for</p> <p>5 this hearing?</p> <p>6 A. Yes, I did.</p> <p>7 Q. And is that marked as Exhibit 13?</p> <p>8 A. Yes, it is.</p> <p>9 Q. Please discuss the contents of that plat</p> <p>10 for the examiner.</p> <p>11 A. Okay. This cross-section shows it's a --</p> <p>12 it's hung on the top of the upper Wolfcamp, the</p> <p>13 formation. That's the datum on the cross-section.</p> <p>14 It shows the relative thickness of the</p> <p>15 Wolfcamp formation is fairly uniform across it.</p> <p>16 It also shows that the third Bone Spring</p> <p>17 sand thins as we move to the east. In the cross --</p> <p>18 this cross -- the cross-section.</p> <p>19 What -- the other thing that this</p> <p>20 cross-section shows is that the porosity is greatly</p> <p>21 diminished from the -- in the third Bone Spring than</p> <p>22 it is in the upper Wolfcamp zone.</p> <p>23 And then we also show the -- the bold red</p> <p>24 line shows the proposed lateral in the upper</p> <p>25 Wolfcamp.</p> |
| <p style="text-align: right;">Page 71</p> <p>1 It shows the -- the unit that we are</p> <p>2 looking to pool, with the surface and bottom hole</p> <p>3 location of the Airstrip well in the dark blue</p> <p>4 circle and square. And then also the data points</p> <p>5 used to make this map are in the purple.</p> <p>6 And then you will also see the</p> <p>7 cross-section AA prime, which will be in a future</p> <p>8 exhibit, its location.</p> <p>9 Q. And does Matador intend to drill and</p> <p>10 complete this well in the Wolfcamp formation?</p> <p>11 A. Yes.</p> <p>12 Q. The land witness testified earlier that</p> <p>13 HEYCO originally proposed this well as a Bone Spring</p> <p>14 proposal.</p> <p>15 Is that correct?</p> <p>16 A. That is correct.</p> <p>17 Q. Why did you recommend changing the target</p> <p>18 formation to the Wolfcamp?</p> <p>19 A. When we looked at the third Bone Spring,</p> <p>20 the formation thins as we move across the section.</p> <p>21 The porosity in Wolfcamp is much better than the</p> <p>22 porosity in the third Bone Spring, and we thought we</p> <p>23 would make a much better chance of making an</p> <p>24 economic well out of the upper Wolfcamp zone here.</p> <p>25 Q. Are there any known geological impediments</p> | <p style="text-align: right;">Page 73</p> <p>1 Q. Now, do you consider the wells in this</p> <p>2 cross-section representative of the Wolfcamp</p> <p>3 formation in this area?</p> <p>4 A. Yes, I do.</p> <p>5 Q. Would you move on to Exhibit 14, and</p> <p>6 identify that for the examiner?</p> <p>7 A. Yes, sir. This is a gross thickness</p> <p>8 isopach map of the Wolfcamp formation in the area.</p> <p>9 And it shows that over the unit well area that we</p> <p>10 have fairly uniform thickness. There's no major</p> <p>11 thickness changes in this area and in the Wolfcamp</p> <p>12 zone.</p> <p>13 It also shows that the thickness is around</p> <p>14 a thousand to 1,100 feet across the area.</p> <p>15 Q. And what conclusions have you drawn from</p> <p>16 your geologic study of this area?</p> <p>17 A. We believe there will be no impediments to</p> <p>18 drilling a horizontal well in this area, and we</p> <p>19 fully expect each quarter/quarter section to be</p> <p>20 productive in the Wolfcamp formation.</p> <p>21 We also expect horizontal drilling to be</p> <p>22 the most efficient method to develop this acreage</p> <p>23 and we will avoid drilling unnecessary wells.</p> <p>24 Q. Mr. Juett, during preparation over the</p> <p>25 past couple of months for the hearing, do you know</p> |

19 (Pages 70 to 73)

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| <p style="text-align: right;">Page 74</p> <p>1 that Jalapeno and Yates claim that the forced 2 pooling of horizontal wells is not permissible? 3 A. Yes. 4 Q. As a geologist, would you recommend to 5 management drilling four vertical horizontal wells 6 in this 160 acres? 7 A. No, I could not. 8 Q. Why? 9 A. It gets down to area of reservoir that's 10 going to be touched in a vertical well. In this 11 upper Wolfcamp section, each four vertical wells 12 would be the equivalent of basically one stage of a 13 horizontal well. And we plan on putting 15 stages 14 in the well, and I believe that it would strand 15 reserves and create waste. 16 Q. Moving ahead a couple of exhibits to 17 Exhibit 17. 18 A. (Witness complies.) 19 Q. Could you identify that exhibit and 20 discuss its contents briefly? 21 A. Yes. This is a map that shows the unit 22 area that -- where we're proposing the pooling. And 23 the green outline with the -- the green box with the 24 red outline. 25 This also shows the Wolfcamp wells that</p> | <p style="text-align: right;">Page 76</p> <p>1 And so there are several variables. One, 2 the porosity and permeability being preserved in the 3 area. But... 4 Q. And you won't know that until you drill 5 the well? 6 A. That's right. 7 Q. From a geologic standpoint, is a risk 8 charge of cost plus 200 percent justified in this 9 case? 10 A. Yes, sir. I believe it is. 11 Q. Finally, could you move back to Exhibit 15 12 and just briefly discuss that for the examiner? 13 A. Yes, sir. This is a wellbore diagram that 14 shows the location of how the well will be placed in 15 the section. 16 It shows the surface and bottom hole 17 locations and their respective measurements to the 18 section lines. 19 It shows the first and last take points 20 that we plan in this well. 21 Q. And will -- the completed interval, will 22 it -- the beginning and the ends of the completed 23 interval be orthodox? 24 A. Yes, sir. 25 Q. In your opinion is the granting of</p> |
| <p style="text-align: right;">Page 75</p> <p>1 have been drilled in the area. And what this 2 shows -- what we've posted on the map is -- is 3 that -- are the casing designs that were used for 4 each of these wells. 5 The other thing to note is that -- on this 6 map -- is that all of these wells have been drilled 7 to a deeper zone in the Wolfcamp. They have not 8 been drilled for the upper Wolfcamp zone. 9 Q. Even with that in mind, how close is the 10 nearest Wolfcamp well? 11 A. The nearest Wolfcamp well is a well that 12 Matador drilled, and it is five miles to the 13 north -- northwest. 14 Q. And of course this does show -- going back 15 to a prior question by Mr. Jones -- who the other 16 Wolfcamp operators are in this area? 17 A. Yes, sir. 18 Q. How do you define geologic risk? 19 A. Well, there's multiple parts in that. The 20 first part is, is the zone present or absent? 21 That's the big question. Is the zone present or 22 absent? 23 And then after that we get down to, is the 24 zone going to be -- have porosity, permeability, 25 well enough to produce at economic rates?</p> | <p style="text-align: right;">Page 77</p> <p>1 Matador's application in the interest of 2 conservation and the prevention of waste? 3 A. Yes. 4 Q. And were Exhibits 12 through 15 and 17 5 prepared by you or compiled under your direction and 6 control? 7 A. Yes, they were. 8 MR. BRUCE: Mr. Examiner, I would move the 9 admission of Exhibits 12 through 15 and 17. 10 LEAD EXAMINER GOETZE: Mr. Gallegos? 11 MR. GALLEGOS: No objection, Mr. Examiner. 12 LEAD EXAMINER GOETZE: Very good. 13 Exhibits 12 through 15 and 17 are so entered. 14 MR. BRUCE: I pass the witness. 15 LEAD EXAMINER GOETZE: Mr. Gallegos, your 16 witness. 17 EXAMINATION 18 BY MR. GALLEGOS: 19 Q. Mr. Juett, let's first direct your 20 attention to Section 31. 21 A. Okay. 22 Q. What are the extent of vertical 23 penetrations by wells in Section 31 in the Wolfcamp? 24 A. There are the -- there's two penetrations 25 in Section 31, vertical penetrations.</p> |

20 (Pages 74 to 77)

Page 78

1 Q. What are those wells? Would you identify
2 those?
3 A. One is the southeast Airstrip well, in the
4 southwest quarter section.
5 And the other, I believe, is the Airstrip
6 Number 1 well in the northwest quarter.
7 Q. And did they establish the presence of the
8 Wolfcamp formation?
9 A. Yes, they did.
10 Q. Okay.
11 A. One of those is actually on the
12 cross-section.
13 Q. Oh, it is? It's one of your cross-section
14 wells?
15 A. Yes, sir.
16 Q. Now, your Exhibit 12 is illustrating what
17 land area? Is that -- are those four townships
18 illustrated, or what are we seeing there?
19 A. What we're seeing is an area that --
20 around Section 31 it's basically two and a half
21 miles north, south, east, and west of Section 31.
22 So there are four townships represented,
23 but they're -- this is just in -- since Section 31
24 is in the corner, you're seeing four townships. Not
25 the whole township, though.

Page 79

1 Q. Okay. So can you tell the examiner the
2 extent of vertical wells penetrating the Wolfcamp in
3 that area?
4 A. In the area of the map, the Wolfcamp
5 structure data points you'll see is the light purple
6 attributes.
7 All of those wells penetrated the Wolfcamp
8 and went all the way through to the Strong.
9 There are a few other wells out here that
10 went into the top of the upper Wolfcamp, but those
11 are not depicted.
12 I use these because these are the wells
13 that I used for the iso- -- gross thickness isopach
14 map.
15 Q. So all -- all of the wells that -- I guess
16 purple, whatever it is, kind of a violet color?
17 A. Yeah. It's kind of a violet color, the
18 way it came out.
19 Q. Whatever it is.
20 All of those are vertical wells that
21 penetrated the Wolfcamp?
22 A. Yes, sir.
23 Q. Okay. And the formation is present in all
24 of those wells?
25 A. Yes, it was.

Page 80

1 Q. The -- so you have -- you do show on here
2 some -- a few third Bone Spring producers?
3 A. Yes. Those -- what I'm showing is third
4 Bone Spring horizontal producers.
5 Q. Right. And are there not several of those
6 that are lying, what I would say, just to the
7 southwest of the -- of this west half/west half of
8 Section 31?
9 A. Yes, there are.
10 Q. What are the -- they're in the -- in
11 Section 1 -- well, section -- adjoining Section 36
12 and offsetting Section 1?
13 A. Yes, they are.
14 Q. All of those are successful producers?
15 A. They were producers. I don't know if I
16 would call them successful.
17 Q. Okay. Well, I'm interested, then, if you
18 could tell the examiner about your porosity
19 contrast.
20 I think you said that your porosity was
21 much better in the wolf springs [sic] here than in
22 the Bone Springs.
23 Can you give us the values?
24 A. The Bone Spring production -- or porosity,
25 if you will, go to the cross-section. The porosity

Page 81

1 of the --
2 Q. Okay. That's Exhibit 13?
3 A. Yes, sir. Exhibit 13.
4 The third Bone Spring sand is the interval
5 between the green marker and the purple marker on
6 this cross-section.
7 And what I've highlighted here is porosity
8 greater than 8 percent. And on this cross-section,
9 porosity --
10 Q. I'm sorry. Is that -- how is that
11 highlighted? I'm trying to follow.
12 A. In the porosity curve, if you will notice
13 the label at the top, there's a red line on each one
14 of the wells.
15 Q. All right. The red vertical line?
16 A. Yes, sir.
17 Q. Okay. And it has 8 percent above it?
18 A. Yes, it has 8 percent. That is the
19 8 percent porosity cutoff for that well.
20 And then also, we have highlighted the
21 density porosity over 8 percent.
22 And when you look at the third Bone Spring
23 section there's very little of the sands that show
24 up with 8 percent porosity or greater.
25 But when we move down into the Wolfcamp,

1 we see an increase in porosity in the upper
2 Wolfcamp.

3 **Q. Are we seeing a greater than 8 percent in**
4 **the Wolfcamp?**

5 A. Yes.

6 **Q. What would you say that value is?**

7 A. That value is anywhere between 8 to 12,
8 and stringers of 14 percent porosity.

9 **Q. As opposed to the Bone Springs porosity,**
10 **which looks to you to be about what?**

11 A. It looks to me to be mostly less than 8,
12 with a few stringers of up to possibly 10 in the
13 unit area.

14 **Q. Now, the -- the Wolfcamp is a vertically**
15 **extensive formation, correct, of a thousand feet or**
16 **more?**

17 A. Yes, sir.

18 **Q. I've seen some references, I think maybe**
19 **in your materials, that your aim is the X, Y -- X**
20 **and Y portion of the Wolfcamp?**

21 A. Yes, sir. The X and Y sands are upper
22 Wolfcamp target sands, and that nomenclature is what
23 we use down south.

24 And these sands have similar
25 characteristics to the sands that we have down

1 south.

2 Whether they're actually X, Y, correlative
3 sands or not, they are -- have a similar nature.
4 And so they are basically what we're looking to
5 complete and drill as the upper Wolfcamp portion of
6 the Wolfcamp section.

7 **Q. And why do you consider that particularly**
8 **prospective?**

9 A. When we look at the Wolfcamp wells that
10 have been drilled in the area, on exhibit -- I
11 believe it's 17. Yes.

12 On Exhibit 17 all of these wells were
13 drilled in the lower part of the Wolfcamp, and they
14 are marginal producers.

15 And down south, in the upper Wolfcamp,
16 in -- we see much better production than what these
17 wells have proved to be in the lower Wolfcamp up
18 here.

19 **Q. And in fact, has Matador had considerable**
20 **success in the Wolfcamp -- not in this immediate**
21 **area, but in that portion of the -- of the**
22 **Wolfcamp --**

23 A. Yes, we have.

24 **Q. -- in other wells?**

25 A. Yes, we have.

1 **Q. Can you give us some information in that**
2 **regard?**

3 A. Most of my knowledge of that is down in
4 Texas in Loving County. We have had some X, Y sand
5 wells that have -- we have reported reserves
6 greater -- and I'm trying not to speak too much off
7 the cuff here. But I know that in excess of 500-,
8 600,000 barrels of ultimate recoveries.

9 **Q. What do you expect the recovery to be in**
10 **this Airstrip well?**

11 A. In this Airstrip well, I -- we're hoping
12 to get somewhere in the 350- to 400,000-barrel
13 range. It's -- it's hard to tell. I mean, we -- we
14 really don't know. We know what we would like to
15 have. But without having any producers or anything
16 in the area to really tighten the curve, it's hard
17 to tell what we might expect.

18 **Q. But in order for the decision to be made**
19 **by Matador to drill this well, you have done a**
20 **reserve estimate, have you not?**

21 A. Yes, sir.

22 **Q. And what did that reserve estimate show?**

23 A. Actually, it's going to be in the -- I
24 believe the 400,000-barrel range is our estimate.

25 **Q. Okay. I've seen reference somewhere to**

1 cross-leaf development in these shale wells.

2 **What does that mean?**

3 A. I'm not familiar with that term, sir.

4 **Q. You're not familiar with that?**

5 A. No, sir.

6 **Q. You have drilled, in Southeast New Mexico,**
7 **some Wolfcamp wells --**

8 A. Yes, sir.

9 **Q. -- have you not?**

10 A. Yes, sir, we have.

11 **Q. And what has been the experience with**
12 **those wells in terms of recovery?**

13 A. I'm really -- not really the person to
14 speak to that, because several of those wells were
15 drilled before I came back to Matador.

16 When I left Matador the first time we had
17 3,500 acres. When I came back we had 90,000 acres
18 in the basin. So I -- there's been a lot of
19 activity going on out there that I haven't been
20 privy to since I've been gone.

21 **Q. When did you come do back?**

22 A. February of 2015, so I've been back about
23 seven or eight months.

24 **Q. Okay.**

25 **Is it a fact that you're not targeting the**

| | |
|---|--|
| <p style="text-align: right;">Page 86</p> <p>1 Wolfcamp in order to -- to have the 160 acres so 2 that then at some later time you would go up to the 3 Bone Springs? 4 A. Please restate the question, because I 5 don't -- 6 Q. Well, the objective of the Wolfcamp is 7 really because of what you expect to be the success 8 in that formation as opposed to, say, we're going to 9 get this lower formation, and then we've held the 10 acreage to get -- to come up to the Bone Springs. 11 A. Yes. We -- we plan on and want to drill 12 the Wolfcamp. And if holding the third Bone Spring 13 through this well is a benefit, then that is 14 something that takes place. 15 But the main reason for this well is to 16 drill and produce the Wolfcamp formation. 17 Q. What is the depth at which the well is to 18 go horizontal? 19 A. We are targeting, as you can see -- we 20 should have that on -- 21 Q. Is that Exhibit 16? 22 A. Yes, sir. Exhibit 16 is the well plan 23 that has not been introduced yet. 24 Q. Okay. So it shows the deviation at 25 10,974?</p> | <p style="text-align: right;">Page 88</p> <p>1 close vertical Wolfcamp wells? 2 A. No, sir. 3 Q. You don't know whether they are available 4 or not? 5 A. I do not. 6 Q. Have you studied the porosity in those 7 wells? 8 A. In the -- yes. 9 Q. In the -- in the vertical wells that are 10 just adjacent? In fact, two of them are in this 11 Section 31? 12 A. Yes. And they -- and when you look at the 13 porosity on the cross-section, Exhibit 13, the 14 Southeast Airstrip well, which is in the section, is 15 the third well from the right -- or the left of the 16 page, that the lateral is going through. 17 Q. Oh, I see. Yes. Okay. 18 And that tells you what, in terms of 19 porosity? 20 A. It's encouraging that we have the porosity 21 there, that we should expect to encounter the same 22 porosity. 23 But we have seen wells where, in a pilot 24 hole we've had great porosity and perm. And as we 25 get out into the lateral and get way from the pilot</p> |
| <p style="text-align: right;">Page 87</p> <p>1 A. Yes, sir. 2 Q. And the lateral -- or if I'm asking some 3 questions that somebody else is going to testify to, 4 let us know. 5 A. Okay. 6 Q. Is there another witness that will talk 7 about the well plan and the -- 8 A. Yes, sir. 9 Q. Okay. All right. I won't take you 10 through that, then. 11 So in terms of your opinion, the 12 geologist, the Wolfcamp zone is present? 13 A. Yes, it is. 14 Q. And the porosity is a -- is at a favorable 15 rate, the 8 to 12 percent rate that you told us 16 about, which you believe is indicative of success? 17 A. It's at a much more favorable rate than 18 the third Bone Spring. 19 One thing, we never know with these -- 20 this perm, we can't really -- it's hard to tell the 21 perms, which is the ability of the formation to 22 flow. Because we can have higher porosity and low 23 perm, and the rock could be higher and it may not 24 flow at economic quantities. 25 Q. Do you not have some pores of this very</p> | <p style="text-align: right;">Page 89</p> <p>1 hole -- this is basically an 8-inch wellbore, and 2 this tool measures the area around that 8-inch 3 wellbore. 4 When we get away from this, we don't know 5 what we're going to find. 6 Q. Okay. 7 A. And we've seen wells that we've had 8 150-foot of section, and when we get -- by the time 9 we get to the lateral, we're down to 75. We've seen 10 thicknesses change and porosities and perms change. 11 Q. Is it not your opinion, then, that every 12 quarter section will be similar and be productive? 13 A. I believe it will be. But until we drill 14 it we're not going to know. 15 Q. Okay. But your opinion is that it is? 16 A. In my opinion, yes, it is. 17 MR. GALLEGOS: Okay. Thank you. 18 No further questions. 19 THE WITNESS: You're welcome. 20 LEAD EXAMINER GOETZE: Redirect? 21 MR. BRUCE: Just a couple, Mr. Examiner. 22 FURTHER EXAMINATION 23 BY MR. BRUCE: 24 Q. Once again, Mr. Gallegos questioned you 25 about this.</p> |

23 (Pages 86 to 89)

Page 90

1 This -- as you stated, this is an upper
2 Wolfcamp test?
3 A. Yes, it is.
4 Q. And the other ones, for instance, that are
5 shown on Exhibit 17 that you tes- -- that you
6 testified about, are lower Wolfcamp producers?
7 A. Yes, sir.
8 Q. Without being, you know, giving the
9 mileage in decimal points, is the nearest upper
10 Wolfcamp producer quite some distance away?
11 A. Yes, it is.
12 Q. We're talking tens of miles or even more?
13 A. Probably 20. 20 plus.
14 Q. Okay.
15 A. Horizontal producers.
16 Q. Horizontal producers.
17 Now you've talked a little bit about
18 estimated ultimate recoveries, et cetera.
19 At this point, because the nearest upper
20 Wolfcamp producer is so far away, it's just a guess
21 what might happen here in Section 31?
22 A. Yes. I believe it is.
23 Our engineers do a great job in trying to
24 do the best they can in planning. But until we
25 actually drill the well and try to produce it we

Page 91

1 don't know.
2 Q. But if Matador does successfully drill the
3 well, would that -- would that be proof of its
4 hypothesis of what might happen when drilling upper
5 Wolfcamp wells?
6 A. Yes, sir.
7 Q. But a hypothesis is just that. It's a
8 guess at this point?
9 A. That's right.
10 Q. Okay. And you talked about some other --
11 you know, other Eddy County wells.
12 Are there different teams at Matador for
13 different areas of New Mexico?
14 A. Yes, there are. We have, actually, three
15 teams. We have the -- in the Delaware Basin. The
16 New Mexico portion of the Delaware Basin is broken
17 into two teams, and it's a north/south delineation
18 that -- I want to say it's around the row of
19 townships that are 21.
20 And then the other team takes 21 south
21 down to Texas.
22 And then the other team has the Texas
23 wells. So we have...
24 Q. So when you're talking about other areas,
25 there's a number of other wells that aren't in your

Page 92

1 area that you're not fully knowledgeable about?
2 A. That is right. Yes.
3 Q. That's not your job. Your job is to
4 concentrate on this particular team area?
5 A. Yes, sir.
6 MR. BRUCE: Thank you.
7 LEAD EXAMINER GOETZE: Very good.
8 Mr. Wade, any questions?
9 MR. WADE: I have no questions.
10 LEAD EXAMINER GOETZE: Mr. Jones?
11 MR. JONES: Yes.
12 Mr. Juett, the -- first of all, I'm not a
13 geologist, and -- but I do remember the Wolfcamp/Abo
14 play that was going on a few years ago, and it was
15 drilling right on the base of the Abo or right on
16 the top of the Wolfcamp.
17 And where was -- where is that, compared
18 to where we're at now? Where are we now, anyway?
19 It's kind of smoky outside, I know. But...
20 THE WITNESS: I wish I had a whiteboard to
21 draw you a picture.
22 We should have probably put a locator map
23 in the exhibits to show where we are.
24 This section, if you will look at the
25 Delaware Basin, there's reef trend that goes across

Page 93

1 the top of the Delaware Basin, and then the
2 San Simon Channel breaks that reef trend. It runs
3 on the eastern side and around the north. And part
4 of the San Simon Channel breaks through, and it's
5 bringing sediment in.
6 The -- this particular area is -- if you
7 think about New Mexico and the Delaware Basin, it is
8 in the northeast corner of that, and it's a few
9 miles south of the reef trend.
10 Those Wolfcamp/Abo wells that you
11 referenced are further north. They are probably --
12 the closest one is going to be probably 10 miles to
13 the north.
14 And they are actually on the Bone Spring
15 sands, climb up out of the basin, and -- and go
16 away. And that Abo is the Bone Spring equivalent,
17 basically. And the formation below that is the
18 Wolfcamp, and that's where those were.
19 MR. JONES: Okay. Yeah. So the Abo is
20 10 miles way from here?
21 THE WITNESS: Yes, sir.
22 MR. JONES: And here it's just Bone
23 Spring.
24 And is this called an unconformity?
25 Disconformity? What is this?

