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

APPLICATION OF BASS ENTERPRISES PRODUCTION CO. FOR AN ORDER AUTHORIZING THE DRILLING OF A WELL IN THE POTASH AREA, EDDY COUNTY, NEW MEXICO.

CASE NO. 13367
(DE NOVO)

APPLICATION OF DEVON ENERGY PRODUCTION COMPANY, L.P. FOR AN ORDER AUTHORIZING THE DRILLING OF A WELL IN THE POTASH AREA, EDDY COUNTY, NEW MEXICO.

CASE NO. 13368
(DE NOVO)

APPLICATION OF DEVON ENERGY PRODUCTION COMPANY, L.P. FOR APPROVAL OF AN UNORTHODOX WELL LOCATION AND AUTHORIZATION TO DRILL A WELL IN THE POTASH AREA, EDDY COUNTY, NEW MEXICO.

CASE NO. 13372
(DE NOVO)

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APPLICATION FOR REVIEW BY THE SECRETARY OF ENERGY, MINERALS AND NATURAL RESOURCES DEPARTMENT OF THE JULY 13, 2006 ORDERS OF THE OIL CONSERVATION COMMISSION (ORDER NOS. R-12403-A AND R-12403-A) AND THE AUGUST 10, 2006 DENIAL OF THE APPLICATION FOR REHEARING OF BASS ENTERPRISES PRODUCTION COMPANY AND DEVON ENERGY PRODUCTION COMPANY.

Pursuant to N.M.S.A. §70-2-26 (2006), Bass Enterprises Production Company ("Bass") and Devon Energy Production Company ("Devon"), through their undersigned attorneys, seek Secretarial review of Oil Conservation Commission Order Nos. R-12402-A and R-12403-A.[1] Copies of the Commission Order Nos. R-12402-A and R-12403-A are attached to this Application for Review as Exhibits A and B. Bass and Devon request the Secretary exercise her discretion and hold a hearing, pursuant to Section 70-2-26, to determine whether these orders contravene the public interest. In support of this Application, Bass and Devon state:

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[1] The Commission failed to enter an order on the Bass and Devon Application for Rehearing and it was therefore deemed denied as of August 16, 2006. NMSA 1978 §70-2-25 (2006).

INTRODUCTION

On July 13, 2006, the Oil Conservation Commission ("Commission") entered Order No. R-12402-A in Case No. 13367 and Order No. R-12403-A in Case Nos. 13368 and 13372 denying the applications of Bass and Devon for authorization to drill wells in the Potash Area.[2] With these orders, the Commission has announced a new interpretation of Order No. R-111-P and adopted a new Oil Conservation Division ("Division") and Commission policy concerning the regulation of mineral development in the Potash Area. These orders contravene the public interest for they do not conserve oil and gas resources, abdicate to the State Land Office and the Bureau of Land Management the Commission's duties to prevent waste and protect correlative rights, and abandon the Commission's jurisdiction to conserve the State's mineral resources in favor of protecting potential future development on federal lands.

Where the decisions of the Commission contravene the public interest, appeal may lie to the Secretary of the Department of Energy, Minerals and Natural Resources pursuant to NMSA § 70-2-26 which provides:

> "The secretary of energy, minerals and natural resources may hold a public hearing to determine whether an order or decision issued by the Commission contravenes the **public interest**. The hearing shall be held within twenty days after the entry of the Commission order or decision following a rehearing or after the order refusing rehearing. The hearing shall be a *de novo* proceeding, and the secretary shall enter such order or decision as may be required under the circumstances, **having due regard for the conservation of the state's oil, gas and mineral resources**, and the commission shall modify its own order or decision to comply therewith." (Emphasis Added)

Pursuant to this section of the Oil and Gas Act, and the expanded jurisdictional basis for review set forth therein, the Secretary should call these orders before her for further hearing and review and then require that the Commission modify these orders to protect the public interest and conserve the state's oil, gas and mineral resources.

GROUNDS FOR SECRETARIAL REVIEW

Protection of the "public interest" is not a responsibility within the jurisdiction of the Oil Conservation Commission. It is a matter reserved by the Oil and Gas Act to the Secretary and is the primary statutory basis for her review of a Commission decision. See Order No. R-11775-B, Finding 64. While "public interest" has not been interpreted in the context of decisions of the Oil Conservation Commission, the courts have found that analysis of the term "public interest" in other contexts is broad enough to encompass the public's interest in securing the development of mineral resources. *See National*

[2] The Potash Area is the area in which potash mining operations are now in progress, or in which core tests indicate commercial potash reserves. This area is coterminous with the Known Potash Leasing Area as determined by the BLM. See Order No. R-111-P Rule B.