24 (Pages 90 to 93)

| | |
|--|---|
| <p style="text-align: right;">Page 94</p> <p>1 THE WITNESS: I could call this an 2 unconformity between the Wolfcamp and the Bone 3 Spring. 4 MR. JONES: Is that why it's productive, 5 predicted to be productive? 6 THE WITNESS: It -- there are various 7 reasons. I mean the sands were laid down and you 8 have to have -- I mean, the Wolfcamp section has 9 more organic matter in it than the Bone Spring 10 section does. The organics are higher. 11 As the organics cook, they make more 12 porosity. And hopefully they stay around and let us 13 produce them. 14 MR. JONES: Okay. Let's see here. 15 Your porosity you're talking about, that's 16 total or is that effective? 17 THE WITNESS: That's just a total gross 18 porosity, yes, sir. 19 MR. JONES: Total? Okay. 20 And your -- this area is pretty well 21 explored vertically. 22 Is that correct? 23 THE WITNESS: Yes, it is. 24 MR. JONES: And so basically, when you 25 start talking about risk here, you're talking</p> | <p style="text-align: right;">Page 96</p> <p>1 give a casing point election, but we have to tractor 2 them down in horizontal wells because gravity won't 3 let us -- the tools flow sideways down the well. 4 So... 5 MR. JONES: Well, why do they do it in the 6 Gulf, then? They do it -- logging while drilling, 7 don't they? 8 THE WITNESS: They do it logging while 9 drilling. We will log-well drill, but we will get a 10 gamma ray curve. 11 MR. JONES: You don't want anything more 12 than that? 13 THE WITNESS: The price goes up quite a 14 bit as we start adding tools to that string. 15 MR. JONES: But you're the geologist. Do 16 you want anything else? 17 THE WITNESS: I want a lot of things, but 18 they don't give them to me. 19 MR. JONES: Okay. 20 So your geologic risk is -- what would you 21 say? That's one in two here, or is it one to one? 22 Or pretty much geologically, you know you're here, 23 right? You know these formations? 24 THE WITNESS: We know we're here, and we 25 have -- the big part of the risk in this well is the</p> |
| <p style="text-align: right;">Page 95</p> <p>1 about -- first of all, how much of the risk is done 2 by the time you get your well drilled and before you 3 frac the well? Is it -- 4 THE WITNESS: There will be quite a bit 5 of -- the drilling risk, which the next witness is 6 going to speak to, is a big part of the risk. 7 And then we also have reservoir risk that 8 comes into play as well. 9 Once we get -- if we get the well down 10 successfully, then we have reservoir risk that goes 11 into that. 12 And there's still operational risk 13 after -- and just putting the frac away, and 14 mechanical risk with that. 15 But our drilling guy will be able to speak 16 to that better than I can. 17 MR. JONES: But you're not doing a casing 18 point election or anything like that? You're... 19 THE WITNESS: No, sir. In most of these 20 shell plays, a casing point election typically was 21 done when we ran vertical wells and you could run 22 logs through them. 23 MR. JONES: Okay. 24 THE WITNESS: And if we want to greatly 25 increase the AFE, we can run logs through this and</p> | <p style="text-align: right;">Page 97</p> <p>1 reservoir risk, is, will it produce? 2 MR. JONES: Okay. 3 THE WITNESS: Does it have the fact -- the 4 components to make it produce and flow? 5 MR. JONES: Okay. What is that? Is that 6 one in five or is that one in two or what is that? 7 THE WITNESS: Well, most of the wells will 8 flow and produce. We will get some oil out of this. 9 But the risk is, is it going to be in 10 economic quantities? 11 MR. JONES: And what is the risk of 12 commerciality here? 13 THE WITNESS: Uh... 14 MR. JONES: What did you provide your 15 engineer for his economics? 16 THE WITNESS: One of the things -- I would 17 say it's probably a 30 percent chance of success, 18 but I have a hard time speaking to that. 19 MR. JONES: So one in three? 20 THE WITNESS: One in three for -- 21 averaging everything. 22 MR. JONES: But would you call this a 23 wildcat or a development well? 24 THE WITNESS: I would call this a wildcat 25 for this formation, because it has not been drilled</p> |

25 (Pages 94 to 97)

Page 98

1 horizontally yet.

2 MR. JONES: Do you think your engineer

3 could book those reserves as wildcat reserves if you

4 found it, or since you've got -- already got

5 vertical wells already drilled through here -- I

6 guess that's a question for the engineer.

7 THE WITNESS: Yes, sir.

8 LEAD EXAMINER GOETZE: Are you done?

9 MR. JONES: I'm done.

10 LEAD EXAMINER GOETZE: Okay.

11 And give me equal time. I'm not an

12 engineer.

13 So other than your geology from wells in

14 the area, were there any other sources of

15 information? Was there seismic used or proprietary

16 information used?

17 THE WITNESS: For this location, no, sir.

18 LEAD EXAMINER GOETZE: Okay. And your

19 interpretation of logs, other than porosity and --

20 did we use any density, TOC, that's total organic

21 carbon, for evaluation?

22 THE WITNESS: We -- we can generate TOC

23 estimated values off of these logs. We don't have

24 any hard TOC facts --

25 LEAD EXAMINER GOETZE: To correlate?

Page 99

1 THE WITNESS: -- to correlate from these

2 wells right here.

3 LEAD EXAMINER GOETZE: And if you were --

4 and I'm assuming -- going to continue developing the

5 Wolfcamp if this comes out, would you not suggest

6 something other than gamma ray, in addition to what

7 you have planned already for this Wolf? It's a

8 wildcat. Why not have additional information? Are

9 you going to obtain core samples, wall samples --

10 wall cores and...

11 THE WITNESS: Sidewall cores, and -- and

12 we are not going to drill a pilot well right here.

13 LEAD EXAMINER GOETZE: Okay.

14 THE WITNESS: But that -- that greatly

15 adds to the cost of the well also.

16 But we -- we think this zone is worth a

17 test, from the log responses. And if we do drill

18 additional wells, that will have to be determined on

19 what data we think we need at the time.

20 LEAD EXAMINER GOETZE: I have no further

21 questions for this witness.

22 MR. BRUCE: I have no further questions.

23 One comment. Mr. Jones asked about that

24 Abo/Wolfcamp.

25 Since I spent three or four years of my

Page 100

1 life doing hearings every month on that, it's 15

2 south 31 east.

3 MR. JONES: Thank you.

4 LEAD EXAMINER GOETZE: We could start

5 another witness, and then we'll break for lunch.

6 Do we have another witness?

7 MR. BRUCE: One more.

8 MR. GALLEGOS: Mr. Examiner and Counsel,

9 you know, I -- sitting here, we -- obviously, we

10 didn't talk before the hearing because we -- both

11 sides numbered their Exhibits 1, et cetera. So

12 there's going to be some confusion in this record.

13 I'm trying to think -- maybe if we could

14 just say that, you know, this is Applicant's

15 Exhibit 12 or 15 or whatever, and I'll try and say

16 intervener's or something. Otherwise, we're going

17 to have witnesses talking about Exhibit 6 that's --

18 LEAD EXAMINER GOETZE: Well, to the court

19 reporter, what would you like?

20 Let's go off the record for a moment.

21 (Discussion off the record.)

22 (A recess was taken from 11:26 a.m. to

23 11:27 a.m.)

24 (Witness sworn.)

25 THE WITNESS: I'm Aaron Michael Byrd.

Page 101

1 AARON MICHAEL BYRD,

2 after having been first duly sworn under oath,

3 was questioned and testified as follows:

4 EXAMINATION

5 BY MR. BRUCE:

6 Q. Mr. Byrd, where do you reside?

7 A. Dallas, Texas.

8 Q. And who do you work for?

9 A. I am employed by MRC Energy Company, an

10 affiliate of Matador Production Company, as a senior

11 drilling engineer.

12 Q. And what are your responsibilities as a

13 drilling engineer at Matador?

14 A. I am responsible for all aspects

15 associated with drilling a well, for as many as

16 three rigs at a time.

17 In addition to all engineering

18 responsibilities, I also ensure plans and procedures

19 are carried out in the field according to our

20 regulatory requirements, and as planned from an

21 engineering standpoint.

22 Q. Have you previously testified before the

23 division?

24 A. No, I have not.

25 Q. Could you describe your educational

26 (Pages 98 to 101)

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|---|--|
| <p style="text-align: right;">Page 102</p> <p>1 background and work history for the examiner?</p> <p>2 A. I received a bachelor of science in</p> <p>3 petroleum engineering and a business foundation</p> <p>4 degree from the University of Texas in 2005. So</p> <p>5 I've been in the industry for about 10 years now.</p> <p>6 I began my career as a petroleum engineer</p> <p>7 with EnCana. I spent three years going through</p> <p>8 their training program, where I spent time in</p> <p>9 completion, production, reservoir, and drilling.</p> <p>10 I then spent three years drilling</p> <p>11 horizontal wells in the Haynesville Shale in North</p> <p>12 Louisiana.</p> <p>13 After nearly six years with EnCana, I</p> <p>14 moved to Legend Natural Gas. At Legend, I was the</p> <p>15 only member of the drilling group, and I started up</p> <p>16 a two-rig drilling program drilling horizontal in</p> <p>17 the Barnett Shale for them.</p> <p>18 I controlled all drilling operations from</p> <p>19 cradle to grave for a year and a half at Legend</p> <p>20 before leaving and coming to Matador.</p> <p>21 I joined Matador Resources in 2012, where</p> <p>22 my work centered -- concentrated on horizontal</p> <p>23 drilling in the Eagleford Shale, South Texas, as</p> <p>24 well as the Delaware Basin in West Texas and</p> <p>25 Southeast New Mexico.</p> | <p style="text-align: right;">Page 104</p> <p>1 information. It details formation tops, expected</p> <p>2 formation tops, expected mud weights and mud types</p> <p>3 for the wellbore, logs and directional data we plan</p> <p>4 to obtain, casing and cementing details for each</p> <p>5 hole section planned for this well.</p> <p>6 Q. And what is Exhibit 18?</p> <p>7 A. Exhibit 18 is our directional drilling</p> <p>8 plan. This directional plan shows the surface and</p> <p>9 bottom hole locations as well as the geometry of the</p> <p>10 wellbore. It details our directional plan for the</p> <p>11 well, and it includes holding the well vertical down</p> <p>12 to 10,224 feet measured depth and TVD, at which</p> <p>13 point we'll start the curve at a build rate of</p> <p>14 10 degrees per hundred to approximately 75 degrees</p> <p>15 in the curve.</p> <p>16 We will then pick up the lateral assembly</p> <p>17 and drill the remaining part of the curve at</p> <p>18 6 degrees per hundred in order to land the curve at</p> <p>19 11,224 measured depth, 10,810 TVD, and then continue</p> <p>20 drilling the lateral to 15,378 measured depth,</p> <p>21 10,810 TVD.</p> <p>22 Q. These -- the directional drilling plans,</p> <p>23 does Matador normally file those with the division?</p> <p>24 A. Not to my knowledge, no.</p> <p>25 Q. How many completion stages, and what</p> |
| <p style="text-align: right;">Page 103</p> <p>1 Q. Do you hold any certifications or any --</p> <p>2 belong to any professional associations?</p> <p>3 A. Yes. I'm a member of SPE, Society of</p> <p>4 Petroleum Engineers, since 2001, as well as a member</p> <p>5 of the AADE, American Association of Drilling</p> <p>6 Engineers.</p> <p>7 Q. And are you familiar with the application</p> <p>8 filed by Matador?</p> <p>9 A. Yes, I am.</p> <p>10 Q. And are you familiar with the drilling and</p> <p>11 operations proposed for the well which is the</p> <p>12 subject of this application?</p> <p>13 A. Yes.</p> <p>14 MR. BRUCE: Mr. Examiner, I tender</p> <p>15 Mr. Byrd as an expert drilling engineer.</p> <p>16 LEAD EXAMINER GOETZE: Mr. Gallegos?</p> <p>17 MR. GALLEGOS: No objection.</p> <p>18 LEAD EXAMINER GOETZE: Very well. He is</p> <p>19 so qualified.</p> <p>20 Q. (By Mr. Bruce) Mr. Byrd, could you</p> <p>21 identify Exhibit 16 for the examiner and discuss its</p> <p>22 contents?</p> <p>23 A. Yes. This wellbore schematic details how</p> <p>24 we plan to drill the well for the Airstrip State Com</p> <p>25 Number 201H. It includes surface and bottom hole</p> | <p style="text-align: right;">Page 105</p> <p>1 volumes of fluid and proppant are planned for this</p> <p>2 well?</p> <p>3 A. 15 stages, with a total of 9 million</p> <p>4 pounds of proppant and approximately 5.67 million</p> <p>5 gallons of fluid.</p> <p>6 Q. How many horizontal wells has Matador</p> <p>7 drilled in the Delaware Basin?</p> <p>8 A. Over 35.</p> <p>9 Q. And how many of those are Wolfcamp wells?</p> <p>10 A. 25.</p> <p>11 Q. And how many casing strings are you</p> <p>12 proposing for this particular well?</p> <p>13 A. Four.</p> <p>14 Q. Is it possible to drill a Wolfcamp well</p> <p>15 with only three strings of casing?</p> <p>16 A. The answer to that is yes, but you always</p> <p>17 need the lower 7-inch casing string.</p> <p>18 Q. And why is that?</p> <p>19 A. You need that because we -- Matador's</p> <p>20 experience in drilling Delaware wells has validated</p> <p>21 the need for 12.5 pounds per gallon mud weight when</p> <p>22 you're drilling horizontal.</p> <p>23 Q. Horizontal Wolfcamp?</p> <p>24 A. Yes, the horizontal Wolfcamp, the</p> <p>25 horizontal portion of a Wolfcamp well.</p> |

27 (Pages 102 to 105)

1 The upper Bone Spring formations and
2 Delaware Mountain Group sands will not withstand a
3 12.5-pound per gallon environment; and, therefore,
4 it's necessary to place those formations behind
5 casings before drilling the lateral portion of the
6 Wolfcamp well.

7 On previous wells Matador has experienced
8 the Wolfcamp formation will begin collapsing and
9 become unstable if drilled with mud weights lower
10 than 12.5 pounds per gallon.

11 Q. Okay. So you need that mud weight, first
12 of all?

13 A. Yes.

14 Q. And in order to do that, you need the
15 fourth string of casing?

16 A. Correct.

17 Q. If the Wolfcamp formation began
18 collapsing, what are the implications?

19 A. Just like we talked about. You will have
20 collapsing which can lead to a stuck pipe or bottom
21 hole assembly, as well as it can lead to sidetracks
22 and loss of the well.

23 Q. Could you go back to Exhibit 11, which is
24 the AFE?

25 LEAD EXAMINER GOETZE: And that would be

1 Wolfcamp well.

2 Those are probably five or six of the
3 larger reasons.

4 Q. And if it's a deeper well, just in the
5 abstract, would it take longer to drill, just in a
6 general basis?

7 A. Yes.

8 Q. And you say a larger frac design.

9 Have the fracs been getting larger and
10 more substantial over the last couple of years?

11 A. Yes.

12 Q. It's not just Matador using the larger
13 fracs, it's other such companies as Concho,
14 et cetera?

15 A. Correct.

16 Q. Is this AFE representative of your best
17 estimate of costs at the time it was prepared?

18 A. Yes.

19 Q. Have costs, drilling costs, declined since
20 the AFE was prepared?

21 A. Yes, they have.

22 Q. And after an order is issued, will a
23 revised and current AFE be prepared and sent to all
24 parties subject to a pooling order?

25 A. Yes.

1 Applicant's Exhibit 11?

2 MR. BRUCE: Applicant's Exhibit 11,
3 Mr. Examiner. Thank you.

4 Q. (By Mr. Bruce) Who prepared the AFE?

5 A. I did, along with my coworkers at Matador.

6 Q. There's -- you've been sitting here
7 listening to the testimony, have you not?

8 A. Yes.

9 Q. And the comments made about the cost of
10 this well.

11 Is the extra string of casing part of the
12 increased cost on the AFE over and above the prior
13 Bone Spring AFE?

14 A. Yes, it is.

15 Q. What parts of this AFE are different than
16 the original HEYCO Bone Spring AFE?

17 A. It is a deeper well. It requires a fourth
18 string of casing.

19 It's a higher stimulation cost, when you
20 compare a higher frac rating of a Wolfcamp versus a
21 Bone Spring well.

22 You have a larger frac design than the
23 original HEYCO well, a considerable larger frac
24 design.

25 The mud type and mud weight needed in the

1 Q. And after the proposed well is drilled and
2 completed, will all actual costs be made available
3 to the parties subject to the pooling order?

4 A. Yes.

5 Q. In your opinion, from an operations
6 standpoint, is a cost plus 200 percent risk charge
7 justified in this case?

8 A. Yes.

9 Q. How would you define operational risk, in
10 general terms?

11 A. I would say it's not only the possibility
12 of losing the wellbore, but also drilling completion
13 issues that you have to have extensive planning to
14 mitigate, as well as anything unforeseen while
15 drilling or completing the well that could add days
16 or costs to the well.

17 Q. Could you tell the examiner about some of
18 the surface to TD drilling risks involved in drilling
19 horizontal wells in this area of Southeast
20 New Mexico?

21 A. There are examples of shallow air and
22 shallow gas pockets; shallow water flows; caverns;
23 boulders, while trying to run casing; lost
24 circulation across the entire wellbore; red beds and
25 swelling in the surface holes; thick salt sections,

1 sometimes leading to washouts; severe deviation
2 issues; H2S hazards; saltwater disposal wells;
3 anticollision with old wellbores; chert and hard
4 limestones; faults; pilot hole sidetracking issues;
5 logging issues; build rate issues; drill string
6 wear; and geo-pressured zones.