Indian Youth Council v. Andres, 623 F.2d 694 (10th Cir. 1980) (citing *Battle v. Anderson*, 564 F.2d 388, 397 (10th Cir. 1977)). But an interpretation by the courts is not required in this case for the Oil and Gas Act defines what the term public interest means in the context of this statute. While the statutory basis for secretarial review is contravention of the public interest, in making her review, the Secretary must determine if these Commission order have "due regard for the conservation of the state's oil, gas and mineral resources."

Order Nos. R-12402-A and R-12403-A cause the waste of the state's oil gas and mineral resources and therefore violate the public interest. Review of these Commission orders by the Secretary is required by statute.

BACKGROUND

Potash and oil and gas are produced from the same lands and this has created problems for the oil and gas industry for decades. It has also created problems for the Oil Conservation Division since it is charged by the Oil and Gas Act with the prevention of waste of both oil and gas (N.M.S.A. § 70-2-2 (2006)) and potash resources. N.M.S.A. § 70-2-3.F (2006) and N.M.S.A. § 70-2-12.B(17) (2006).

In 1988, because operations had become "virtually unworkable because of the lack of tolerance on the part of both oil / gas and Potash Industries regarding the activities of the other industry in areas where leasehold interests are overlapping..." (Order No. R-111-P, Finding (3)), the Division convened a study committee from both industries to develop amendments to the regulations governing the development of these resources in the Potash Area.

The study committee reached an agreement ("Industry Agreement") which the Commission considered at its February 18, 1988 hearing. On April 21, 1988, Order R-111-P was adopted which promulgated "The Rules and Regulations Governing the Exploration and Development of Oil and Gas in Certain Areas Herein Defined, Which are Known to Contain Potash Reserves" ("the Potash Rules").

In adopting these rules, the Commission accepted much of the Committee's report including provisions for the creation of "Life of Mine Reserves" Areas ("LMR") within the potash area. Under this scheme, potash lessees annually designate lands for inclusion in a "Life of Mine Reserves" area. Data supporting the inclusion of lands in a LMR is submitted for review by the potash lessees to the State Land Office for state and fee lands and to the BLM for federal lands. The data presented by the potash lessee in support of the LMR is kept confidential and not shared with either the owner of the oil and gas interests or the Division or Commission.[3] If the agency agrees with the potash lessee's interpretation of the data, the acreage is included in a LMR. When an oil and/or gas well is proposed, the Division contacts the State Land Office for state and fee lands, or the BLM for federal lands, to confirm if the proposed well is in a LMR. If it is, the application to drill is denied unless certain conditions set out in the Potash Rules are met. Order No. R-111-P, Rule G(e)(3).

[3] Pursuant to R-111-P, "Information used by the potash lessee in identifying its LMR shall be filed with the BLM and SLO but will be considered privileged and confidential 'trade secrets and commercial . . . information' within the meaning of 43 C.F.R. §2.13(c)(4) (1986), Section 19-1-2.1 NMSA 1978, and not subject to public disclosure."

However, the Commission expressly recognized its statutory obligations to both industries. To assure that the owners of minerals rights were not arbitrarily denied the right to develop the minerals under a lease, the Commission added a provision to the proposed rules that provide that applications to drill in the LMR area, including buffer zones, may be approved only by mutual agreement of the owners of the potash and oil and gas mineral rights in a lease. Order No. R-111-P, Rule G(e)(3).

SUBSEQUENT DECISIONS

In the first cases to come before the Division and Commission after the adoption of Order No. R-111-P, each attempted to regulate these resources in a manner that met their statutory obligations to both industries.

In 1992, in **Yates v. NM Potash** ("NM Potash") (Case Nos. 10446 and 10447, Order Nos. R-9650 and R-9651, R-9650-A and R-9651-A), the Commission found that waste occurs if oil and gas operations prevent the mining of commercial potash reserves and that waste also occurs and correlative rights are violated if potash development prevents the development of oil and gas reserves under a lease. Order Nos. R-9650-A and R-9651-A, Finding 10; Order Nos. R-9650-B and R-9651-B, Finding 15.