7 **Q. One final question. I hadn't thought of**
8 **this before.**

9 **But under ideal circumstances, what is the**
10 **approximate time for drilling the well -- days, I**
11 **should say.**

12 **A. The well we're proposing?**

13 **Q. Yes.**

14 **A. It would be the drilling time plus the**
15 **completion time to get it online?**

16 **Is that the question?**

17 **Q. Yes.**

18 **A. Probably 45 days. Maybe as much as 60.**

19 **Q. Unfortunately, that doesn't always happen?**

20 **A. No.**

21 **Q. And that's an operational risk, just the**
22 **days required to drill and complete a well?**

23 **A. Correct.**

24 **Q. And were Exhibits 11, 16, and 18 prepared**
25 **by you or under your supervision?**

1 **A. Yes, they were.**

2 **Q. Applicant's Exhibits 11, 16, and 18.**

3 **MR. BRUCE: Mr. Examiner, Applicant's**
4 **Exhibit 11 was already moved into the record. So I**
5 **would request to have Applicant's Exhibits 16 and 18**
6 **entered into the record.**

7 **LEAD EXAMINER GOETZE: Mr. Gallegos?**

8 **MR. GALLEGOS: No objection.**

9 **LEAD EXAMINER GOETZE: Applicant's**
10 **Exhibits 16 and 18 are so entered into the record.**

11 **Do you pass the witness on to**

12 **Mr. Gallegos?**

13 **MR. BRUCE: Yes.**

14 **LEAD EXAMINER GOETZE: Your opportunity.**

15 **MR. GALLEGOS: Can I have a moment?**

16 **LEAD EXAMINER GOETZE: Yes, you may.**

17 **EXAMINATION**

18 **BY MR. GALLEGOS:**

19 **Q. Do I understand, Mr. Byrd, that one of**
20 **your responsibilities has to do with regulatory**
21 **filings for Matador?**

22 **A. I supply operational information to our**
23 **regulatory department for that, for their filing.**

24 **Q. Have you filed a C-101 application or**
25 **permit to drill for this Wolfcamp well?**

1 **A. Personally, I have not.**

2 **Q. Is that -- would that not be within the**
3 **scope of your responsibility?**

4 **A. No, it is not. That's our regulatory**
5 **department.**

6 **Q. Okay. Do you know whether one has been**
7 **prepared and filed?**

8 **A. I do not know that answer.**

9 **Q. Okay. So when you're showing us**
10 **Exhibit 16, Applicant's Exhibit 16, a wellbore**
11 **schematic, that's presented just on a form -- on a**
12 **Matador form, correct?**

13 **A. This is -- yes. It's an internal Matador**
14 **exhibit.**

15 **Q. So this well plan and wellbore plan has**
16 **not been -- other than in this hearing -- been part**
17 **of the filing before the division.**

18 **Is that a fact?**

19 **A. I don't know that we ever submit a**
20 **wellbore plan to the division.**

21 **Q. Okay. And your drilling plan, likewise,**
22 **that's on a Matador form, not -- not a form**
23 **submitted to the division?**

24 **A. Correct.**

25 **Q. You mentioned that there were 35 wells in**

1 **the Delaware Basin, 25 of which are Wolfcamp wells.**

2 **What were you referring to? Matador wells**
3 **or other operators' wells?**

4 **A. That's only Matador wells.**

5 **Q. All right. So that would be in the**
6 **Delaware Basin of New Mexico that you're talking --**
7 **speaking about?**

8 **A. New Mexico and Loving County, Texas, just**
9 **south of the border.**

10 **Q. You've been -- is it true that the**
11 **Wolfcamp wells in Loving County, Texas, in the**
12 **Wolfcamp, have been highly successful?**

13 **A. Yes.**

14 **Q. So the -- and how many Wolfcamp wells has**
15 **Matador done in the Permian Basin of Southeast**
16 **New Mexico?**

17 **A. We've drilled six.**

18 **Q. Okay. What are those wells? Can you give**
19 **us the well names and the area in which they're**
20 **situated?**

21 **A. Yes. Okay. So we have -- are you**
22 **familiar with the Rustler Breaks area just south of**
23 **Carlsbad, if I can call that an area?**

24 **Q. Yes. We've seen references to that.**

25 **A. We have the Rustler Breaks 12, 24, 27,**

1 Number 1H. And that's a Wolfcamp well.
 2 We have the Guitar 202H, and that's a
 3 Wolfcamp well.
 4 We have the Scott Walker 204H. That's a
 5 Wolfcamp well.
 6 We have the Tiger 224H. That's a Wolfcamp
 7 well.
 8 We have the Tiger 204H. That's a Wolfcamp
 9 well.
 10 We also have the Pickard Number 2H. And
 11 that's a Wolfcamp.
 12 All of those wells have section, township,
 13 and range in the well name. I just can't remember
 14 it off the top of my head right now. I'm surprised
 15 I remembered all the other ones.
 16 Q. Yeah. That was -- I was trying to write,
 17 but I write slower than you talk.
 18 There are eight wells?
 19 A. Six.
 20 Q. Six. Okay. And --
 21 A. The first five were in Eddy County.
 22 Q. Was there only one Rustler Breaks well?
 23 A. So let me clarify something here real
 24 quick.
 25 We have Rustler Breaks, an area, but the

1 very first well we called Rustler Breaks, the well.
 2 There's one Rustler Breaks well. There's five in
 3 the Rustler Breaks area, including that Rustler
 4 Breaks well. I apologize for the nomenclature, but
 5 that's how the company decided to do it. So...
 6 Q. Okay. So the Guitar well, for example, is
 7 in the Rustler Breaks area?
 8 A. Area, yes, sir.
 9 Q. Okay. And was the Rustler -- the well
 10 that's named the Rustler Breaks was the first well
 11 drilled there?
 12 A. For Matador, yes, it was.
 13 Q. So we would understand that that would not
 14 be a development well, correct?
 15 A. Yeah. I would not call it a development
 16 well.
 17 Q. All right. What are the results of that
 18 well?
 19 A. Well, there was challenges with that well
 20 moving into that area. Taking what we've learned in
 21 Loving County and trying to apply it up there, there
 22 were challenges drilling and completing the wells to
 23 start with.
 24 But the -- the results of the well were
 25 very favorable.

1 Q. Can you tell us what the production is,
 2 cumulative production has been, and what the
 3 estimated reserves are?
 4 A. I don't know that number.
 5 Q. But very favorable results today?
 6 A. Favorable, yes.
 7 Q. And when you drill in the Wolfcamp like
 8 that, on the New Mexico side, would you say that
 9 that's a learning process? In other words, you --
 10 the company has learned something about drilling and
 11 completing the Wolfcamp that it can take to other
 12 wells?
 13 A. Yes.
 14 Q. What are the other wells in the Rustler
 15 Breaks area?
 16 A. Besides the ones I just named?
 17 Q. The Guitar, yeah. The Guitar.
 18 A. 202.
 19 Q. Okay. Let's just take them one at a time.
 20 What have been the production results and
 21 the reserves?
 22 A. I don't know any of the reserves numbers
 23 for any of these wells, other than they are all
 24 operational based, from a reservoir standpoint. I
 25 don't know those numbers as far as -- I know what

1 they approximately came on at, but I don't know
 2 EURs, and I wouldn't feel comfortable addressing
 3 those questions.
 4 From an operational standpoint, I can tell
 5 you if we had any problems drilling them, or that I
 6 know of, completing them.
 7 Q. You -- you were the drilling engineer --
 8 A. Correct.
 9 Q. -- on each of these wells?
 10 A. Correct.
 11 Q. Okay. And each of the wells was drilled
 12 to target?
 13 A. To the plan target?
 14 Q. To the plan target.
 15 A. Yes.
 16 Q. And each of the wells was completed as
 17 planned?
 18 A. Correct.
 19 Q. There then is one well -- is it the
 20 Pickard that's not in the Rustler Breaks area?
 21 A. That is correct.
 22 Q. Can you tell us where that is, township
 23 and range, at least?
 24 A. It was the one that was five or six miles
 25 northwest of the Airstrip well that we're discussing

1 today.
 2 Q. Okay. In Lea County rather than Eddy
 3 County?
 4 A. Correct.
 5 Q. All right. Did the -- was the drilling
 6 achieved as planned?
 7 A. Yes.
 8 Q. Okay. And was the completion achieved as
 9 planned?
 10 A. Yes, it was.
 11 Q. Was there a particular rig that has been
 12 used on each of these Wolfcamp wells?
 13 A. We used a variety of our rigs on the
 14 Wolfcamp wells.
 15 Q. That was the question. It's not been the
 16 same -- it's not been the same rig on -- on the six
 17 wells, the six Wolfcamp wells?
 18 A. No.
 19 Q. I'm sorry?
 20 A. No, it hasn't been.
 21 Q. Okay. What was your cost per foot on the
 22 drilling of -- let's take -- let's take the Pickard,
 23 which is five or six miles from the Airstrip.
 24 A. Well, that well was -- I don't know the
 25 number off the top of my head. It was a -- it was a

1 lengthy well.
 2 Q. Lengthy?
 3 A. Time to drill it, operational problems.
 4 Q. So you can't tell us what the cost per
 5 foot was?
 6 A. The cost per foot, no, I don't.
 7 Q. What's the cost per foot in your AFE for
 8 the Airstrip well?
 9 A. On a drilling basis?
 10 Q. Yes.
 11 A. For the original AFE I think it was in the
 12 340 range.
 13 Q. That's calculated out to be about 345, 347
 14 a foot?
 15 A. That sounds like you know it.
 16 Q. Okay. Have you -- any of the other wells
 17 that have approached that, that cost per foot?
 18 A. Some of our wells, yes.
 19 Q. Is the -- is the rig contracted for that
 20 would be drilling the Airstrip well?
 21 A. Is it contracted? Yes.
 22 Q. Yes.
 23 And is it contracted, so whether you drill
 24 this well or not, you're going to be paying a set
 25 rate to keep the -- to keep the rig available?

1 A. If the rig is under contract, yes.
 2 Q. Okay. These are, I think, some references
 3 in your -- are these UT Patterson rigs?
 4 A. Yes.
 5 Q. When -- when were they contracted for?
 6 A. Some of them have been --
 7 MS. ARNOLD: Objection. How is this
 8 relevant?
 9 MR. GALLEGOS: I'm talking about costs and
 10 the expense.
 11 LEAD EXAMINER GOETZE: Well, can we get to
 12 some finality with this, or do we have a point where
 13 we're going towards?
 14 MR. GALLEGOS: I think we have a point --
 15 LEAD EXAMINER GOETZE: Okay. Let's --
 16 MR. GALLEGOS: -- where we're going, I
 17 hope.
 18 LEAD EXAMINER GOETZE: Let's --
 19 MR. GALLEGOS: I mean, if we're -- if
 20 we're dealing with contracts in a hundred dollar a
 21 barrel oil environment, and now we're having to bear
 22 this in this environment, I think it has to do with
 23 the reasonable well expense.
 24 A. No. Our rigs are actually on a sliding
 25 scale for the oil price.

1 Q. (By Mr. Gallegos) Okay.
 2 LEAD EXAMINER GOETZE: Please speak up for
 3 the court reporter.
 4 Q. (By Mr. Gallegos) All right. Let's --
 5 your Applicant's Exhibit 11 is the AFE.
 6 Do you have that in front of you,
 7 Mr. Byrd?
 8 A. I do.
 9 Q. Did you prepare this?
 10 A. I did.
 11 Q. And you prepared it in March of this year?
 12 A. Correct.
 13 Q. Now you are aware, are you not, that there
 14 was an AFE issued in September of 2014 for this
 15 well, except for a completion of the Bone Springs?
 16 A. Correct.
 17 Q. Okay. And the AFE on that well was in the
 18 neighborhood of \$7 million?
 19 A. 7.3.
 20 Q. Okay. And is it your testimony that the
 21 increase of about \$1.8 million is because the
 22 formation is now the Wolfcamp rather than the Bone
 23 Springs?
 24 A. I think that there are numerous reasons
 25 why it's higher.

1 If you look at the original completion
2 design, it's approximately half the amount of
3 proppant that operators, including Matador, are
4 pumping these days. It's about two-thirds the
5 amount of fluid in the frac design.

6 I also will tell you that there's a fourth
7 string of casing that is required in order to drill
8 a Wolfcamp well, and that is part of the cost as
9 well as, like I mentioned before, some of the other
10 technical reasons of drilling a Wolfcamp well
11 require the higher mud weight oil-based mud in the
12 lateral. So yes, that would...

13 **Q. Isn't the completion cost in your**
14 **Applicant's Exhibit 11 AFE significantly less than**
15 **the completion cost was in the AFE for the Bone**
16 **Springs well?**

17 **A.** That looks roughly similar to me, because
18 the Bone Spring, if you're looking at the original
19 AFE, it doesn't include what we include in our end
20 of well rig release costs.

21 If you're comparing dry hole costs on the
22 original HEYCO AFE, it's what Matador considers a
23 drilling cost, they're not apples to apples
24 comparisons. They don't include the production
25 casing in their cost, the production cement, the

1 production casing crew, and anything else.

2 So if you take that amount and put it back
3 over on drilling, I would say the completion costs
4 are almost -- are very similar.

5 **Q. Okay. I was just looking at the line on**
6 **stimulation, which was 2.5 million for the Bone**
7 **Springs well, and I think it's, what, 1.8 for your**
8 **Wolfcamp well.**

9 **A.** Okay.

10 **Q. Okay. Do you have bids from various**
11 **contractors in order to compile an AFE like this,**
12 **Mr. Byrd?**

13 **A.** We have ongoing bids from contractors,
14 yes.

15 **Q. Okay. And that's basically the process by**
16 **which you construct the AFE, right?**

17 **A.** That, and looking at previous well
18 perform- -- previous well information cost data.

19 **Q. Have you done nothing since -- since March**
20 **to re-request bids from the various service**
21 **companies?**

22 **A.** No. As I state in my testimony, costs
23 have come down.

24 **Q. Okay. And as you state in your testimony,**
25 **your rig cost actually is indexed some way with oil**

1 prices?

2 **A.** Correct.

3 **Q. So that would mean from March to now, here**
4 **at the end of September, that rig cost has gone down**
5 **significantly, correct?**

6 **A.** Correct.

7 **Q. Is there any reason you did not redo the**
8 **AFE so we would have it today, so that the division**
9 **would be able to consider what the estimated cost**
10 **for this well is today, rather than in March of this**
11 **year?**

12 **A.** As an operations engineer, I work directly
13 with my land group. And I -- if they've asked me to
14 redo an AFE to submit to partners, I would do it.

15 **Q. But they have not asked you to do that?**

16 **A.** To my knowledge, no.

17 **Q. Do you have experience, Mr. Byrd, in the**
18 **Permian Basin in Southeast New Mexico with vertical**
19 **Wolfcamp wells?**

20 **A.** We've drilled one vertical, and a couple
21 of pilot holes that would have been essentially
22 vertical wells.

23 **Q. But otherwise, your experience is what has**
24 **been with hor- -- strictly with horizontal wells?**

25 **A.** Yes, sir.

1 MR. GALLEGOS: Thank you.

2 That's all the questions I have.

3 LEAD EXAMINER GOETZE: Redirect?

4 FURTHER EXAMINATION

5 BY MR. BRUCE:

6 **Q. Simply, Mr. Byrd, talking about preparing**
7 **an updated AFE for this hearing, depending on**
8 **appeals and everything else, it might be several**
9 **more months before a final order is issued.**

10 **Would the AFE change again from here to**
11 **three or four months in the future?**

12 **A.** Very likely.

13 **Q. So it's always a moving target?**

14 **A.** Correct.

15 MR. BRUCE: Thank you.

16 LEAD EXAMINER GOETZE: Mr. Wade?

17 MR. WADE: I have no questions.

18 LEAD EXAMINER GOETZE: Mr. Jones?

19 MR. JONES: Okay.

20 I'm sorry. Could you spell your last
21 name?

22 THE WITNESS: B-Y-R-D.

23 MR. JONES: Okay. Okay.

24 A three-year training program for a
25 graduating petroleum engineer?

1 THE WITNESS: Yes, sir.
 2 MR. JONES: That was -- that was nice.
 3 That means riding around -- starting to
 4 ride around with the gangs and the pumpers and
 5 production superintendents and the whole bit?
 6 THE WITNESS: Yes, sir.
 7 MR. JONES: But you're -- you're not the
 8 one that would have done the well size distributions
 9 or -- for the economics or...
 10 THE WITNESS: No, sir.
 11 MR. JONES: Someone else would have done
 12 that?
 13 And -- or book the reserves after you
 14 drill? Someone --
 15 THE WITNESS: Correct. I'm not the guy.
 16 MR. JONES: You maybe have a third party
 17 do Matador's reserves or...
 18 THE WITNESS: Well, no. We do it
 19 internally and --
 20 MR. JONES: And externally?
 21 THE WITNESS: -- and a third party as
 22 well.
 23 MR. JONES: Okay. Where do you need this
 24 12 and a half pounds? Is it right at the top of the
 25 Wolfcamp or...

1 THE WITNESS: We have experience drilling
 2 a lot of these X, Y sands, both in Eddy County and
 3 Loving, and we have seen that you need that -- in
 4 any part of the Wolfcamp -- that you need a higher
 5 mud weight before -- or else your well will start
 6 collapsing on you.
 7 MR. JONES: Okay.
 8 THE WITNESS: And it will start flowing as
 9 well.
 10 MR. JONES: Okay. Wow.
 11 I guess I should ask the most critical
 12 things first.
 13 Why are you drilling north/south here and
 14 not east/west or not -- do you have any stress data
 15 from the geologist or from your own DAPPLE sonics or
 16 some sort of pore data that shows you which way to
 17 drill?
 18 THE WITNESS: We do, and I know we've had
 19 that discussion. I just know that probably Andy
 20 would be a better person to answer that question.
 21 I don't know exactly what the stress data
 22 is. I just know that we were requested to drill
 23 north/south.
 24 MR. JONES: And they requested you to
 25 drill pretty much toe up -- or toe down, toe up?

1 THE WITNESS: We think this is actually
 2 very -- pretty flat here.
 3 MR. JONES: Okay.
 4 THE WITNESS: It's 10,810 at the heel and
 5 10,810 at the toe.
 6 MR. JONES: Okay.
 7 THE WITNESS: Until we get in there and
 8 learn otherwise.
 9 MR. JONES: Okay.
 10 THE WITNESS: But per his cross-sections,
 11 it seems it would be fairly flat.
 12 MR. JONES: Okay. Do you have -- do you
 13 subscribe to drill time plots or do you have your
 14 own -- your own, like, a drilling service that
 15 provides your plots in a given area or do you have
 16 your own drill time --
 17 THE WITNESS: We do a lot of our own. And
 18 one, we do all of our own in-house for Matador.
 19 But we also do a lot of evaluation on
 20 other operators and in different areas. Being in
 21 New Mexico, as you know, everything is public, so we
 22 can pull any of that data we want and see how we
 23 compare against other operators.
 24 MR. JONES: Okay. And if you're a working
 25 interest owner with another company you can obtain

1 that area that way also?
 2 THE WITNESS: Absolutely. Yes, sir.
 3 MR. JONES: If you have time to do it, I
 4 guess?
 5 THE WITNESS: Yeah, we do.
 6 MR. JONES: Speaking of that, your info
 7 sharing -- once somebody becomes a working interest
 8 owner with you and you drill -- and you're the
 9 operator, you're going to share your data with them.
 10 Is that correct?
 11 THE WITNESS: We go out of our way to
 12 share our data. We have non -- we have other
 13 working interest partners that -- we share data with
 14 them daily. That is almost non-customary, but we
 15 want them -- their input.
 16 Some of the other operators have been here
 17 longer. We have lunches and conversations with them
 18 about things they've learned. We try to attack it
 19 as a team.
 20 MR. JONES: Okay. So is this going to
 21 flow, this well, do you think, or you'll put a
 22 pumping unit on it pretty quick?
 23 THE WITNESS: One is, I would fully expect
 24 for it to flow. Every Wolfcamp well we have drilled
 25 to date has flowed out the casing. And we don't

1 expect anything otherwise here.
 2 MR. JONES: Really?
 3 THE WITNESS: That is my opinion.
 4 MR. JONES: Are you going to frac down the
 5 casing?
 6 THE WITNESS: Right. Yes, sir.
 7 MR. JONES: You will frac down the casing?
 8 THE WITNESS: (No verbal response.)
 9 MR. JONES: So that's why you're running
 10 that last string down to surface?
 11 THE WITNESS: Yeah. We prefer not to frac
 12 down a liner top or a -- or a frac string.
 13 MR. JONES: Okay.
 14 THE WITNESS: We think this is the better
 15 route to go.
 16 MR. JONES: So you're not gathering bottom
 17 hole pressure data while you frac, or you just infer
 18 it from the -- Halliburton or...
 19 Okay. From --
 20 THE WITNESS: We'll get it on flowback and
 21 we'll get it as we frac the well, yeah. We'll have,
 22 you know, pressure gradients and pressure profiles,
 23 that stuff.
 24 MR. JONES: Okay. They're predicting
 25 what's happening. So...

1 THE WITNESS: Correct.
 2 MR. JONES: Okay. Your -- just quickly,
 3 on your logs that you're going to run -- there's no
 4 logs, I take it?
 5 THE WITNESS: We would get mud logs --
 6 MR. JONES: Mud logs.
 7 THE WITNESS: -- and the gamma ray that we
 8 discussed before.
 9 MR. JONES: Because you've got some pretty
 10 good control?
 11 THE WITNESS: Yes, sir.
 12 MR. JONES: When you frac it, can you just
 13 explain quickly the -- are you going to run chemical
 14 tracers in your frac stages to try to tell where
 15 your oil is coming from versus your water, that kind
 16 of thing?
 17 Was that part of their quote that they
 18 gave you?
 19 THE WITNESS: Not really. Sometimes on a
 20 horizontal -- sometimes we'll do that in the heel,
 21 you know, because you kind of go up into the -- up
 22 into the wellbore.
 23 I don't -- I don't know the answer to that
 24 from a frac standpoint.
 25 MR. JONES: That's okay.

1 THE WITNESS: That wasn't the plan.
 2 MR. JONES: Okay. What about some more
 3 details on the -- on the frac job? Your -- your gel
 4 and type of gel, the gel loading, is it like
 5 30-pound or --
 6 THE WITNESS: We run a 20-pound cross-link
 7 and slick -- and a slick kind of design as well.
 8 It's a combination of -- sorry. It's 30 barrels per
 9 foot of slick water and a 20-pound cross-link
 10 hybrid.
 11 MR. JONES: Okay. And what's the sand
 12 sizes you're going to use?
 13 THE WITNESS: 100 mesh and 30/50.
 14 MR. JONES: Okay. So nothing smaller than
 15 100 mesh?
 16 THE WITNESS: No, sir.
 17 MR. JONES: And this business about the
 18 different stages, how -- how does that work? How do
 19 you -- when you run your -- is this going to be a
 20 slotted line area that you run or...
 21 THE WITNESS: No. Matador came to the
 22 Delaware Basin with our Eagleford experience, and we
 23 fully believe in perf and plug, as you have seen
 24 more operators going to that these days. That --
 25 you know, we'll go in there and do our first -- I'm

1 sure you're familiar with -- we'll go in there and
 2 do our first system, pump out our guns and do our
 3 next stage, and then just plug and perf all the way
 4 back --
 5 MR. JONES: Okay.
 6 THE WITNESS: -- about a 300-foot stage
 7 length.
 8 MR. JONES: Okay. I don't have any more
 9 questions.
 10 Thank you.
 11 LEAD EXAMINER GOETZE: Very good. Just
 12 one question.
 13 The proppant, is that going to be natural
 14 sand or is that going to be a ceramic?
 15 THE WITNESS: It's a natural sand.
 16 LEAD EXAMINER GOETZE: Okay. I have no
 17 other questions for this witness.
 18 You have one more witness?
 19 MR. BRUCE: Not at this point.
 20 LEAD EXAMINER GOETZE: Okay. So this is
 21 going to be the final witness for your side of this
 22 argument.
 23 MR. BRUCE: Unless I want to recall
 24 someone for rebuttal.
 25 LEAD EXAMINER GOETZE: Okay. Very good.

1 At that point, we will take a break for --
 2 let me see -- 1:30.
 3 (A recess was taken from 12:04 p.m. to
 4 1:30 p.m.)
 5 LEAD EXAMINER GOETZE: All right. Are we
 6 all here?
 7 Then let's go back onto the record for
 8 Case Number 15363.
 9 And at this point, turn over to
 10 Mr. Gallegos for your presentation, sir.
 11 MR. GALLEGOS: Thank you, Mr. Examiner.
 12 Yes.
 13 The protestants call Harvey E. Yates,
 14 Junior.
 15 (Witness sworn.)
 16 THE WITNESS: My name is Harvey E. Yates,
 17 Junior.
 18 HARVEY E. YATES, JUNIOR,
 19 after having been first duly sworn under oath,
 20 was questioned and testified as follows:
 21 EXAMINATION
 22 BY MR. GALLEGOS:
 23 Q. Where do you live, Mr. Yates?
 24 A. Albuquerque, New Mexico.
 25 Q. What is your business address?

1 A. 1429 Central, Northeast, Albuquerque --
 2 Northwest, Albuquerque.
 3 Q. What is your connection with Jalapeno
 4 Corporation?
 5 A. I'm the president of Jalapeno Corporation.
 6 Q. And what is the business of that
 7 corporation?
 8 A. Two businesses: Primarily oil and gas
 9 business, and real estate.
 10 Q. Do you have a college education?
 11 A. I do.
 12 Q. Would you tell the examiner about that?
 13 A. I have a BA from the University of Texas,
 14 though having concentrated primarily on geology.
 15 I went to law school at Cornell
 16 University.
 17 Q. And did you graduate?
 18 A. That, I did, yeah.
 19 Q. And you have a degree, a JD degree?
 20 A. Yes, sir.
 21 Q. What year was that achieved?
 22 A. '73.
 23 Q. Beginning with your very first exposure to
 24 the oil and gas business in New Mexico, would you
 25 tell the examiner what that experience has been?

1 A. Well, my father put all of his sons on a
 2 cable tool rig as a tool dresser at age 14. So
 3 that's, for me, 60 years ago. It's gone downhill
 4 since then.
 5 Q. The industry or you?
 6 A. Well, the industry goes up and down.
 7 I have done most jobs in the industry, in
 8 the sense that I've worked as a landman. I've done
 9 some engineering, in the sense of getting wells
 10 drilled, where I created the AFE, and was a drilling
 11 engineer.
 12 I have done a lot of geology, and I've
 13 worked in various executive positions.
 14 Q. Let's focus on Jalapeno Corporation.
 15 How long has that company been in
 16 business?
 17 A. Oh, I'm guessing. I think it's 15 to 17
 18 years.
 19 Q. Can you give the examiner a general idea
 20 of the scope of its business, you know, the
 21 properties and the locale and the...
 22 A. It is an operator, operating primarily
 23 shallow holes. We explore primarily in Chaves
 24 County, but we have drilled in a number of other
 25 places.

1 I -- it has a large nonoperating position.
 2 For instance, it has -- it almost mirrors Matador's
 3 position in the Delaware Basin, in the -- in a
 4 portion of the Delaware Basin.
 5 Q. I'm going to ask you some more about that,
 6 some specifics about that.
 7 But as president of the corporation, do
 8 you oversee others in the company who perform their
 9 work in other disciplines?
 10 A. Yes, I do.
 11 Q. Now at some time, from an acreage position
 12 or leasehold position, would -- were -- did your
 13 company have relations with the Harvey E. Yates
 14 Corporation?
 15 A. Yes, it did.
 16 Q. Could you give us the background in that?
 17 A. Harvey E. Yates Company was a company
 18 formed out of my father's assets. My brother George
 19 became president of that corporation. My brother
 20 Fred and I had earlier both spun off, taking our
 21 proportionate of share of assets and added to them.
 22 And Fred spun off Yates Energy, and I spun
 23 off as Cibola Energy, later part of Jalapeno
 24 Corporation.
 25 Q. Did that result in approximately one-third

1 divisions of the acreage positions that HEYCO had in
2 Southeast New Mexico?

3 A. I think we -- I think Jalapeno has less
4 than one-third. You're talking about what HEYCO and
5 Matador had?

6 Q. Yes. From the division, yes.

7 A. Probably less.

8 Q. And is your -- the Fred Yates company, is
9 that Yates Energy Company?

10 A. Yates Energy, yes.

11 Q. Now at some time, did the -- HEYCO's
12 properties become the properties of the applicant
13 here, Matador?

14 A. Yes. HEYCO merged into Matador. And I
15 think that agreement was struck in February --
16 January or February of 2015.

17 Q. Okay. Now, what effect has that had in
18 regard to your companies doing business that will be
19 impacted by Matador's activities?

20 A. Well, because we have a large joint lease
21 spread, we'll be dealing with Matador for an awfully
22 long time.

23 Some of that acreage is covered by
24 operating agreements, and a great deal is not.

25 Q. About roughly how many acres would be

1 involved that -- that you have a working interest in
2 and Matador has a working interest position?

3 A. I don't -- I cannot give you an exact
4 answer. It depends on whether you're including
5 rights earned. Say you take 40 acres and enter into
6 a section operating agreement that is a section, so
7 you end up with some kind of interest in that whole
8 area.

9 If you take that whole area, we're
10 probably looking at something like 90,000 acres in
11 which we would have a very small interest.

12 If you just -- if the question has to do
13 with our gross acreage position outside of those
14 operating agreements, you're probably looking at
15 30,000 acres or something.

16 Q. And is that about the same situation with
17 Fred's company, Yates Energy?

18 A. I think Fred's company probably has
19 slightly more than we do.

20 Q. Because of this overlap, I would call, of
21 leasehold interests, does the -- do the issues in
22 this particular proceeding have a much greater
23 significance than just your 3 or 4 percent working
24 interest in the proposed spacing unit?

25 A. Yes. Yes, they do. Because subsequently,

1 we're going to be dealing with Matador. And
2 consequently, both Fred and I have gone out of our
3 way to try to work with Matador. Not necessarily
4 because of this spacing unit, but because we have
5 many acres with which to work with them in the
6 future.

7 Q. Okay. Is -- what experience have you had
8 with Matador, if any, prior to this proceeding
9 involving horizontal wells?

10 A. Do you mean prior to the receipt of an AFE
11 from them?

12 Q. Yes.

13 A. Well, I'm on the board of directors of a
14 company called Spiral, which is a company that also
15 has acreage within what I will call the Matador box
16 in the Delaware Basin.

17 And in that role as director, I met with
18 Joe Foran and participated in the negotiation of a
19 joint venture agreement between Spiral and Matador.

20 Q. And did that involve the potential
21 drilling of horizontal oil wells?

22 A. Yes, it did. It was put together, in
23 large part, for that purpose.

24 Q. Before you received the proposed AFE and
25 joint operating agreement involving what we're

1 calling the Airstrip well, had you had any other
2 direct experience with Matador in horizontal wells?

3 A. No.

4 Q. Have you been qualified, Mr. Yates, to
5 give testimony as an expert oil and gas lease and
6 well operator before this division?

7 A. Yes, I have.

8 Q. Have you also been qualified and given
9 testimony as an expert oil and gas lease well
10 operator before the Oil Conservation Commission?

11 A. Yes, I have.

12 MR. GALLEGOS: Mr. Examiner, a good bit of
13 Mr. Yates' testimony will be factual, but we offer
14 that he will be giving opinion testimony on
15 operations -- drilling operations of oil and gas
16 companies that are pertinent to the issues here.

17 We offer him as qualified to give such
18 opinion testimony.

19 LEAD EXAMINER GOETZE: Mr. Bruce?

20 MR. BRUCE: Well, generally, I have no
21 objection, but I might have objections to specific
22 questions and we'll address them at that time.

23 LEAD EXAMINER GOETZE: We'll review them
24 as they go along.

25 At this point you are so qualified as an

1 expert witness in oil and gas leasing and
2 operations.

3 **Q. (By Mr. Gallegos) What do you understand**
4 **Matador is seeking by this application?**

5 A. They are attempting to essentially take
6 our property in the spacing unit, at least as to the
7 Wolfcamp.

8 And they are seeking to do that by
9 imposing on us a risk penalty that has no
10 relationship to actual risk.

11 They're seeking to create a spacing unit
12 which I do not think is authorized under the law,
13 but which in -- so long as the -- such agreements
14 are reached voluntarily, which I believe that they
15 are permissible.

16 **Q. Have you -- in your opinion, has Matador**
17 **made a good faith effort to obtain your agreement**
18 **to -- agreement of Jalapeno -- to participate in**
19 **this well?**

20 A. Well, I do think that the men who
21 testified here earlier today believe that they have
22 made a good faith effort, but that there's a problem
23 with that.

24 The -- and I'll go through each part of
25 what happened.

1 But the basic problem is that company --
2 that Matador and companies like it use the oil
3 conservation division's propensity, if not rule, to
4 give 200 percent risk penalty regardless of the
5 facts on the ground. That they use that as
6 leverage, as a bargaining tool.

7 And that these gentlemen who testified
8 today -- Mr. Sims, for instance, has every reason to
9 believe they have negotiated in good faith.

10 But once -- but he has no capacity to
11 alter the noncon- -- for instance, the nonconsent
12 provisions of an operating agreement.

13 So I want to address that, but I'll go
14 through specifically.

15 **Q. I'm going to ask --**

16 A. Okay.

17 **Q. Excuse me.**

18 I'm going to ask you about the specific
19 instances and letters that have been exchanged.

20 But I do want to ask you: In your
21 experience in the industry, are JOAs often modified
22 from the particular APL forms that are in common use
23 by reason of mutual negotiations between the
24 parties?

25 A. Yes. From time to time they are. Let me

1 give you my experience on that.

2 As we have received operating agreements
3 from other companies other than Matador, prior to
4 Matador's entry into the area, I would receive a
5 proposed operating agreement that might have
6 300 percent nonconsent.

7 And to these companies I would send a
8 letter. I often would -- if we were going to
9 participate in the well, I would sign the AFE, but
10 would tell them that we would not sign an operating
11 agreement that contained nonconsent provisions that
12 did not meet reality in -- in the horizontal
13 drilling world, in the horizontal drilling era.

14 And so from time to time I would -- one of
15 them would back off and we would enter an operating
16 agreement. Often they wouldn't, and we would drill
17 a well where we just had signed an AFE, no operating
18 agreement.

19 **Q. Has the current commonly-used form of**
20 **joint operating agreement been in use for**
21 **approximately 25 years?**

22 A. Yes. It has varied some over time. Those
23 major companies, primarily, get together and make
24 changes to the operating agreements.

25 But the one that Matador referenced

1 earlier, I think, was created in 1989, I will point
2 out, during the vertical well era.

3 **Q. Okay. And what -- what change in the**
4 **industry has come about now, as far as drilling**
5 **techniques, as opposed to what, for decades, was the**
6 **vertical well approach?**

7 A. Horizontal drilling. And the geologist
8 here today gave a very good rendition of why risk is
9 less with horizontal drilling. And it's been
10 remarkable.

11 Two things have happened: Cost of wells
12 have gone up and the risk has dropped way down.

13 **Q. Do you believe that the form JOA that**
14 **has -- I think was promulgated some 20, 25 years**
15 **ago -- accommodates the change in the industry**
16 **that's come about with the advent of horizontal**
17 **drilling and completion?**

18 A. No. No, I don't.

19 **Q. Let me -- was this -- was this well first**
20 **proposed by HEYCO rather than Matador?**

21 A. Yes, it was.

22 **Q. Let me direct your attention, Mr. Yates,**
23 **to our exhibits which will be Protestant's Exhibit**
24 **Number 2.**

25 A. I have it here.

1 Q. Okay. Would you identify what that is?
 2 A. That is a certified letter from Harvey E.
 3 Yates Company to us. And it has to do with the
 4 Airstrip 31 State Com 2H well.
 5 And it's proposing a well, and with it was
 6 an AFE.
 7 Q. Okay. And is it proposing that the well
 8 be completed in the third Bone Springs formation?
 9 A. Yes, it is.
 10 Q. Is the AFE the third page of Protestant's
 11 Exhibit 2?
 12 A. Yes.
 13 Q. What did you do when you received this
 14 letter and the AFE?
 15 A. We signed the AFE. I signed the AFE and
 16 sent it back.
 17 Q. All right. And how much is the proposed
 18 well cost?
 19 A. I think it's 7.3 million. Yeah, a total
 20 of \$7,317,000.
 21 Q. So Jalapeno was willing to participate in
 22 the well?
 23 A. Yes.
 24 Q. What happened after that?
 25 A. Nothing, for an awfully long time. And we

1 would call HEYCO to see if they intended to drill.
 2 Then a merger took place with Matador, and
 3 we received a letter dated April 28, 2015.
 4 Fred received the same letter.
 5 And -- I'm sorry. Dated earlier. I -- on
 6 March 31, I think. And...
 7 Q. Is that Exhibit 3, Protestant's Exhibit 3?
 8 A. Yes, it is.
 9 Q. Okay. Let's -- just so we've got the
 10 sequence straight.
 11 So September you get the -- you get the
 12 proposal, the AFE, you sign it, you're willing to
 13 participate in the \$7 million drilling.
 14 Nothing happens.
 15 And then you say you believe that it was
 16 about February when HEYCO merged with Matador?
 17 A. That's correct.
 18 Q. Okay. So then the next thing that has
 19 anything to do with this property was this March 24,
 20 2015, letter to you from Matador?
 21 A. Yes. Two other things happened in the
 22 in-between time.
 23 Q. Okay. Tell us about that.
 24 A. Oil prices fell markedly, and service cost
 25 prices fell markedly.

1 Q. About what was the oil price in September,
 2 when you received the first proposal for the
 3 Airstrip well?
 4 A. I would have to go back and look. I
 5 believe it was between 80 and \$90.
 6 Q. And by the time -- March 2015 -- do you
 7 recall roughly what the price was?
 8 A. I think between 45 and \$50, probably.
 9 Q. Okay. Now, what was your reaction to this
 10 letter from Matador signed by Melissa Randall?
 11 A. Well, actually, I was offended by the
 12 letter for several reasons.
 13 There's the fact that the AFE is a
 14 million-seven higher, but that might be explained if
 15 one set aside the fact that there had been
 16 significant declines in service company prices.
 17 But the reason I was offended -- and I
 18 believe the same is true for Fred -- is that the
 19 letter sent a JOA. The JOA had 100/300 percent,
 20 covered the whole section. It sent an AFE, as I
 21 said, that was a million-seven more than the earlier
 22 AFE.
 23 He gave us 15 days to make a decision.
 24 And if we decided to participate, we were to
 25 consider the letter from Melissa Randall as an

1 invoice and send our money in for the well.
 2 Q. And is it your testimony that the
 3 operating agreement was not just for the proposed
 4 well, 160 acres, but for the entire Section 31?
 5 A. That's correct.
 6 Q. Okay. And what was your opinion of
 7 whether that was appropriate or not?
 8 A. Well, I thought, first off, because of the
 9 nonconsent provisions, I'm not -- I'm not going to
 10 sign an operating agreement like that. As I said,
 11 it doesn't reflect actual risk.
 12 So I -- I thought it inappropriate, and I
 13 went back with an alternative offer.
 14 Q. Okay. Before that, I want to point out in
 15 this letter.
 16 Did -- as an alternative to participating,
 17 in the second page of Ms. Randall's letter, were
 18 there other proposals that were presented to you by
 19 Matador?
 20 A. Yes, there were.
 21 Q. Okay. What were they, and what was your
 22 reaction?
 23 A. Well, assign all of your interest to MRC
 24 Delaware for \$1,800 per net acre was one of them.
 25 And assign all of your interest in the

1 same company delivering a 75 percent net revenue
2 interest reserving an overriding royalty, which
3 would equal the difference between existing burdens
4 and 25 percent interest proportionately reduced.

5 **Q. What was your opinion of the fairness of
6 this \$1,800 per acre offer?**

7 A. Remember, I had just participated in a
8 joint venture with Matador, where Matador paid
9 \$8,000, valued the acreage at \$8,000 an acre in this
10 same general area.

11 And so now they're offering \$1,800 an
12 acre.

13 So I thought it unreasonable.

14 **Q. Okay. Did you reply to Ms. Randall, and
15 is that reply reflected in Petitioner's [sic]
16 Exhibit 4?**

17 A. Yes, it is.

18 **Q. What is the date -- what was the date of
19 that letter?**

20 A. April 28, 2015.

21 **Q. What was your purpose in writing Matador,
22 addressed to this land manager?**

23 A. I felt she was deserving of a response,
24 and -- or not equivocating about the problems.

25 And so in my letter I raise the issue of

1 the \$1.7 million additional AFE.

2 I discuss the issue of the nonconsent
3 provision, I believe.

4 **Q. Yes. I'll direct your attention to the
5 second full paragraph.**

6 **What did you have to say regarding the
7 risk issue?**

8 A. I said:

9 "While we may be willing to participate in
10 the proposed well, we are unwilling to execute a JOA
11 written as you have proposed. The nonconsent
12 provision included in your JOA suggests a much
13 greater geologic risk, a risk inherent in the
14 vertical well world, but far overestimates the
15 geologic risk inherent in the Bone Spring or
16 Wolfcamp horizontal drilling world.

17 "Because of this, any JOA we execute with
18 terms even approaching those you have suggested
19 would have to be limited to the well's spacing unit
20 and be limited to the horizon to be drilled in the
21 wells proposed lateral, in this case, the Wolfcamp."

22 **Q. What is the rationale between the risk
23 inherit in a vertical -- vertical well development
24 as opposed to the horizontal well development?**

25 A. I'm -- I'm sorry. I don't -- why am I

1 saying that?

2 **Q. Yes. Why are you saying that?**

3 A. Okay. Well, we have spent a great deal of
4 time analyzing risk in the horizontal era. And I
5 think at some point we will probably show some
6 slides as to that, but let me -- let me just analyze
7 it.

8 We analyzed the well -- all the horizontal
9 wells drilled in the four townships surrounding the
10 Airstrip, the proposed Airstrip well.

11 There were 87 wells drilled there,
12 horizontal wells.

13 Of those 87 horizontal wells, I believe
14 there was one dry hole, and that was drilled to the
15 Delaware.

16 And there was one well lost to an en- --
17 to an engineering problem. That was a well drilled
18 by Matador. It lost -- it had a casing collapse, I
19 think it was, and it was a Wolfcamp attempt. But I
20 think it -- they had a problem with the casing
21 collapse, and they went on and completed it in the
22 Bone Springs, if I remember right.

23 So out of 87 wells -- and this includes
24 some first Bone Springs wells, Delaware wells, one
25 or two Wolfcamp wells, and Bone Springs wells.

1 80 percent of those wells are capable of
2 producing 100,000 barrels or more.

3 If you analyze the risk -- the engineering
4 risk -- every AFE you receive has a contingency for
5 the sort of risk that the gentleman up here was
6 discussing earlier today.

7 As to actual loss of well, you've got 1
8 out of 87. As to actual dry holes, you've got 1 out
9 of 87.

10 Now, I -- I want to say that you're
11 looking at a guy who was once force pool king. I
12 came to this commission at one point and force
13 pooled nine locations at the same time. I was
14 engaged in a wildcat program covering four
15 townships.

16 At another date I came here, I think, for
17 seven.

18 I understand risk. And the drilling
19 program that I engaged in, I have ample evidence
20 that 200 percent was insufficient as a risk.

21 But when you get to -- when you start
22 drilling these horizontal wells and you're drilling,
23 for instance, 87 wells and you come up with a
24 circumstance where the -- you're at the risk guard,
25 that you're going to get 100,000 barrels or more,

1 you don't have a 200 percent risk.
 2 And I'll say that these four townships are
 3 not quite as good as some other townships.
 4 We've analyzed a multitude of townships
 5 where people have sent us AFEs and so forth, to try
 6 to analyze the actual risk.
 7 There's another thing.
 8 One of the issues, of course, that was
 9 addressed here today, is the geologic zone there?
 10 Now where I was drilling rank wildcat
 11 wells, there were always -- there's always a
 12 question: Is the -- is the horizon actually there?
 13 Well, this particular -- these four
 14 townships have been penetrated by more than 300
 15 wells. The Wolfcamp has been penetrated by more
 16 than 300.
 17 So how can you -- how can you say there's
 18 a geologic risk there?
 19 I am vociferous. I'll stop and you can
 20 ask questions.
 21 **Q. No. The only -- the only other question I**
 22 **had relates back to our Exhibit 4, and to ask you:**
 23 **Did you also, in that letter, raise with Matador the**
 24 **issue of the expenses?**
 25 A. Yes, I did.