Most importantly, the Commission did not accept the regulatory system announced in Order No. R-111-P that allows the potash industry to create LMR's that deny oil and gas operators the right to drill on leases in the Potash Area based on information kept secret from both the Division and the oil and gas operator. Order Nos. R-9650-A and R-9651-A, Findings 6 and 7. It did not treat the State Land Office/BLM process for the creation of an LMR as something that relieves the Commission of its duty to prevent the waste of oil and gas.

The Commission found that the mining plans that had been presented to it in these cases were little more than a "guess" of future activity and should not be relied upon until they incorporate oil and gas activity and firm development commitments by both parties. (Finding 15(6) R-9650-A and R-9651-A). It concluded that the evidence presented in these cases by both sides on safety issues, including subsidence, were argued from "a theoretical perspective." It characterized the data of the potash industry as "conjecture" and stated that "hard data" was needed. (Findings 12 and 15, Order Nos. R-9650-A and R-9651-A).

To avoid the mere conjecture, the Commission announced standards of proof that had to be met by operators in cases brought before it. The Commission prescribed the type of proof that it would require of potash operators to establish that oil and gas drilling would cause the waste of potash. These requirements are set out in Order Nos. R-9650-A and R-9651-A, Finding 15, and includes facts concerning the economics of drilling, actual methane measurements at the wells, core information to develop ore body information, actual subsidence measurements and "hard data" from pilot holes. Before the rights of an oil and gas owner could be denied, these standards had to be met.

The Commission also ordered a study of the technical issues involving the development of these competing resources - specifically addressing how new technologies impact the formation of LMR's and Buffer Zones (Order No. R-9650-B and R-9651-B, Finding 25) and called for the adoption of standards to govern the creation of an LMR. Order Nos. 9650-A and R-9651-A, Finding 15.

The facts in **Yates v. Noranda** ("Noranda") (Case No. 10490, Order No. R-9990) heard by the Commission in 1993 are virtually identical to those presented in these cases. Yates proposed to drill in the LMR area on a fee tract at a location 330 feet from a Noranda Minerals, Inc. potash lease. Noranda objected to the well location. The fee owner of the potash rights in the lease supported the Yates plan to drill the well and appeared at the hearing in support of Yates. In its findings in the order approving the application of Yates, the Division summarized its interpretation of the Potash Rules and expanded on the findings in Commission Cases Nos. 10446 and 10447. Order No. R-9990, Finding 23. The Division found that a potash lessee may not include in a LMR lands in which it has no potash lease and that, in approving the Application for Permit to Drill, the fundamental issue was "that all parties owning potash and oil and gas interests underlying a particular lease reached agreement on the extraction of their minerals." Order No. R-9990, Finding 11. (Emphasis added) It observed that the subject well location was within the Noranda LMR buffer zone (Order R-9990, Finding 12) but that there was agreement between the owner of the potash rights and the oil and gas operator and that the application therefore should be approved. Order No. R-9990, Findings 10, 13 through 15.

With these orders, the Commission tried to meet its statutory charge to both industries. Prior to the Commission orders at issue in these cases, the Division and Commission applied the evidentiary standards announced in NM Potash and each consistently recognized that wells may be drilled on **leases** where there is agreement for the drilling of the well between the owners of the potash and the oil and gas rights.[4] Prior to the Commission orders at issue in these cases, the Division has consistently approved applications for well permits in the Potash Area where there is no objection from the owner of the potash rights.[5]

BASS AND DEVON APPLICATIONS

The facts in each of these cases are the same and are virtually identical to the facts in the Noranda case. In each case, a mutual agreement for the development has been reached between all owners of the potash reserves and all owners of oil and gas rights in the fee leases upon which these wells are proposed to be drilled. In each case, Bass or Devon notified IMC Potash Carlsbad, Inc., (predecessor to Mosaic) the only lessee of potash reserves within one mile of the proposed well location, of its intent to drill the well and sought IMC's waiver of objection to the proposed location. In two cases, Mosaic did not timely object and the Applications for Permit to Drill were approved by the Division. In each case, Mosaic eventually objected to the applications and they were rescinded and set for hearing before a Division Examiner. In each case, the owner of the fee minerals, oil and gas and potash, appeared and testified in support of the application.

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[4] *See*, Yates / NM Potash, Case Nos. 10446 and 10447, Order No. R-9650-B and R-9651-B, Finding 8; Yates / Noranda, Case No. 10490, Order No. R- 9990; Devon / Mosaic, Case No. 13272, Division Order No. R-12158; and Bass / Mosaic, Case No. 13367, Order No. R-12402.