1 **Q. And did you provide a counterproposal?**
 2 A. I did. I said:
 3 "As an alternative to your proposal we
 4 would offer:
 5 "One, we would agree to sell Matador a
 6 one-year term lease covering our interest in the
 7 Wolfcamp underlying the spacing unit for \$5,000 per
 8 net acre. We would reserve an overriding royalty
 9 equal to the difference between 25 percent and the
 10 existing burdens."
 11 **Q. And what happened as to -- as a response**
 12 **to your proposal or any other communications with**
 13 **Matador?**
 14 A. Well, nothing happened for a long time. A
 15 landman with Matador called and talked to my -- a
 16 land person in my office. I was not in the office
 17 at that time.
 18 I called that person back, did not get a
 19 return call.
 20 Subsequently, in meetings, I think perhaps
 21 Rudy -- it was a phone conversation. What I was
 22 told is that this was not going to work. This
 23 spacing unit concept was not going to work because
 24 they wanted me to sign an operating agreement
 25 covering the entire section.

1 **Q. Now, we have heard some testimony this**
 2 **morning about a Dallas meeting. I think the date**
 3 **was June 15, 2015.**
 4 **Did you attend that meeting?**
 5 A. No, I did not.
 6 **Q. Did you have a representative attend?**
 7 A. My son, Emmons, attended, and my brother
 8 Fred attended. And my niece, Becky, attended.
 9 **Q. Did you learn that Matador had put up on a**
 10 **whiteboard the alternatives that you working**
 11 **interest owners might have in this proposal?**
 12 A. Well, yes, I did. My son actually
 13 photographed it and brought it back to me.
 14 **Q. Okay. And what does that show? What did**
 15 **it show?**
 16 A. I'm going to pull it up. But essentially,
 17 as I remember, it shows -- two things stood out to
 18 me.
 19 One, that -- one was that one alternative
 20 deal we can make with them was to be force pooled.
 21 As I said, Matador uses forced pooling as
 22 leverage to make other things work.
 23 The other issue, the other thing that
 24 stood out to me, is no JOA is acceptable to them
 25 unless it covers the entire section.

1 **Q. Okay. Did any -- anything come out of the**
 2 **meeting in terms of possibilities, even, for a**
 3 **voluntary agreement?**
 4 A. Well, we had -- we had subsequent
 5 conversations as a result of that.
 6 But today, earlier, there was testimony
 7 that that was -- that meeting was something caused
 8 by Matador. And I suppose, in a sense, it was.
 9 But the reason the meeting took place,
 10 Fred and I conversed about it. Fred had, years
 11 earlier, played handball with Joe Foran, the
 12 president of Matador.
 13 Because we have a great mutual interest in
 14 the future, we thought it was best to see if we
 15 could not start the relationship on a bad note. And
 16 so Fred called Joe Foran and requested that a
 17 meeting take place.
 18 And Foran called back, and eventually,
 19 that meeting took place at our request.
 20 **Q. At any time in these various**
 21 **communications did Matador indicate any willingness**
 22 **to accommodate your request concerning a risk**
 23 **penalty and a JOA and confining the JOA to the**
 24 **specific property being developed?**
 25 A. No.

1 Q. Let me turn your attention to Protestant's
2 Exhibit Number 1, which is dated August 17, 2015.

3 A. (Witness complies.)

4 Q. Did you write this letter to Van Singleton
5 at Matador?

6 A. Yes, I did. Let me give you a little
7 background on this letter.

8 Van Singleton was the gentleman that I had
9 met, and I think that he probably is the boss -- is
10 Rudy's boss here.

11 But in any case, he's, I think, the chief
12 landman for Matador.

13 Because we had been able to make no
14 headway, I sought out Van Singleton at an oil and
15 gas event here in Santa Fe and told him what we were
16 interested in doing, that we wanted to -- we would
17 like to see Matador drill this well. We wanted to
18 get off on a good foot. And so we discussed the
19 various possibilities.

20 And so I laid those out to Van. The
21 crunch point always became the nonconsent provisions
22 of the...

23 And in the course of time between the
24 letter to Melissa Randall and to Van Singleton, I
25 had -- I laid out several other possible trades that

1 provisions in its proposed JOA to 100/150."

2 That is a 50 percent risk penalty.

3 "Jalapeno will nonconsent as to the
4 drilling of Airstrip Wolfcamp well, but may well
5 consent to the Bone Springs horizontal wells, or
6 even later Wolfcamp wells, within acreage covered by
7 the JOA depending, of course, on the then posted oil
8 price."

9 Second:

10 "It can trade its Section 17" -- let me --
11 let me explain that in the trade with HEYCO, Matador
12 received some interest in some acreage in Chaves
13 County, where we have a joint interest, and we
14 developed a prospect there. And before Matador ever
15 came along, we had proposed to HEYCO that they farm
16 that out to us. And that involves 320 acres in
17 Chaves County.

18 But between the time we had made the
19 proposal to HEYCO and the time of this letter, we
20 had bought the interest of other -- of another party
21 for \$250 an acre there. So a little background.

22 "It can trade its Section 17 Chaves County
23 acres..."

24 Q. This is the second proposal?

25 A. Yes.

1 would work for us.

2 Q. Now this letter was characterized by one
3 of Matador's witnesses as having a tone, I think was
4 the word, that they thought was inappropriate.

5 What was your purpose in writing this
6 August 17, 2015, letter?

7 A. I wanted to see if we could reach a deal.
8 And I wanted all of -- much of our conversation,
9 almost all of the conversation up to that point, or
10 the negotiation, had been verbal. So I wanted to
11 lay out in writing what we had offered to Matador
12 beforehand.

13 Q. And is that memorialized on page 3 of this
14 letter?

15 A. Yes, it is.

16 Q. Explain to the examiner what you were
17 willing to do to try and achieve an agreement with
18 Matador.

19 A. I agreed -- the first one was this -- now
20 this is actually the second one, because the first
21 one was laid out in the letter to Melissa Randall.
22 I've already read that.

23 Q. Right.

24 A. "It can simply" -- as to Matador -- "It
25 can simply change the terms of the nonconsent

1 "It can trade its Section 17 Chaves County
2 acreage."

3 And incidentally, Matador did not know
4 they owned this property. These landmen who were
5 talking to me didn't know. They said, We don't own
6 it.

7 I -- one of the things I did with
8 Singleton is I said, You go back and look. You got
9 this acreage. In fact, they paid nothing for it,
10 but they ended up getting it.

11 "It can trade its Section 17 Chaves County
12 acreage for our interest in the Airstrip spacing
13 unit at the earlier specified prices."

14 And that was \$250 for the Chaves County
15 acreage, 5,000 for the Lea County acreage that we're
16 talking about, Airstrip acreage.

17 And you may think the differential in
18 those prices is great, but let me tell you, the
19 capacity of Airstrip acreage to produce is much,
20 much greater.

21 "It could then place its newly-acquired
22 interest in the Airstrip unit into a JOA and drill
23 the well."

24 In other words, just acquire the acreage
25 and put it in a JOA. Didn't have to worry about my

1 concern about nonconsent provisions.
 2 Or next:
 3 "It can purchase Jalapeno's acreage within
 4 Section 31," the whole section, "on a term
 5 assignment and convey to us its acreage in the west
 6 half of Section 17, as discussed above."
 7 And as discussed above --
 8 **Q. Yeah. Explain that.**
 9 A. As discussed above is \$5,000 a net acre.
 10 What I said above is that would give
 11 Matador the capacity to drill within that whole
 12 section. They could take that acreage and put it in
 13 the JOA. My condition was, if they -- if we got
 14 back the acreage, any -- any acreage we got back as
 15 a consequence of their failure to drill, to drill
 16 and earn all the acreage under the term assignment
 17 we offered, that acreage would come back
 18 unencumbered with a 100/300 percent nonconsent
 19 agreement.
 20 **Q. Mr. Yates, were the proposals you made**
 21 **here something beyond ordinary, or unique, as**
 22 **opposed to the kind of terms that are frequently**
 23 **made in industry agreements?**
 24 A. Well, as I told Van Singleton, it looked
 25 to me like we had gone way overboard trying to reach

1 a deal.
 2 Now I want to say, I would like to see
 3 Matador drill this well. That's not the problem
 4 here. And I agree horizontal wells are the better
 5 way to do it rather than vertical wells.
 6 But this risk, the real risk, needs to be
 7 taken into consideration.
 8 **Q. And has Matador ever given the slightest**
 9 **ground on that particular --**
 10 A. No.
 11 **Q. -- issue of your negotiations?**
 12 A. No.
 13 **Q. Let -- let me ask you.**
 14 **On your first proposal, you mention then**
 15 **posted prices of oil.**
 16 **How does that bear on your**
 17 **decision-making?**
 18 A. Well, we -- in my company we generally
 19 look for the period -- calculate -- attempt to
 20 calculate the period of time it will be until we get
 21 our money back.
 22 And I'm going to show the division some
 23 slides later, here, that will evidence this, our
 24 experience.
 25 That while this division was imposing a

1 200 percent nonconsent penalty for risk, we were
 2 getting payback in less than a year on wells in the
 3 Bone Springs.
 4 Our general rule of thumb was -- and this
 5 is, in part, because of other opportunities we had
 6 in the industry in Texas, where we have participated
 7 in better wells.
 8 Our general rule of thumb was that we did
 9 not want to drill a well where we had payout in more
 10 than two years. That was it. With the higher oil
 11 prices later, that stretched. But...
 12 **Q. Okay. Let me turn now to our Exhibit 7,**
 13 **Protestant's Exhibit 7, which is a slide.**
 14 A. (Witness complies.)
 15 **Q. Did you prepare this?**
 16 A. Yes.
 17 **Q. Explain what you are conveying by this**
 18 **particular slide.**
 19 A. Well, years ago the Oil Conservation
 20 Commission decided -- had a hearing, and I think it
 21 was in 2003. And that had to do with setting an
 22 automatic 200 percent risk penalty.
 23 And at that hearing, a gentleman who --
 24 before whom we had appeared often -- said he divided
 25 risk. The legislature said to the commission, You

1 can impose up to a 200 percent risk.
 2 Well, this gentleman had divided that risk
 3 into three parts. One was geologic risk. Is the
 4 zone there? Is the horizon there?
 5 Second was operational risk. Sometimes we
 6 refer to it as engineering risk.
 7 And the third was reservoir risk.
 8 Reservoir risk deals with such things as
 9 was testified to here today. Will the reservoir
 10 produce?
 11 And he had taken that 200 percent, divided
 12 it into thirds, 66.6 percent, whatever that works
 13 out, and then he would reduce each of those based on
 14 the evidence in the case as to each of those risks.
 15 So for instance, geologic risk, if there's
 16 no question that you're going to find the zone, then
 17 that would be reduced proportionately, and on and
 18 on.
 19 **Q. Right. Was that the testimony of -- when**
 20 **you would say "he," was that the testimony of Former**
 21 **Examiner Michael Stogner?**
 22 A. Yes, it was.
 23 **Q. And so have you -- have you attempted to**
 24 **evaluate risk on the same basis that he indicated**
 25 **was an appropriate standard?**

1 A. Yes, we have.

2 Q. Okay.

3 What is Protestant's Exhibit 8?

4 A. That is a four township map. The Airstrip
5 is right in the center of those four townships.

6 And that shows every penetration we could
7 identify through the Wolfcamp in those four
8 townships.

9 And so that goes to the geologic risk.

10 Can a geologist take -- and I think there's
11 something like 300 points there.

12 Can a geologist go to management and say,
13 Wolfcamp is here.

14 Q. And what does that tell you about --

15 A. There's no geologic risk in terms of
16 finding the zone.

17 Q. Now, the -- and what is the second page of
18 Exhibit 8, Protestant's Exhibit 8?

19 A. Let me find it here.

20 This is -- this shows the wells drilled in
21 those four -- horizontal wells drilled in the --
22 those four townships.

23 I believe there are 87 of them.

24 They are color coded based -- this is
25 important to keep in mind -- based on production so

1 far, not based on expected ultimate recoveries.

2 And so when I gave you a minute ago
3 100,000 barrels out of more than 80 percent of the
4 wells, this is how we went about it.

5 We took -- we took the 20 oldest wells in
6 these four townships. We construct -- we
7 constructed a decline curve based on the average of
8 those 20 oldest wells. And so we would take, in
9 each of these cases, the actual production of a
10 well. And then when actual production stopped,
11 because it hadn't been producing long enough, we
12 would use the average decline curve from those 20
13 oldest wells in order to attempt to ascertain how
14 much the ultimate recovery of those wells would be.

15 And I would point out that the one dry
16 hole drilled is on the far bottom right-hand corner.

17 It's a Delaware well, a Delaware dry hole.

18 And there --

19 Q. This is --

20 A. Yeah.

21 Q. That's right down in there?

22 A. I believe that's the well.

23 Q. Okay.

24 A. But when we went through and used this
25 process, and we -- we used -- the question of price

1 came up today, and that's always a very interesting
2 thing, isn't it, related to -- to risk.

3 We used actual prices, and then we used
4 not our judgment as to where prices are going, but
5 the Bank of Oklahoma's price deck on where -- if
6 we -- if we put dollars in there.

7 And the reason that was important,
8 where -- even where we're talking about barrels
9 coming out rather than dollars coming out, is that
10 if the prices collapse, just absolutely collapse,
11 they shut in wells.

12 But if the prices continue at a reasonable
13 level, then you continue to produce.

14 So the price does affect the life of the
15 well, and so that's what we did.

16 And you can go through and do that
17 yourself. I think that the division ought to be
18 doing that, to let just -- if a citizen walked into
19 an agency, or the governor, or the -- a state
20 legislature or legislative body and asked, Where is
21 the depository for knowledge about the oil and gas
22 industry in the whole government, what would the
23 answer be? It would be the OCD.

24 So I would sure recommend to the OCD that
25 it be looking at actual risk, what's going on here.

1 There's been a world change. What
2 happened is that in 2003 there -- because a number
3 of larger producers came in here and asked to
4 eliminate the need to come and give testimony as to
5 actual risk, and because dealing with that testimony
6 was also cumbersome on the division, the OCC decided
7 that it was going to automatically impose a
8 200 percent risk unless a person came in here to
9 object.

10 Well, I want to show you in a minute the
11 results of that issue to some people.

12 But something tremendous happened then, in
13 2007 and 2008.

14 Cimarex, I think, came in with the first
15 forced pooling application in 2007, and then they
16 ballooned in 2008.

17 From that time forward, drilling in this
18 state turned from vertical drilling, for the most
19 part, to horizontal drilling, and risk markedly
20 changed.

21 And yet, we continue with this automatic
22 200 percent business.

23 In any case, this slide up here goes --
24 you can look at it. Just keep in mind that it's
25 production up to that date. It's not estimated

1 total recoveries.

2 **Q. You've pointed out, in the lower**
3 **right-hand corner, the Delaware dry hole well.**

4 **Where is the one operational failure well?**

5 A. You know, I --

6 **Q. I'm sorry to --**

7 A. Yeah. I think it is up in Section 34, if
8 I remember correctly, that Matador drilled a
9 Wolfcamp and had a -- that collapsed.

10 That's the only lost well we are familiar
11 with. So when they talk about engineering or
12 operational risk, keep in mind two things.

13 One is the AFE usually has something like
14 a 15 percent contingency fee for problems.

15 But in terms of lost well, one out of 87?
16 In terms of just absolutely losing, one out of 87.
17 I mean, what kind of risk are you looking at?
18 That's less than a 2 percent risk.

19 **Q. Okay. Does Protestant's Exhibit Number 9**
20 **illustrate your conclusions, from the information**
21 **concerning what the risk is, on a proposed well?**

22 A. Yes. I've already been through geologic
23 risk, where you have four sections penetrated by
24 more than 300 holes.

25 Any geologist can map evidence that the

1 Wolfcamp is there, so there's zero geologic risk.

2 Operational risk. If you have one out of
3 87 wells, you come up with about a 1.1 percent
4 chance of risk, setting aside the fact that AFEs
5 will cover smaller risk through their contingencies.

6 And then reservoir risk, we came up with
7 an 81 percent chance that you're going to get
8 100,000 barrels or more.

9 I'm not sure that the legislature ever
10 meant that there is risk in a well --

11 MR. BRUCE: I would object to this. I
12 don't know that Mr. Yates has any knowledge of what
13 the legislature meant.

14 And I would like him to point out in the
15 statute where it describes what its intent was.
16 You'd just have to look at the statute.

17 And even these risk factors that they
18 noticed in Exhibit 7, those aren't set forth
19 anywhere in the pooling statute.

20 And I would object to him speculating
21 about the intent of the New Mexico legislature over
22 the decades.

23 MR. GALLEGOS: I'll phrase a question I
24 think that would be appropriate.

25 **Q. (By Mr. Gallegos) What is -- what is your**

1 **personal view of the provision in Section 70-2-17 in**
2 **the statute which provides that up to 200 percent**
3 **risk penalty can be allowed by the division?**

4 A. My personal opinion on that is, the
5 legislature gave the Oil Conservation Commission and
6 division the authority to impose -- to inquire as to
7 the actual risk and impose that actual risk penalty
8 on it.

9 And that the division attempted, earlier,
10 to divide that risk into three parts, as I have
11 explained before, and that's what we are following
12 here.

13 **Q. How did you arrive at the 19 percent for**
14 **the reservoir factor?**

15 A. Well, as I -- as I was trying to say,
16 where we found that looking at those producing
17 wells, among the 87, that 81 percent of them would
18 produce 100,000 barrels or more, then we came up
19 with that 19 -- the reciprocal of that --

20 19 percent. And that's how we came up with that.

21 Now as I started to say, I'm not at all
22 sure that one would have had to produce
23 100,000 barrels. I mean, let's say a well produces
24 50,000 barrels. There are many -- anyway, point
25 made.

1 **Q. All right. Mr. Yates, because of your**
2 **interest in this particular issue, have you**
3 **investigated into what -- what happens to small**
4 **working interest owners, unlike Jalapeno, who are**
5 **force pooled and subjected to this automatic risk**
6 **penalty?**

7 A. Yes, I have.

8 MR. BRUCE: I object as to the relevancy
9 of that question.

10 MR. WADE: Mr. Gallegos, why is the
11 question relevant?

12 MR. GALLEGOS: The question is relevant to
13 show the propriety of having just a 200 percent risk
14 penalty without investigation into the actual risk,
15 and the effect that it has on parties, small
16 interest owners, who are unable to take any steps to
17 protect their interest.

18 And we're talking about correlative
19 rights. It bears directly on correlative rights,
20 because if people are losing their right to share in
21 production because of this practice, then that's
22 pertinent evidence. The division should be
23 considering that.

24 MR. WADE: I'm not sure that it's relevant
25 to this particular case, though.

1 So we'll sustain.

2 **Q. (By Mr. Gallegos) Mr. Yates, would, in**
3 **your opinion, a decision by the OCD allowing a**
4 **200 percent risk penalty protect the correlative**
5 **rights of Jalapeno and Yates Energy, who elect not**
6 **to participate in this \$9.1 million well proposal?**

7 A. No, for -- for this reason.

8 If -- what you're talking about is
9 300 percent, the cost of the well back plus twice
10 that, the 200 percent penalty, plus operating.

11 So you can look at these wells, and what
12 you'll see is that companies often will drill these
13 wells, get their money back within the first year,
14 sometimes the first two years, as I said, or three
15 years.

16 MR. BRUCE: Objection. He's speculating
17 again.

18 A. I have seen this over and over in these
19 wells that we've participated in.

20 **Q. (By Mr. Gallegos) Well, you're relating**
21 **your experience, Mr. Yates?**

22 A. Yes, I am.

23 LEAD EXAMINER GOETZE: Let -- let's --
24 we'll let experience -- his experience be presented,
25 and we'll go forth from there. Okay?

1 A. So what you will often find is that those
2 wells, even though they have been fabulous wells,
3 never reach that 300 percent.

4 So the question then comes, and from our
5 standpoint, what have we received from those
6 correlative rights? If a company gives you a
7 \$9 million AFE, they're going to have to receive
8 \$27 million plus operating costs back before we see
9 any benefit at all from that oil and gas that was
10 ours in the ground.

11 Now, how is that protecting correlative
12 rights?

13 **Q. (By Mr. Gallegos) Mr. Yates, did you hear**
14 **the testimony this morning that recognized that the**
15 **AFE before the division and the parties was prepared**
16 **in March of this year, it's conceded that costs have**
17 **gone down, but the AFE has not been revised to**
18 **reflect current costs?**

19 And I ask, if you had current cost
20 information, would that bear on your decision and
21 participation as a working interest owner?

22 A. Yes, it would have. If -- if they had
23 gone back and -- if two things had happened -- well,
24 three things, I guess.

25 If they had gone back and that -- if they

1 had revised their AFE, and it had come back in the
2 \$7 million range, number one, if prices -- oil
3 prices had jumped up to about \$60 a barrel, which
4 they were for a while, and if Matador did not
5 require an operating agreement that is 300 percent
6 nonconsent penalty, then we likely would have
7 gone -- would have participated.

8 **Q. In your negotiations, did -- did you take**
9 **the position that there was to be no risk penalty**
10 **whatsoever?**

11 A. No, I didn't.

12 **Q. Were you willing to -- to compromise and**
13 **meet Matador --**

14 A. Yes. We -- we have this data from these
15 four townships, and many others, showing that the
16 risk is actually something like 20 percent, just
17 like I've shown here.

18 **Q. But were you willing -- but were you**
19 **willing to accept a JOA?**

20 A. We more -- we more than doubled that, and
21 we offered to sign a JOA that had a 100/150, which
22 is equivalent to 50 percent risk penalty.

23 MR. GALLEGOS: Mr. Examiner, I -- I move
24 the admission of Protestant's Exhibits 1, 2, 3, 4,
25 7, 8, and 9, and pass the witness.

1 Oh, yeah. And I need to move the
2 admission of exhibit -- Protestant's 14, which was
3 referred to earlier.

4 MR. BRUCE: Could you identify those
5 exhibits again for me?

6 MR. GALLEGOS: Yes. 1, 2, 3, 4 -- all of
7 those are letters -- 7, 8, 9, and 14.

8 MR. BRUCE: Just a second here,
9 Mr. Examiner.

10 I would -- I don't have any objection to
11 those, except as to Exhibit 7, because I don't think
12 there is any backup that the legislature intended --
13 discussed these particular -- all of these as the
14 only risks to be covered by the forced pool
15 legislation.

16 MR. GALLEGOS: I don't -- I don't think
17 the exhibit is meant to do more than illustrate the
18 factors that Mr. Yates applied because of the
19 Stogner -- what I call the Stogner factors in the
20 Order 11.

21 LEAD EXAMINER GOETZE: Who prepared
22 Exhibit 7?

23 THE WITNESS: I did.

24 LEAD EXAMINER GOETZE: That is your
25 interpretation?

1 THE WITNESS: Yes.
 2 LEAD EXAMINER GOETZE: Okay.
 3 And then 1 through 4, 8, and 9 were
 4 prepared by you, as far as the summary of the wells?
 5 THE WITNESS: 8 was prepared under my
 6 direction.
 7 LEAD EXAMINER GOETZE: Okay.
 8 And Number 9?
 9 THE WITNESS: The same.
 10 LEAD EXAMINER GOETZE: And then 14 is just
 11 public -- the APD for the well that was previously
 12 approved at this location for the Bone Springs.
 13 We'll go ahead and admit Protestant's,
 14 Exhibits 1, 2, 3, 4. We will do 7, 8, and 9 and 14
 15 also.
 16 We also notice that the presentation and
 17 discussion given on the screen matches the exhibits
 18 that were submitted in the notebook, so any
 19 references -- it's the same material?
 20 MR. GALLEGOS: It is.
 21 LEAD EXAMINER GOETZE: Okay.
 22 At that point, let's take a break in honor
 23 of Mr. Stogner and be back here in 10 minutes,
 24 please.
 25 (A recess was taken from 2:34 p.m. to 2:46

1 p.m.)
 2 LEAD EXAMINER GOETZE: All right. Okay.
 3 We're back on the record for Case Number 15363.
 4 Mr. Bruce, I believe it is your witness.
 5 MR. BRUCE: And this witness, I'll let my
 6 cocounsel, Dana Arnold, cross.
 7 LEAD EXAMINER GOETZE: Very good.
 8 Proceed.
 9 EXAMINATION
 10 BY MS. ARNOLD:
 11 Q. I want to start with the dataset that you
 12 were talking about before, I believe Exhibits 8, 10,
 13 and possibly some of the other ones.
 14 LEAD EXAMINER GOETZE: And that would be
 15 Protestant's exhibits?
 16 MS. ARNOLD: Protestant's exhibits,
 17 exactly.
 18 Q. (By Ms. Arnold) What formation were these
 19 wells -- I believe there's 86 or 87 wells -- drilled
 20 to?
 21 A. All the horizontal wells in that -- those
 22 four townships -- are shown here that we could
 23 identify. We took those wells off of the OCD
 24 information. And so Delaware -- most of them are
 25 for Bone Springs, I believe.

1 Q. Do you know how many of them were Bone
 2 Spring wells versus Wolfcamp wells?
 3 A. Most of them, but I can't tell you
 4 exactly. Wolfcamp -- versus Wolfcamp wells?
 5 Q. Yes.
 6 A. There were, I think, only one or two
 7 Wolfcamp wells, as I said in my testimony.
 8 Q. Is that the same dataset that you used
 9 when you were calculating the risk numbers that you
 10 put forth earlier?
 11 A. Yes. We took -- we took the Delaware
 12 well -- ev- -- all the horizontal wells in those
 13 four townships.
 14 Q. So when you were calculating your risk
 15 with the numbers that you put forth earlier, you
 16 were -- you used primarily, you know, let's say,
 17 86 -- around 86 of them were Bone Spring wells not
 18 Wolfcamp wells?
 19 A. Fewer were Bone Springs. But yes, your
 20 analysis is more or less right.
 21 Our rationale for that was this. Matador
 22 is a good operator, would not be drilling a Wolfcamp
 23 well if it were going to be worse and a Bone Springs
 24 well; therefore, we thought that this analysis was
 25 justified.

1 Q. So do you think that -- in your opinion,
 2 is the risk of drilling a Wolfcamp well, then, the
 3 same as the risk of drilling a Bone Spring well?
 4 A. Well, based on the testimony that I heard
 5 today, it ought to be a better well.
 6 Q. But is the risk the same?
 7 A. You know, that's difficult to say. It
 8 probably isn't, but I can't tell you exactly what it
 9 would be.
 10 Q. So you don't --
 11 A. But -- but if you -- our point is that if
 12 you drill a horizontal well in those four townships,
 13 here are the results.
 14 Q. But in the case here, we have a horizontal
 15 Wolfcamp well, correct?
 16 A. Right.
 17 Q. So the risk that we're talking about for
 18 this specific well is the risk that would be
 19 associated with a horizontal Wolfcamp well?
 20 A. Is it what?
 21 Q. The applicable risk standard.
 22 A. It seems to me that the risk is
 23 approximately the same; that is, that you have at
 24 least an 80 percent chance of having
 25 100,000 barrels, and probably almost no chance of a

1 dry hole.

2 **Q. Let's start with the 100,000 barrels.**

3 **What -- where did you get that number and**
4 **what exactly is driving that number?**

5 A. Well, as I said, we took the actual
6 production from those 87 wells, from the oil
7 producing wells out of the 87. And as long as we
8 had the actual production, then that went on a
9 chart.

10 And then we imposed on that, after the
11 production was no longer there -- and of course you
12 have wells in a variety of lengths of time they have
13 been producing.

14 We imposed, like, a declining curve. And
15 where did we get that declining curve?

16 We took the 20 oldest wells in the four
17 townships and averaged those declining curves, and
18 then estimated from that how much those wells would
19 produce.

20 **Q. And how many of that 20-well dataset were**
21 **Wolfcamp wells versus other formations?**

22 A. Well, as I say, about a -- one or two
23 Wolfcamp wells.

24 **Q. So one or two out of the 20 of the dataset**
25 **that you used here were Wolfcamp?**

1 **Q. The well here.**

2 A. You mean this particular well right here?

3 **Q. Yes.**

4 A. What price? What price level?

5 **Q. Well, let's use the prices that you used.**

6 **I think it was -- around \$45 was one of the price**
7 **scenarios that we saw.**

8 A. Well, I would have to go -- what is the
9 AFE? At the AFE you gave us?

10 **Q. Yes.**

11 A. It would probably be more than
12 100,000 barrels. If the AFE dropped down where it
13 ought to be, 100,000 barrels would probably make it
14 economic.

15 **Q. Where -- when you say "where it ought to**
16 **be," in your opinion, where ought it to be?**

17 A. Well, that's 7 million, something like
18 that. 7.3 million.

19 **Q. So more akin to an AFE for a Bone Spring**
20 **well?**

21 A. Uh-huh.

22 **Q. Even though it's a different formation?**

23 A. It's a little bit different. I mean, it's
24 a little bit deeper.

25 **Q. Are there any other things that you think**

1 A. Oh, no. You mean the older wells?

2 **Q. Yes.**

3 A. I'm -- I could ask that question of my
4 son, but I don't know. I don't know if any of them
5 were. Maybe one was.

6 **Q. And the 100,000 barrel number, is that**
7 **what you're saying is what makes this well economic?**
8 **Or what --**

9 A. Well, I was trying to get at that
10 unartfully, based on the earlier question.

11 My point is, when they talk about risk,
12 what are they really talking about? Is it risk of
13 getting a certain number of barrels? What is it?

14 And that -- if you go through and look at
15 the various price points, 100,000 sort of jumps out
16 at you as something you have a chance to get payback
17 in at low prices and do very well, do much -- much
18 better at higher prices.

19 You choose a figure. I mean, it could be
20 80,000 barrels, but that's the reason for it.

21 **Q. So that's the number.**

22 **I guess my question is: What is the**
23 **number to you, number of barrels, that would make it**
24 **economic?**

25 A. Make what economic?

1 **make the Wolfcamp -- drilling the Wolfcamp well**
2 **different that might account for additional costs**
3 **over and above a \$7 million Bone Spring AFE?**

4 A. There are some things about the Wolfcamp
5 that perhaps cause the cost to be better.

6 But as it was pointed out earlier today,
7 the \$7.3 million HEYCO AFE had as much fracing or
8 completion cost as -- as the Wolfcamp well.

9 And that was given as one of the reasons,
10 by your engineer, one of the reasons for the higher
11 cost. And yet, I believe that the completion cost
12 of a Bone Springs well was about as much.

13 You know there were a number of things
14 about the AFE that created concerns for us.

15 The 200- -- the supervision cost. There
16 was a supervision cost of \$105,000, and your
17 supervision cost of \$234,000. I mean, things like
18 that. For how many days out there? Now, that's
19 strange.

20 So there were a number -- a number of
21 things that caused us angst there.

22 But the point you're asking is what --
23 whether 100,000 barrels is a rational breakeven cost
24 at some price level and some -- some AFE cost.

25 I don't know. It depends. You -- you

1 choose another figure. If you can tell me a figure
2 of the number of barrels there is, we'll run those
3 figures.

4 But what you'll find is that it's not
5 200 percent. It's not rational to impose a
6 200 percent nonconsent penalty.

7 **Q. Can we flip to your -- I think what the**
8 **legislature intended slide, to talk about those**
9 **points a little bit?**

10 A. What number is it?

11 **Q. I think it's Exhibit 7, Protestant's**
12 **Exhibit 7.**

13 LEAD EXAMINER GOETZE: Thank you.

14 **Q. (By Ms. Arnold) You define geologic risk**
15 **here as the risk that the targeted zone doesn't**
16 **occur at the well's location.**

17 **Are there any additional types of geologic**
18 **risk?**

19 A. Well, there are -- you can -- if you go
20 through the documents on risk in these kinds of
21 discussions, you can sometimes find that people
22 categorize all these risks as geologic risk.

23 For instance, reservoir risk is geologic
24 risk.

25 The reason we categorized it, even though

1 some gentlemen up here don't like that, categorized
2 it this way, was because of the -- the fact that
3 someone else here in the OCD had used this
4 breakdown.

5 **Q. So I guess specifically, are there**
6 **additional types of risk, besides just that the**
7 **targeted zone won't be there, that you would put**
8 **into the geologic risk category?**

9 A. Well, as I said, some people will put what
10 is called here, reservoir risk, in there.

11 Will the zone produce? Will there be
12 permeability and porosity in those zones?

13 And that is intended, here, to be covered
14 by reservoir risk.

15 **Q. So you don't consider porosity or**
16 **permeability to be geologic risks?**

17 A. As I said, if you want to -- if you want
18 to lump together reservoir and geologic risks,
19 that's fine with me. Many people do.

20 But because here at the OCD they had been
21 separated out, we separated them out.

22 You can go back and -- the documents where
23 people write about these things, and sometimes they
24 talked about geologic risk as encompassing more than
25 we do right here. There's more than the existence

1 of the zone, because they include what we call here
2 reservoir risks. But we have provided for it.

3 **Q. So the definition of risk, as it pertains**
4 **to geology, but perhaps also reservoir or other**
5 **components, are open to interpretation depending on**
6 **who you ask in the industry?**

7 A. Absolutely. We -- absolutely.

8 If you could refer me to a hard-and-fast
9 statement as to what risk is, we'll be glad to use
10 it. We -- we searched for what someone else, a
11 neutral party here in the OCD, had categorized as a
12 risk, and we used it.

13 **Q. Let's talk about the operational risks.**

14 You know you define it here, perhaps with
15 OCD influence. It's the risk that the hole will be
16 lost by equipment malfunctions or by mistakes.

17 **Are there any other kinds of operational**
18 **risks, then, specifically pertaining to horizontal**
19 **wells, that you think is applicable here?**

20 A. Of course. But my point was that those
21 risks -- there's a continued -- all the AFEs --
22 virtually all the AFEs I've seen have some sort of
23 contingency provision, and it is to cover some of
24 those risks you are talking about.

25 **Q. Does this AFE have it? Can you point it**

1 **out to us?**

2 A. I haven't looked at that in a long time.
3 But it seems to me, with all of the extra costs,
4 that it has it in there. Let's -- if you will
5 direct me to that.

6 **Q. It's Exhibit 11 for applicant, and I don't**
7 **know what one it is for you.**

8 A. There's a contingency risk on the drilling
9 of 390,000, completion of 289,000, production of
10 98,000.

11 I think -- I have trouble reading it, but
12 I think 690,000 of contingency here.

13 **Q. So --**

14 A. In the -- as to intangibles.

15 **Q. So what about -- how would you define this**
16 **contingency? What types of risks do you think fall**
17 **into this category?**

18 A. Well, if -- I mean, you -- somebody -- on
19 every well I've been on, from very simple to more a
20 complicated well, somebody screws up somewhere.
21 Someone brings the wrong equipment out there and
22 consequently creates a delay of a day or whatever.
23 I mean, that always happens. And I think those
24 kinds of things are intended to be covered by
25 contingency.

1 And often what happens is engineering
2 departments in these companies do not want
3 management to come back and say, Why did you
4 underestimate that drilling cost, and so they puff
5 up the figures to cover just the kinds of things
6 that I've talked about.

7 Sometimes it's done through extra
8 contingency costs. Other times it's done because
9 they bought -- they bought the pipe three months ago
10 at this price. Even though it's dropped down, they
11 use this price.

12 **Q. So what you mentioned there as your**
13 **examples are relatively small, you know, risks or**
14 **failures that might occur.**

15 **You're talking about a day or pipe.**

16 **What about some bigger risks? And I think**
17 **our drilling engineer talked about them earlier:**
18 **Shallow air, gas pockets, water flows, caverns, lost**
19 **circulation.**

20 **A. Those are encountered every day in the**
21 **drilling operation. And generally, they would be**
22 **covered by the AFE cost.**

23 **There is -- every time I go out and drill**
24 **a well there are problems of some kind like that,**
25 **and they're -- generally an engineering department**

1 in a company like Matador is going to not want
2 management to come in and say, Well, you know, last
3 time you drilled here there was an air pocket that
4 created a problem. Why in the hell didn't you cover
5 it this time? You know, that kind of thing.

6 **And so they build these AFEs to cover**
7 **those things.**

8 **Q. What about some, you know, doubling the**
9 **days on a rig because of encountering chert? And**
10 **would you think that would be -- fall under this**
11 **contingency or --**

12 **A. Yes, generally, because they will look at**
13 **the drilling in similar wells elsewhere and will**
14 **take that into account on the number of drilling**
15 **days they have imposed.**

16 **But the question is whether -- you're**
17 **really addressing -- is whether the risk -- the**
18 **operational risk should escalate the amount by which**
19 **you can impose a risk penalty on someone who is**
20 **being force pooled.**

21 **You have control when you come into the**
22 **commission with your AFE.**

23 **Q. Agreed. So I guess my real -- my question**
24 **here is, you would think that if we were to say**
25 **double the days on a well, that you would expect the**

1 **drilling contingency to be double, to account for**
2 **that risk that always exists when you go out**
3 **there --**

4 **A. No. What I said --**

5 **Q. -- or do you think it would be a smaller**
6 **percentage?**

7 **A. What I think is that an engineering**
8 **department will look at the last 10, 15, 20 wells**
9 **they've drilled, and -- and those having encountered**
10 **these various problems you're talking about, those**
11 **will be built into those averages, and they will be**
12 **in the AFE as a consequence.**

13 **Q. So there's no other operational risks that**
14 **are not covered by this contingency factor that an**
15 **operator might encounter?**

16 **A. Well, yeah, loss of the hole. And**
17 **that's -- we pointed out how often that happens. In**
18 **the 87 wells it happened once.**

19 **Q. So that is the only way that you define**
20 **that?**

21 **A. Well, why don't you -- if you want to**
22 **specifically ask me about other risks -- I mean,**
23 **you're suggesting that there are other risks that**
24 **aren't covered by the operating agreement or that**
25 **aren't represented in that lost hole.**

1 **Q. Pilot hole, sidetracking, logging issue,**
2 **build rate issues, drill string wear, washout,**
3 **severe deviation, H2S.**

4 **A. Common in the industry. All common in the**
5 **industry, and taken into account by the**
6 **engineering -- a good engineering department, and**
7 **I'm sure Matador has one.**

8 **Q. If a revised AFE -- let's turn back to the**
9 **AFE.**

10 **If a revised AFE were provided, would you**
11 **change your election?**

12 **A. I -- I was asked that question earlier,**
13 **and I said there are three issues.**

14 **What is the price of oil when it comes in?**
15 **And the revised AFE, what is it going to**
16 **come in at? That's an issue.**

17 **The price of oil, and do I have to sign an**
18 **operating agreement that is a 300 percent**
19 **nonconsent?**

20 **I'm not going to sign one of those.**

21 **Q. Have you ever signed one before?**

22 **A. Of course I have.**

23 **Q. In the last five years?**

24 **A. I have in these circumstances, where I've**
25 **raised the same issues, and the operator had**

1 wanted -- might have sent an operating agreement
2 covering a section or covering 320 acres or
3 whatever, and they were going to drill on a
4 proration unit. And I have agreed, in that specific
5 proration unit, to sign that operating agreement
6 because I was going to participate in the well.

7 Under those circumstances I have signed,
8 because it won't be imposed -- the terms of that
9 won't be imposed on me -- very unlikely that the
10 terms of that would be imposed on me, because I am
11 participating in that particular well.

12 **Q. So if you are not going to participate in**
13 **a well, you would never sign a JOA that would**
14 **impose, in your words, 100/300 percent?**

15 A. No, I would not.

16 **Q. But --**

17 A. But I have. Now, please understand me.
18 Let's make clear what we're talking about.

19 If we're talking about an area where we're
20 drilling vertical wells, a 200 -- or a 200 percent
21 risk penalty in that 100/300, which is built in, is
22 often not enough.

23 My point is, we need to have these
24 nonconsent provisions tailored to the real world.
25 The real world changed with horizontal drilling.

1 **Q. And that's -- it's not enough, based on**
2 **your experience being an operator of vertical wells?**

3 A. That's right. Sometimes it is. If you're
4 in the development area, then sometimes it
5 overstates it.

6 But if you are in a wildcat area, it
7 understates it. I've drilled a number of wells on a
8 wildcat basis where the chances of success are
9 5 percent, 7 percent, something like that. In that
10 case it doesn't begin to --

11 **Q. How many wells have you operated -- how**
12 **many horizontal wells have you operated in**
13 **New Mexico?**

14 A. None. None.

15 **Q. How many horizontal Wolfcamp wells?**

16 A. Probably over 100. I -- I don't know.

17 **Q. But you yourself haven't operated any**
18 **horizontal wells in New Mexico?**

19 A. No. We have participated in many, and we
20 have participated in many in Texas.

21 **Q. But you've never, yourself, borne the**
22 **risks as an operator of horizontal wells in**
23 **New Mexico?**

24 A. No. I've watched the risk. I've borne
25 the risk in the sense that, as a non-operator, I

1 bear that risk as well.

2 **Q. Let's talk about, again, the AFE.**

3 **If Matador were to provide you with an**
4 **AFE, would you expect that it would provide all of**
5 **the potential working interest owners with an**
6 **updated AFE?**

7 A. They should.

8 **Q. Even interest owners that they've already**
9 **reached a deal with?**

10 A. I think that a number of the interest
11 owners Matador has reached a deal with were put in
12 that position because their choice was forced
13 pooling, 200 percent risk penalty, or sign Matador's
14 deal. Sure, it ought to.

15 **Q. And what does that do as -- you know,**
16 **every time AFE numbers change, you think that an**
17 **operator should be required to provide an updated**
18 **AFE?**

19 A. It depends on how material they are. If
20 it's -- if it's significantly material, the answer
21 is -- is yes.

22 I understand. We're -- we operate as
23 well. You can't provide a new AFE every time you
24 turn around. But if there's a material difference,
25 we try to go back to nonparticipants and let them

1 know that.

2 **Q. So let's talk about the timing in the last**
3 **six months and everything that's occurred.**

4 **Between March and June, when the first**
5 **meeting was that we talked about earlier, was there**
6 **a material change in pricing, would you say, in that**
7 **time period? Would we have already -- would Matador**
8 **have already had to provide an updated AFE at that**
9 **point?**

10 A. Yes. My guess is that Matador's figures
11 for the March AFE came from earlier -- earlier
12 periods. I mean, that's just -- that's just
13 reasonable, and came from a period before the oil
14 prices started collapsing and before all the service
15 companies were scattered around looking for work.

16 And so in that period of time I think it
17 very likely that had Matador rerun the AFE it would
18 have dropped.

19 **Q. If an order is issued in this case, we get**
20 **to that point, Matador has testified that they'll**
21 **provide an updated AFE at that point where you**
22 **would, again, have the opportunity to participate or**
23 **not.**

24 **Why is that insufficient?**

25 A. Well, because we can make it -- if we get

1 an AFE at this point, we can go back and consider
 2 that AFE, we can look at oil prices and consider
 3 that.
 4 And of course, then, the question with
 5 Matador, the question you're posing, what would the
 6 nonconsent penalties be? What are you talking
 7 about? In that single well?
 8 Listen. I have offered to sell my acreage
 9 lock, stock, and barrel to Matador, sell it. I'll
 10 be out of it. Matador can take that spacing unit
 11 and go enter an operating agreement of its choice.
 12 They don't have to worry about me.
 13 That has been on the table for an awfully
 14 long time.
 15 But Matador won't do that because it wants
 16 me to sign an operating agreement covering the whole
 17 section, having nothing to do with that particular
 18 well.
 19 **Q. I'm sorry. I don't think that you**
 20 **answered my question, so I am going to try to**
 21 **rephrase it.**
 22 **A. All right.**
 23 **Q. Why, specifically, is receiving an updated**
 24 **AFE after an order is issued and Matador is**
 25 **approaching drilling the well, with its best**

1 estimates of the cost at that time, insufficient?
 2 **A. Well, because we -- we've got -- we'll**
 3 **have to make a decision very quickly at that point,**
 4 **to participate or not, rather than having the time**
 5 **to look at this and consider the matter.**
 6 **Q. What -- when you say "quickly," what's the**
 7 **time period that we're talking about here?**
 8 **A. I forget what the commission's orders are,**
 9 **but I think that it's probably 30 days or less.**
 10 **Q. Is 30 days atypical for a decision to make**
 11 **an election as to whether you're going to**
 12 **participate in a well?**
 13 **A. No, not if -- not if you have all the**
 14 **other information.**
 15 **But I'll tell you that -- the thing about**
 16 **having an AFE that is -- has gone -- you go back and**
 17 **you really take a look at -- you take a look at it**
 18 **is, you have time to consider that AFE, match it**
 19 **with prices, do your own internal economics to see**
 20 **if you can participate or not, which is a lot**
 21 **different than the cir- -- a lot different than this**
 22 **circumstance.**
 23 **I'm not going to participate in the well**
 24 **unless the prices are right, unless the nonconsent**
 25 **provisions -- or their equivalent from this**

1 division -- is right and the AFE is right.
 2 **Q. In all of your years of experience, when**
 3 **you sign -- or see, for that matter, operating**
 4 **agreements -- do they typically cover just the unit**
 5 **or do they cover the whole section?**
 6 **A. They vary markedly.**
 7 **Q. So most of the time what do you see?**
 8 **A. Generally, an operating agreement is put**
 9 **together covering more than one lease.**
 10 **Q. More than one lease.**
 11 **What about more than one unit?**
 12 **A. Spacing unit?**
 13 **Q. Yes.**
 14 **A. Yeah. Generally they cover more than one**
 15 **spacing unit.**
 16 **Q. And why is it objectionable to you that**
 17 **Matador requests a JOA covering more than one**
 18 **spacing unit?**
 19 **A. Because Matador wants, in that spacing**
 20 **unit, a 300 percent nonconsent penalty.**
 21 **I have already offered Matador the**
 22 **alternative. I've said I would enter a JOA covering**
 23 **the entire section if it were a 100/150 percent.**
 24 **What's Matador's objection to that?**
 25 **Q. I think I'm the one asking the questions.**

1 But...
 2 **A. Oh.**
 3 **Q. Let's talk about the 150 --**
 4 **100/150 percent. I believe it was in your letter,**
 5 **which is Protestant's Exhibit 2 -- 4?**
 6 **Both letters, whichever sections that they**
 7 **may be. Both letters that you have sent to Matador**
 8 **in the last six months, seven months.**
 9 **Your attorney and you briefly discussed**
 10 **earlier -- in depth, discussed that Matador would**
 11 **not budge on its 100/300 percent.**
 12 **Do you feel like you budged at all on your**
 13 **100/150 percent number?**
 14 **A. Well, as I showed you earlier today, the**
 15 **number ought to be 100 and 20 percent. 100 and 20**
 16 **percent. So we moved it up to 50 percent.**
 17 **If you double the risk -- if you think**
 18 **there's more risk in a Wolfcamp well, you double**
 19 **those risks, you're about at that level, at 140**
 20 **or -- 40 or 50 percent.**
 21 **Q. But at any point, did you try to negotiate**
 22 **at some middle ground between 100/150 and 100/300?**
 23 **A. Well, listen. Did -- I don't remember**
 24 **Matador being willing to discuss anything but**
 25 **100/300 percent.**

1 I had a discussion with Joe Foran about
2 that on the Spiral deal I testified to earlier.
3 But Matador hasn't, in this circumstance,
4 been willing to budge an iota.
5 If they had been willing to budge, they
6 could have sent me a letter back saying, We'll do
7 this. Or one of these guys' landmen could have
8 called me and said, Look. What do you think about
9 this?
10 That never happened. The only thing that
11 happened was the visual sheet that Joe Foran put up
12 when my son, Emmons -- I've got a copy of it --
13 force pool or the operating agreement as he
14 specified.
15 **Q. I'm glad you brought that up. You called**
16 **yourself the forced pool king earlier.**
17 **Did you ever use forced pooling to get**
18 **wells drilled or to -- as a bargaining negotiation,**
19 **as you said earlier?**
20 A. Not -- not to -- not in the sense that it
21 is used -- used today.
22 Where I -- in the circumstance where I
23 used it, I had acquired most of the leasehold
24 interest in about four townships, and -- in Chaves
25 County -- and was attempting to drill a number of

1 wildcat wells to find fields.
2 And I attempted to negotiate these. These
3 were risk -- this was a risky endeavor, much riskier
4 than this right here.
5 But you're asking me whether I went to
6 someone and said, I will just force pool you if you
7 don't agree to my terms.
8 **Q. Did Matador say that, or did they present**
9 **you with four or five different options, one of**
10 **which was forced pooling?**
11 A. Well, that -- yes, they did that. They
12 presented options. I -- but every one of them has
13 to do with my entering a JOA with 300 percent.
14 And I say -- I'm overstating the matter,
15 actually, when I say they numbered -- offered a
16 number of options.
17 Those options are the ones that were
18 discussed earlier, related to what Joe Foran did. I
19 don't know that Matador has done anything else.
20 **Q. I'm sorry. Can you -- let's just go into**
21 **that a little bit more.**
22 In your opinion, do you usually see, when
23 you're working with operators, meetings with --
24 publicly-traded large operators -- meetings with
25 around 20 of their executive staff and CEO?

1 **And secondary question --**
2 A. Well, restate that one. 20 people around
3 the table seems to be of significance to the
4 question. I don't understand that.
5 **Q. When you are negotiating or working in**
6 **good faith to reach a deal to avoid forced pooling,**
7 **is it typical in your experience to see the entire**
8 **executive staff come to you and set up a meeting?**
9 A. Well, let me give you my impression about
10 that.
11 First off, the meeting was set up as a --
12 as a consequence of my brother Fred's call to Joe
13 Foran. We did not expect 20 people.
14 I have seen the song and dance of Matador
15 before in earlier meetings with -- that I had
16 discussed earlier. The same people.
17 I think those people are brought into the
18 room to try to impress the person who is meeting
19 with them with Matador's strength and capacity,
20 meaning that we're going to force this thing down.
21 The -- what had happened -- I've got a
22 visual of what Foran offered. He walked in, raised
23 up --
24 MS. ARNOLD: I object to this a little bit
25 because, first of all, hearsay. He wasn't

1 specifically there.
2 And second of all, this visual is not
3 being introduced as an exhibit.
4 LEAD EXAMINER GOETZE: Well, let's --
5 THE WITNESS: We will next time.
6 LEAD EXAMINER GOETZE: Well, let's confine
7 ourselves to what you -- the experience.
8 But you opened the door, so if you're
9 going to ask these questions, be a little more
10 specific as to where you're going with it.
11 MS. ARNOLD: Do you object to having Jim
12 Bruce ask the second half of the questions?
13 LEAD EXAMINER GOETZE: Mr. Gallegos?
14 MR. GALLEGOS: The second half? You're
15 just halfway through?
16 MS. ARNOLD: I don't know how many
17 questions he has.
18 MR. BRUCE: I wouldn't have many.
19 MR. GALLEGOS: I suggest that Mr. Bruce
20 can write a note to his cocounsel and she can
21 complete her examination.
22 LEAD EXAMINER GOETZE: I don't really -- I
23 think it just behooves us to get this procedure
24 going again.
25 Let's allow you to finish up with the

1 final questions you have.
 2 MR. BRUCE: Okay.
 3 EXAMINATION
 4 BY MR. BRUCE:
 5 Q. Just briefly, Mr. Yates.
 6 You mentioned correlative rights.
 7 Can you define correlative rights without
 8 reading a statute or a rule?
 9 A. I'm going to read it.
 10 Q. Go ahead.
 11 A. "The opportunity afforded, so far is
 12 practical, to do -- to do so to owner of each
 13 property in a pool to produce without waste to a
 14 just and equitable share of oil or gas from a pool."
 15 Q. And if this well is drilled, wouldn't your
 16 just and equitable share of oil and gas be produced?
 17 A. No. It would be produced by Matador for
 18 Matador's interest under the terms of this deal.
 19 Q. Well, then, your problem is really with
 20 the state legislature for adopting pooling statutes,
 21 correct?
 22 A. No, it's not. It's with the Oil
 23 Conservation Commission for automatically assuming
 24 that it ought to be 200 percent rather than applying
 25 the actual risk.

1 Q. And then --
 2 A. To be clear to you, Mr. Bruce, I do not
 3 object to the driller receiving his money back for
 4 the drilling. It is the risk portion that we're
 5 talking about.
 6 Q. Okay. But when you said -- I think early
 7 on you said you objected because Matador would be
 8 taking your property.
 9 A. Exactly right. They take the difference
 10 between the actual risk and the risk and the
 11 200 percent, whatever the --
 12 Q. You would -- Jalapeno and Yates would
 13 still own their leasehold interest, wouldn't they?
 14 A. Minus extricated from Matador.
 15 Q. They wouldn't have lost their leasehold
 16 rights?
 17 A. They would have lost -- those leasehold
 18 rights are only of value because of what's in the
 19 ground.
 20 Q. Pursuant to statute?
 21 A. Well, I don't think it's --
 22 MR. GALLEGOS: Well, this has turned into
 23 just an argument.
 24 LEAD EXAMINER GOETZE: We're not getting
 25 very far, and this is something that is --

1 Q. (By Mr. Bruce) But you're talking about
 2 risk.
 3 If Matador drills an economic well, a
 4 successful well at this location, it will prove up
 5 Jalapeno and Yates' offsetting acreage, won't it?
 6 A. Yes, it will. That's one of the reasons
 7 I've said I want them to drill this well.
 8 Q. And that's of benefit to you, to Jalapeno
 9 and Yates?
 10 A. Well, it would be -- if we can
 11 participate, yes.
 12 Q. Well, if it proves up offsetting acreage,
 13 is benefiting the offset acreage?
 14 A. That's right. That's why I offered to
 15 virtually give this acreage to Matador, but I'm not
 16 going to enter a JOA of their...
 17 Q. And I think you discussed this. When you
 18 and people in your company looked at oil prices,
 19 they don't remain constant, do they?
 20 A. They certainly don't.
 21 Q. You have been in the business longer than
 22 me.
 23 A. I am not going to admit that. But...
 24 Q. I'll speculate to that, Mr. Yates.
 25 Just over the last 35 years there's been

1 constant fluctuation of prices, has there not?
 2 A. There has been fluctuation of prices.
 3 Q. And pricing is always a risk, isn't it?
 4 A. If your -- the question, pricing is always
 5 a risk, of course, in terms of a person figuring out
 6 what they are going to do.
 7 And so then come back. Is it a rational
 8 decision to drill a well at low oil prices?
 9 Of course you always get back to that.
 10 Did the legislature intend for that to be
 11 part of the calculus of risk?
 12 I think that's arguable.
 13 Q. Just one final question.
 14 But let's go back to -- after the sixth
 15 recession that I've been through in the business,
 16 let's go to 2008.
 17 Oil prices got up to \$135, and then they
 18 went down to \$35.
 19 A. 36.
 20 Q. Well, plus or minus.
 21 A. Sure.
 22 Q. You might have been -- anybody might have
 23 been -- proposed a well when the oil prices are
 24 \$135, might have taken a little while to drill the
 25 well, and all of a sudden you're looking at

| | |
|---|---|
| <p style="text-align: right;">Page 210</p> <p>1 \$35-a-barrel-oil when you're producing that well, 2 it's coming on line? 3 A. Yeah. 4 Q. That's a risk? 5 A. It sure is. 6 MR. BRUCE: Thank you, Mr. Yates. 7 LEAD EXAMINER GOETZE: Mr. Gallegos? 8 MR. GALLEGOS: I have no redirect, 9 Mr. Examiner. 10 I do suggest that since counsel asked 11 about Protestant's Exhibit 7, which had been 12 objected to and not admitted, now that it's been 13 questioned about -- 14 LEAD EXAMINER GOETZE: No, no, it was 15 admitted. 16 MR. GALLEGOS: Oh, it was admitted? 17 LEAD EXAMINER GOETZE: Yeah. We're not 18 going to waste your time. It was admitted. 19 MR. GALLEGOS: Okay. Good. I have no 20 redirect. 21 Thank you. 22 LEAD EXAMINER GOETZE: So at this point, 23 do you have any questions? 24 MR. WADE: I will have a couple of 25 questions.</p> | <p style="text-align: right;">Page 212</p> <p>1 Mr. Yates, you said Mr. Stogner actually testified. 2 And that's what you are basing, now, your 3 slide, I think ?? 4 THE WITNESS: I'm trying to get a case 5 number for you. 6 MR. WADE: Yes, that would be helpful. 7 THE WITNESS: If that's what you need. 8 MR. GALLEGOS: If I might help. The order 9 number is 11992. 10 THE WITNESS: July 2003, and it was a case 11 on charge -- it was a charge for the risk case. 12 MR. WADE: Okay. 13 THE WITNESS: And I think he gave you the 14 order number. The case number was 13069. 15 MR. WADE: Is that something that you took 16 part in or is that something you just -- 17 THE WITNESS: In 2003? No. 18 MR. WADE: Okay. That's something that 19 you have reviewed. And I believe, ultimately, your 20 Slides 7 and 9 -- 21 THE WITNESS: I have reviewed Stogner's 22 testimony in that. 23 MR. WADE: And that's -- 24 THE WITNESS: It went -- there was much 25 more than that.</p> |
| <p style="text-align: right;">Page 211</p> <p>1 LEAD EXAMINER GOETZE: Very good. 2 MR. WADE: Do you want to take a break 3 or... 4 LEAD EXAMINER GOETZE: Well, one more 5 question. 6 Do you have any other witnesses? 7 MR. GALLEGOS: No, I do not, Mr. Examiner. 8 LEAD EXAMINER GOETZE: Okay. So we're 9 going to pare it down. 10 Let's take another 10-minute break and 11 let's wander back in and have another discussion. 12 Thank you. 13 (A recess was taken from 3:25 p.m. to 3:34 14 p.m.) 15 LEAD EXAMINER GOETZE: Well, let's return 16 to the record for Case Number 15363. 17 And we have our questions from the 18 examiners. 19 We'll start off with Mr. Wade, legal 20 counsel. 21 MR. WADE: I just have a couple of 22 questions. 23 You keep referring to a -- I believe a 24 commission hearing in a -- or a commission -- 25 leading to a commission order where I think,</p> | <p style="text-align: right;">Page 213</p> <p>1 MR. WADE: Okay. But specifically, 2 Mr. Stogner's testimony is what you would have based 3 7 -- your Slides 7 and 9 on? 4 THE WITNESS: Yes. 5 MR. WADE: Okay. And going to your 6 Slide 9, I just want to clarify. 7 The risk factor that you assigned in this 8 particular case would be -- I think you testified 9 120 percent, or was it ultimately 150 percent? 10 THE WITNESS: The risk is -- well, to 11 avoid confusion, 100 percent recovery of the well 12 cost plus -- 13 MR. WADE: 20 percent? 14 THE WITNESS: -- 20 percent. 15 MR. WADE: I see. Okay. And that's what 16 Exhibit 9 would reflect? 17 THE WITNESS: Right. 18 MR. WADE: Okay. 19 But in your letters, the offer was 20 150 percent? 21 THE WITNESS: That is correct. 22 MR. WADE: Okay. 23 I have no further questions. 24 LEAD EXAMINER GOETZE: Examiner Jones, 25 please.</p> |

54 (Pages 210 to 213)

1 MR. JONES: Mr. Yates --
 2 THE WITNESS: Mr. Jones.
 3 MR. JONES: -- I guess I should say
 4 quickly, I apologize for the reaction when Michael
 5 Stogner's name was mentioned. We didn't really mean
 6 to negate any of his statements about risk. We were
 7 just talking -- kind of his personality.
 8 THE WITNESS: No. We were searching -- I
 9 think I said before -- we were searching for some
 10 basis for analyzing risk that was an objective
 11 standard.
 12 Now, there are some things about the way
 13 Mr. Stogner went about it that I thought lacked the
 14 final approach. But this was, at least, his
 15 approach. It wasn't ours. So that was the basis.
 16 MR. JONES: Okay. So the risk penalty you
 17 would ask for would be -- instead of the 100 plus
 18 200, would be 100 plus 20 percent?
 19 THE WITNESS: Correct.
 20 MR. JONES: Okay. And you've showed some
 21 evidence of that in your exhibits.
 22 Do you believe this is more of a
 23 development well? It's not a -- you don't -- you
 24 believe it's less of a wildcat and more of a
 25 development well.

1 Is that correct?
 2 THE WITNESS: Well, it's sure not a rank
 3 wildcat well, like drilling in the Tularosa Basin.
 4 It's not that.
 5 MR. JONES: Well, the Mescalero --
 6 THE WITNESS: But I -- I think that the
 7 evidence that Matador produced suggests that the
 8 well will likely be better than many of the third
 9 Bone Spring wells.
 10 And the evidence from other places where
 11 it's drilled also suggests that.
 12 But I know that it's a step-out. It's --
 13 it's a step-out.
 14 That is why we then go back to looking at
 15 all the wells, all of the horizontal wells in those
 16 four townships, and ask what the results were.
 17 I don't think you're going to get worse
 18 results in drilling the Wolfcamp than you did in the
 19 average of all of those others.
 20 MR. JONES: The -- the issue of signing a
 21 JOA that would have a higher risk, but also for the
 22 whole section where you might drill at least four
 23 wells and maybe -- maybe a lot more wells.
 24 And so is it true that you would almost
 25 never be able to go nonconsent on those wells

1 because you've already signed away your rights to do
 2 so?
 3 THE WITNESS: If you go under the
 4 horizontal deal -- I mean, we were going to put some
 5 graphs on which dis- -- I mean some decline curves
 6 -- which displayed this.
 7 They start very high, have a very steep
 8 decline curve. Generally you get payout in that
 9 period when it's steep, and then it comes out. And
 10 by the time you get out here, nothing is left.
 11 So 300 percent means, often, that you get
 12 nothing, even though the operator, the driller, has
 13 made -- for instance in this, if there were a
 14 50 percent penalty in this case, Matador would have
 15 to make 4 million bucks -- 4.5 plus million bucks.
 16 This is -- this is after all of the
 17 operating -- and on its investment.
 18 Now I mean, look around the world.
 19 Where -- where do you get those investments?
 20 MR. JONES: The JOA that you would sign,
 21 does that have a percentage of the working interests
 22 that would -- would have to sign before the operator
 23 could proceed with CAPEX cost?
 24 In other words, is it like a 5 percent --
 25 I'm sorry -- 95 percent sign-on, and the 5 percent

1 could -- could not -- if 5 percent didn't sign that
 2 they would go ahead and spend the money for, let's
 3 say, drilling or facilities or whatever you're -- in
 4 other words, your joint operating agreement, would
 5 that have -- does that require 100 percent sign-up
 6 by everybody, all --
 7 THE WITNESS: In order to drill?
 8 MR. JONES: In order to do anything out
 9 there.
 10 THE WITNESS: No. No, that's why that
 11 nonconsent provision is there.
 12 MR. JONES: Right. Okay.
 13 But what I mean is, there's no limiting
 14 percentage in it to actually...
 15 THE WITNESS: Let -- let me ask is -- see
 16 if this is -- are you saying if someone proposes a
 17 well and he owns 25 percent in an operating
 18 agreement, can he cause the drilling to go forward?
 19 Is that what you're asking?
 20 MR. JONES: Yes. But kind of the
 21 opposite, but yeah.
 22 In other words, if 5 percent --
 23 THE WITNESS: If he's willing to carry the
 24 consent interest, my understanding is yes.
 25 MR. JONES: Okay. Okay.

Page 218

1 Do you agree with the direction
2 north/south in this case for the well?
3 THE WITNESS: Uh-huh.
4 MR. JONES: It's okay?
5 THE WITNESS: I would point out that
6 Matador could have drilled this east/west under an
7 existing operating agreement.
8 MR. JONES: But --
9 THE WITNESS: An old operating agreement,
10 and we wouldn't be here.
11 MR. JONES: Okay.
12 THE WITNESS: And I trust their -- they
13 did not bring the testimony forward related to how
14 the formation is laid down and how they wanted to
15 cross it.
16 MR. JONES: But you would -- your sign is
17 to agree that north/south is a more logical way to
18 drill?
19 THE WITNESS: In this area.
20 MR. JONES: In this area.
21 What about one mile versus one and a half
22 mile or...
23 THE WITNESS: I'd like to see the
24 commission, and if necessary the legislature,
25 establish horizontal well rules that allowed that to

Page 219

1 happen.
2 It's unfortunate that we've walked up to
3 the door and haven't got that done.
4 MR. JONES: But optimally, if there was no
5 rules, just engineering and geology and economics,
6 you would drill a longer than one mile well?
7 THE WITNESS: Well, it depends on where
8 you're doing it. But yes.
9 MR. JONES: Okay. But -- okay.
10 But you're okay in this case with the one
11 mile?
12 THE WITNESS: When you say am I okay, I
13 hope you're not asking me to set aside our objection
14 to stringing together these --
15 MR. JONES: I guess that's --
16 THE WITNESS: I object to that.
17 MR. JONES: Okay.
18 THE WITNESS: Because what we're not
19 doing, in my opinion, is following the law. So...
20 MR. JONES: What about the 7,000 and the
21 700? Is that too much COPAS or not enough?
22 That \$7,000 a month while drilling and
23 \$700 a month while producing, is that an issue?
24 THE WITNESS: I think that sounds all
25 right to me.

Page 220

1 MR. JONES: That sounds all right?
2 Is this Wolfcamp -- I know they've got it
3 placed on an oil pool. But do you agree that -- do
4 your people agree that it's going to be oil? Do you
5 know the gravity and the -- that kind of stuff?
6 THE WITNESS: There was a DST in the
7 Wolfcamp in one of the wells that penetrated in this
8 section. And I believe that it flowed, and that
9 there was a lot of gas with it.
10 And I think it was maybe a little lower --
11 I'm surprised Matador didn't bring that up.
12 But I think it was maybe not right in the
13 top, where they're drilling maybe a little bit
14 lower. I would have to go back and look at that.
15 But I suspect there would be some gas, but
16 I think it was primarily oil.
17 MR. JONES: I saw some of them were open
18 hole completions in the lower Wolfcamp in those
19 surrounding wells.
20 Those -- those might be gas, and then the
21 upper part might be oil?
22 THE WITNESS: Uh-huh.
23 MR. JONES: Do you believe that Matador
24 has made a good faith effort to obtain joinder by
25 not only Yates and Jalapeno, but all of the

Page 221

1 non-consenting owners of this well?
2 THE WITNESS: No, for the reasons I stated
3 before. And I don't mean to state that the
4 gentlemen here, the land people, don't think they
5 have.
6 But I think they have a baseline, you
7 cannot change these nonconsent provisions.
8 MR. JONES: Okay. Thank you.
9 LEAD EXAMINER GOETZE: And I just have one
10 final question.
11 In your letter to MRC Delaware, you quote
12 footage prices based on two wells. That's COG's
13 CTA, and Devon's Bellatrix.
14 Where are those two wells completed? Are
15 they...
16 THE WITNESS: I think they're third Bone
17 Springs.
18 LEAD EXAMINER GOETZE: Okay.
19 I have no more questions for this witness.
20 And we do have one thing to clean up. We
21 have an Exhibit 5, 6, 10, 11, 12, and 13 included in
22 your package.
23 Are we going to visit this during the
24 hearing or are we going to take them out or...
25 MR. GALLEGOS: We have not offered those.

56 (Pages 218 to 221)

1 LEAD EXAMINER GOETZE: Okay.
 2 MR. GALLEGOS: And if it's best -- I mean
 3 as far as the reporter's exhibits, those would not
 4 be included.
 5 LEAD EXAMINER GOETZE: Would you please
 6 amend it so that what he has is what has been
 7 entered, please?
 8 MR. GALLEGOS: Yes, Mr. Examiner.
 9 LEAD EXAMINER GOETZE: At this point you
 10 have another witness.
 11 Is that correct?
 12 MR. BRUCE: I have one rebuttal witness.
 13 LEAD EXAMINER GOETZE: Yeah, I know.
 14 We're getting to rebuttal. Thank you.
 15 Rebuttal, please.
 16 MR. BRUCE: I'll be recalling Mr. Byrd to
 17 the stand. And if the record could reflect that he
 18 was sworn in and previously qualified as an expert.
 19 LEAD EXAMINER GOETZE: It is so noted.
 20 AARON MICHAEL BYRD,
 21 after having been previously duly sworn under oath,
 22 was questioned and testified further as follows:
 23 EXAMINATION
 24 BY MR. BRUCE:
 25 Q. Mr. Byrd, let me hand you -- this is

1 Applicant's Exhibit 17 Mr. Gallegos is looking at.
 2 You were sitting here during Mr. Yates'
 3 testimony, were you not, Mr. Byrd?
 4 A. Yes, I was.
 5 Q. And you heard something about -- and I
 6 forget the exact number now -- 86 or -7 -- 87 wells
 7 that he used on -- for his analysis?
 8 A. Correct.
 9 Q. Only one or two of which was Wolfcamp, if
 10 I can so summarize.
 11 A. I believe that's what he said, yes.
 12 Q. First of all, do you think it is proper to
 13 use Delaware and Bone Spring wells when you're
 14 analyzing the Wolfcamp?
 15 A. I don't, for -- when you have another
 16 casing string required, you have a different mud
 17 system, you have a geo-pressured zone that you don't
 18 see in those shallower zones.
 19 Q. Okay. Now, in looking at Exhibit 7 --
 20 Applicant's Exhibit 17, there are seven wells on
 21 there. Seven existing wells, correct?
 22 A. Yes.
 23 Q. Does Matador's proposed well -- Airstrip
 24 well -- is that proposed to test a different zone
 25 than the other Wolfcamp wells on this plat?

1 A. Yes, it is.
 2 Q. Does drilling a first well to a specific
 3 zone in an area incur risk, extra risk?
 4 A. In Matador's experience, the first well in
 5 an area has incurred more risk -- more cost than
 6 subsequent wells, yes.
 7 Q. And second, there's, I think like I said,
 8 seven wells on that plat.
 9 Have any of them experienced difficulty
 10 and risk in drilling -- during drilling operations?
 11 A. Yes. I can tell you that the COG Poptart
 12 12 Federal Number 4 was sidetracked three times,
 13 including one off the pilot hole, one in the curve,
 14 one in the lateral, and then taking the TD.
 15 Total operations on that well was 136
 16 days. I --
 17 Q. Go ahead.
 18 A. I believe that was, if not their first, it
 19 was one of their first couple wells of Wolfcamp
 20 wells.
 21 Q. Wolfcamp wells in this general area?
 22 A. Yes, sir.
 23 Q. What about any problems with time and
 24 drilling on other wells?
 25 A. Well, we all know about the Pickard

1 State -- well, at least the guys at Matador do.
 2 That was -- that well was over 100 days. It had to
 3 do with a lot of the pilot hole and other operations
 4 that were specific to that well.
 5 And that was our first well in the area as
 6 well.
 7 Q. To a deeper zone?
 8 A. Correct.
 9 Q. So what you're looking at is, rather
 10 than -- Mr. Yates was talking about 1.1 percent
 11 operational risk for these wells. All of a sudden
 12 you're up to almost one out of three of the wells is
 13 having significant operational risk?
 14 MR. GALLEGOS: I object to the leading
 15 question.
 16 Q. (By Mr. Bruce) Well, how many -- how many
 17 wells -- okay.
 18 How many wells have severe operational
 19 problems out of the seven on this plat?
 20 MR. GALLEGOS: Are we talking about just
 21 the seven on Exhibit 17?
 22 MR. BRUCE: The seven.
 23 MR. GALLEGOS: Seven or 87?
 24 MR. BRUCE: Seven.
 25 LEAD EXAMINER GOETZE: The seven on the

1 exhibit?
 2 MR. BRUCE: The seven on exhibit --
 3 Applicant's Exhibit 17.
 4 MR. GALLEGOS: Okay.
 5 Q. (By Mr. Bruce) So out of those seven, how
 6 many have had substantial operational problems?
 7 A. Two that I know of.
 8 Q. That's a little bit higher than
 9 1.1 percent, isn't it?
 10 A. Yes.
 11 Three of those had shorter laterals, as
 12 you can see, too. They are only about 1,500-foot
 13 laterals on the Wolfcamp.
 14 So I don't know what they would have
 15 experienced if they would have ran all the way to --
 16 to a 4,500-foot lateral.
 17 Q. Were -- were they originally proposed as
 18 shorter laterals or did that just happen during
 19 drilling?
 20 A. I can't answer that question. I don't
 21 know.
 22 Q. Okay. Certainly, Matador wouldn't be
 23 proposing to drill a 1,500-foot lateral?
 24 A. No.
 25 Q. One final thing, then I'll be quiet.

1 A well was mentioned, a CTA well. Are you
 2 aware of that well?
 3 A. I am.
 4 Q. Do you have any comments about that well?
 5 A. The CTA well is in the northern part of
 6 Eddy County. It is a second Bone Spring well, not a
 7 third Bone Spring well.
 8 It was to an equivalent depth of our Bone
 9 Spring wells in Eddy County, of roughly 13,000-foot
 10 measured depth, close to 75- to 80,000-foot TVD.
 11 Q. 75 to 8,000?
 12 A. 75 to 8,000 TVD. What did I say?
 13 Q. 80,000.
 14 A. Oh. Sorry about that.
 15 7,500 to 8,000-foot TVD.
 16 And when you compare what our first Bone
 17 Spring in Eddy County well was, our rig released
 18 cost for our well was within plus or minus \$5 per
 19 drilled foot of their CTA Number 6 AFE.
 20 Q. So Matador is drilling at very comparable
 21 rates?
 22 A. Absolutely.
 23 MR. BRUCE: That's all I have.
 24 I pass the witness.
 25

1 EXAMINATION
 2 BY MR. GALLEGOS:
 3 Q. Mr. Byrd, looking at Exhibit 17 -- I -- I
 4 don't take notes very rapidly.
 5 The two wells that you said were a
 6 problem, would you identify those again for me,
 7 please?
 8 A. On the far west side, the COG operating
 9 the Poptart 12 Federal.
 10 Q. Okay. Just a second. Okay. The Poptart.
 11 All right.
 12 A. As well as the Matador well on there.
 13 It's the northeast well, Pickard State Number 2H.
 14 Q. All right. Then as far as comparison of
 15 Bone Springs wells versus Wolfcamp wells, you said
 16 the -- you thought the comparison was inappropriate
 17 because of the different casing strings?
 18 A. You have a different casing string.
 19 The -- what you see on this design is, everybody has
 20 either drilled down vertically and kicked out or
 21 else they have either set a 7-inch at an angle and
 22 drilled the remaining part of the lateral. So...
 23 Q. Or sidetracking?
 24 A. That's correct.
 25 MR. GALLEGOS: Okay.

1 That's all the questions I have. Thank
 2 you.
 3 LEAD EXAMINER GOETZE: Anybody have any
 4 questions for this witness?
 5 MR. WADE: I don't have any questions.
 6 LEAD EXAMINER GOETZE: Mr. Jones?
 7 MR. JONES: No questions.
 8 LEAD EXAMINER GOETZE: We have no more
 9 questions for this witness at this time.
 10 We will offer the opportunity, unless
 11 anybody has anything else to provide in testimony, a
 12 closing statement by those folks who wish to give
 13 one.
 14 Mr. Gallegos, do you have a closing
 15 statement?
 16 MR. GALLEGOS: I don't have a closing
 17 statement. I -- what I would like to do, and I do
 18 this so we have it clear.
 19 We continue the grounds that were
 20 previously stated for our motion to dismiss
 21 regarding the lack of the division authority for
 22 entertaining these applications and granting them as
 23 nonstandard spacing units.
 24 And then we raise the legal issue we have
 25 regarding Order Number 11992, which is the order

Page 230

1 that adopted what I think is referred to often as
 2 Rule 35, the automatic 200 percent risk penalty
 3 rule.
 4 Otherwise, we -- we just -- we stand on
 5 the -- on the evidence as presented on our case,
 6 Mr. Examiner.
 7 If the division would be assisted by
 8 closing briefs we'll be happy to provide them.
 9 LEAD EXAMINER GOETZE: Mr. Bruce?
 10 MR. BRUCE: Let me defer to Ms. Arnold on
 11 that.
 12 I do like -- she may do the closing
 13 argument, but I would like the opportunity, like
 14 Mr. Gallegos, to present a proposed order, or at
 15 least proposed findings.
 16 CLOSING STATEMENT
 17 BY MS. ARNOLD:
 18 Just really briefly. You know we talked a
 19 lot here about Order R11992.
 20 Mr. Yates said that he didn't oppose it at
 21 the time. It's been in effect for several years
 22 now, and Matador operated under the rules in this
 23 case.
 24 On Number 38 -- this is a finding, or it's
 25 number -- Finding 38 of this order says that the

Page 231

1 maximum 200 percent risk charge is appropriate in
 2 the vast majority of cases being assessed by the
 3 division.
 4 And this case we have here falls into the
 5 vast majority of the case -- cases.
 6 And you know, there's no unique
 7 circumstances that were presented by the opponents
 8 here.
 9 Most of the testimony and the facts that
 10 they presented were for Bone Spring wells, and we
 11 have a Wolfcamp well at hand here. And it's not
 12 apples to apples when you look at it on any of the
 13 different risk components.
 14 Further, it seems like opponent's main
 15 issue is with the statute itself, and this is an
 16 inappropriate forum to be challenging that. If they
 17 really have a problem with it, then he should be
 18 going to the legislature.
 19 Lastly, you know, Matador has operated in
 20 good faith for several months trying to -- to reach
 21 a deal here, and feels like just because it didn't
 22 want to give on the 100 percent/300 percent does not
 23 mean that it did not go over and above what would be
 24 considered good faith negotiations, and would like
 25 to drill this well to protect correlative rights,

Page 232

1 including the rights of the State, and believes that
 2 drilling a horizontal well here will prevent waste.
 3 LEAD EXAMINER GOETZE: Thank you.
 4 MR. GALLEGOS: Mr. Examiner, may we submit
 5 a requested form of order?
 6 MR. WADE: I would defer to the hearing
 7 examiners. It seems to me the practice here is to
 8 not take into account proposed findings of fact.
 9 LEAD EXAMINER GOETZE: We -- we tend to
 10 write our own. And in this case, I think we
 11 probably will be ending up writing our own. This is
 12 going to be something different.
 13 So you will have to suffer with our poor
 14 penmanship and wordings, and we will make our own
 15 order.
 16 We do thank you for the offer, but we will
 17 take it up within our own group and provide you with
 18 the findings.
 19 At this point, let's go ahead and close
 20 this case and take it under advisement.
 21 And thank you very much for coming for
 22 this special hearing.
 23 (The proceedings concluded at 4:00 p.m.)
 24
 25

Page 233

1 CERTIFICATE
 2
 3 I, Paul Baca, RPR, CCR in and for the
 4 State of New Mexico, do hereby certify that the
 5 above and foregoing contains a true and correct
 6 record, produced to the best of my ability via
 7 machine shorthand and computer-aided transcription,
 8 of the proceedings had in this matter.
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Rudy H. Sims, Jr. Testimony
Special Examiner Hearing, Sept. 29, 2015
Page 47:13-23

13 Q. Okay. And Matador was not willing to
14 budge 1 percent on the risk penalty, was it?

15 A. We are not, and were not, willing to
16 accept something that does not represent custom and
17 practice in our industry.

18 Q. Okay.

19 A. So we would not go below a 100/300 percent
20 nonconsent penalty in the JOA.

21 Q. And that's because it's custom and
22 practice in the industry?

23 A. It is absolutely custom and practice.

Rudy H. Sims, Jr. Testimony
Special Examiner Hearing, Sept. 29, 2015
Page 51:12-25

47

12 Q. I'm starting with a JOA and just asking
13 you: Has there been a situation where Matador said,
14 Okay. We want to work with you so we'll -- we'll
15 give, and we won't require the
16 100 percent/300 percent in order to have agreement.

17 Has there been any instance of that sort
18 that you can tell us?

19 A. And as I said, custom and practice in our
20 industry is for a 100/300 percent nonconsent
21 penalty.

22 That is the penalty that Devon uses.
23 That's the penalty that Cimarex uses. That's the
24 penalty that virtually all oil and gas companies
25 use.

James Andrew Juett Testimony
Special Examiner Hearing, Sept. 29, 2015
Page 71:17-72:03

17 Q. Why did you recommend changing the target
18 formation to the Wolfcamp?

19 A. When we looked at the third Bone Spring,
20 the formation thins as we move across the section.
21 The porosity in Wolfcamp is much better than the
22 porosity in the third Bone Spring, and we thought we
23 would make a much better chance of making an
24 economic well out of the upper Wolfcamp zone here.

25 Q. Are there any known geological impediments
1 to drilling this well to the Wolfcamp formation?

2 A. There are none that I can see by the
3 mapping that I've done.

James Andrew Juett Testimony
Special Examiner Hearing, Sept. 29, 2015
Page 79:1-8, 20-25

1 Q. Okay. So can you tell the examiner the
2 extent of vertical wells penetrating the Wolfcamp in
3 that area?

4 A. In the area of the map, the Wolfcamp
5 structure data points you'll see is the light purple
6 attributes.

7 All of those wells penetrated the Wolfcamp
8 and went all the way through to the Strong.

...

20 All of those are vertical wells that
21 penetrated the Wolfcamp?

22 A. Yes, sir.

23 Q. Okay. And the formation is present in all
24 of those wells?

25 A. Yes, it was.

James Andrew Juett Testimony
Special Examiner Hearing, Sept. 29, 2015
Page 81:2-9

2 Q. Okay. That's Exhibit 13?

3 A. Yes, sir. Exhibit 13.

4 The third Bone Spring sand is the interval
5 between the green marker and the purple marker
6 on
7 this cross-section.

8 And what I've highlighted here is porosity
9 greater than 8 percent. And on this cross-section,
10 porosity --

James Andrew Juett Testimony
Special Examiner Hearing, Sept. 29, 2015
Page 81:25 - 82:8

25 But when we move down into the Wolfcamp,
1 we see an increase in porosity in the upper
2 Wolfcamp.

3 Q. Are we seeing a greater than 8 percent in
4 the Wolfcamp?

5 A. Yes.

6 Q. What would you say that value is?

7 A. That value is anywhere between 8 to 12,
8 and stringers of 14 percent porosity.

James Andrew Juett Testimony
Special Examiner Hearing, Sept. 29, 2015
Page 84:18-24

18 Q. But in order for the decision to be made
19 by Matador to drill this well, you have done a
20 reserve estimate, have you not?

21 A. Yes, sir.

22 Q. And what did that reserve estimate show?

23 A. Actually, it's going to be in the -- I
24 believe the 400,000-barrel range is our estimate.

Aaron Michael Byrd Testimony
Special Examiner Hearing, Sept. 29, 2015
Page 117:11-18

11 Q. Okay. And each of the wells was drilled
12 to target?

13 A. To the plan target?

14 Q. To the plan target.

15 A. Yes.

16 Q. And each of the wells was completed as
17 planned?

18 A. Correct.

Aaron Michael Byrd Testimony
Special Examiner Hearing, Sept. 29, 2015
Page 127:1- 9

1 THE WITNESS: We have experience drilling
2 a lot of these X, Y sands, both in Eddy County and
3 Loving, and we have seen that you need that -- in
4 any part of the Wolfcamp -- that you need a higher
5 mud weight before -- or else your well will start
6 collapsing on you.

7 MR. JONES: Okay.

8 THE WITNESS: And it will start flowing as
9 well.

10 MR. JONES: Okay. Wow.

Aaron Michael Byrd Testimony
Special Examiner Hearing, Sept. 29, 2015
Page 129:20- 130:1

20 MR. JONES: Okay. So is this going to
21 flow, this well, do you think, or you'll put a
22 pumping unit on it pretty quick?

23 THE WITNESS: One is, I would fully expect
24 for it to flow. Every Wolfcamp well we have
drilled
25 to date has flowed out the casing. And we don't
1 expect anything otherwise here.

Chapter 1

Definition of a Resource Play

What is a Resource Play?

The term "Resource Play" first appeared in publications in the early 1990s and was used to describe an accumulation of hydrocarbons known to exist over a large areal expanse that was believed to have a lower geological and/or commercial development risk. With this term, the oil and gas industry hoped to describe a "new" type of exploration and development process that exhibited both low risk and repeatable results. This was in contrast to conventional exploration projects with higher geologic uncertainty and hydrocarbon (wet?) risk. Some industry publications even compared this development process to the manufacturing and farming segments to describe the repeatable nature of the exploration process. Please note, the term "Resource Play" does not describe the classification of the hydrocarbon deposits, reserves versus resources in the SPE PRMS nomenclature, but rather the continuous aspect of the hydrocarbon deposit over a large regional extent.

Tier 1 Criteria

The characteristics nearly always observed in Resource Plays are:

1. Exhibits a repeatable statistical distribution of Estimated Ultimate Recoveries (EURs).
2. Offset well performance is not a reliable predictor of undeveloped location performance.
3. Continuous hydrocarbon system that is regional in extent.
4. Free hydrocarbons (non-sorbed) are not held in place by hydrodynamics.

If the reservoir being evaluated satisfies these four criteria, there is a very good chance the reservoir is a Resource Play and can be evaluated using the techniques discussed herein. Conversely, if any one of these characteristics is absent, it is quite likely the reservoir is NOT a Resource Play. The Tier 1 criteria are listed in order of significance. Both geological and

engineering data must support these criteria. If data conflicts exist, the evaluator should seriously consider if these guidelines and evaluation techniques are applicable.

The Tier 1 Criteria possess both engineering and geological aspects, and determination of whether a reservoir is a Resource Play cannot be made without consideration of both aspects. The geological depositional model needs to describe a reservoir with regional extent, while the engineering data needs to show statistically repeatable EURs over time. Obviously, to arrive at these conclusions requires sufficient time - time for historical data to accumulate, and time to analyze the data.

As a practical matter, Resource Plays will encompass many more than 100 completed wells in the reservoir. Two factors influence this determination. First, to develop a usable statistical model in a Resource Play typically requires about 100 wells. Secondly, a reservoir of sufficient areal extent to be considered a Resource Play will likely encompass a minimum of 100 wells.

Tier 2 Criteria

Although the following reservoir characteristics are not required, these are commonly observed in Resource Plays:

5. Requires extensive stimulation to produce at economic rates.
6. Produces little in-situ water (except for Coalbed Methane and Tight Oil Reservoirs).
7. Does not exhibit an obvious seal or trap.
8. Low permeability (< 0.1 md).

Although all of the characteristics are important in properly categorizing Resource Plays, it is the first characteristic "Exhibits a repeatable statistical distribution of EURs" that forms the focal point of the SPEE Resource Play Committee and the procedures for estimating reserves and resources.