[5] *See,* Yates / Noranda, Case No. 10490, Order No. R- 9990; Yates / Mississippi, Case Nos. 11913. 11914, 11915, 11916, Order No. R- 10950; Hallwood / Mississippi, Case Nos. 12055, 12056, Order Nos. R-11092 and R-11093; Devon / Mosaic, Case No. 13272, Division Order No. R-12158; and Bass / Mosaic, Case No. 13367, Division Order No. R-12402.

Relying on the Noranda decision, the Applications for Permit to Drill were approved by the Division.

COMMISSION'S NEW INTERPRETATION OF THE POTASH RULES

With Order Nos. R-12402-A and R-12403-A, the Commission has changed its interpretation of the Potash Rules. Unlike its decisions in NM Potash and Noranda, the Commission does not attempt to balance the interests of the two industries and prevent waste of oil and gas. Instead, this new interpretation effectively creates areas that are off limits to oil and gas drilling, causes waste in contravention of the public interest.

With these orders, the Commission abdicates its statutory duty to prevent waste. It does not require evidence from potash operators that meet the standards of proof announced in the NM Potash orders. Instead, it denies applications for well permits based on determinations of the State Land Office and BLM and thereby abdicates its duties to prevent waste in violation of the Oil and Gas Act. Denying these permits prevents the production of oil and gas and prevents the owners of the potash rights from producing the minerals under their lands. These orders were entered without due regard for the conservation of the state's mineral resources and therefore contravene the public interest.

Unlike its prior orders, the Commission now interprets Order No. R-111-P to prevent the drilling of wells on fee lands that are under its jurisdiction to protect possible future development on federal lands that are not subject to Order No. R-111-P but, instead, regulated under the jurisdiction of the BLM. This interpretation violates the standard for secretarial review for it ignores the "conservation of the state's oil, gas and mineral resources" and therefore contravenes the public interest.

Finally, the new interpretation of the Potash Rules creates confusion. The standards of proof that had to be met before an oil and gas owner could be denied the right to drill are no longer applied to potash operators resulting in the denial of the right to drill based on mere conjecture of the potash lessee. Mutual agreement between the owners of both the oil and gas and potash interests to first develop their oil and gas interests no longer assures these owners the right to do so - as it has been since the order in Noranda. Under this new interpretation, the absence of an objection by the owner of the potash rights under the lease on which a well is proposed to be drilled does not clear the way for drilling. All of these departures form the Commission's prior interpretation, create confusion and cause the waste of the resources of the state in contravention of the public interest.

I
THE COMMISSION ORDERS PREVENT OIL, GAS AND MINERAL DEVELOPMENT AND THEREBY CONTRAVENE THE PUBLIC INTEREST

By statute, public interest includes the conservation of the state's oil, gas and mineral resources. An objective of the Potash Rules adopted by Order No. R-111-P is the conservation of these mineral resources. Order No. R-111-P (A. Objective) However, the Commission's new interpretation of the Potash Rules prevents drilling and creates areas that are off limits to oil and gas development.

The Commission decisions in the NM Potash and Noranda cases recognize that waste occurs when the owner of an oil and gas interest is prevented from developing its oil and gas reserves in the Potash Area and authorized the drilling of a well where the parties who owned interests under the subject land had reached a mutual agreement to do so (Order No. R-9650-A and No. R-9651-A, Finding 10). The Commission has ignored the mutual agreement of all owners in these leases and denied their applications for a permit to drill thereby denying their right to recover these resources.

This new interpretation of the Potash Rules effectively means that owners of oil and gas leases, like Bass, Devon, Stacy Mills and Kenneth Smith, who own mineral interests in fee tracts cannot develop their oil and gas rights – or their potash rights. Suggestions to the contrary are simply untrue and not supported by the record in these cases for the evidence established that Bass and Devon cannot economically develop these reserves by drilling horizontal or directional wells and that the Commission orders in these cases will cause substantial oil and gas to be left in the ground[6]. Contrary to prior interpretations of these rules, the Commission found that "[d]rilling for oil and gas after potash mining has occurred is difficult, if not impossible, because of the caverns created during the potash ore's extraction." (Orders R-12402-A and R-12403-A, Finding 12). The mining of potash can preclude the development of the underlying oil and gas reserves and an order that prevents the development of these resources causes waste in contravention of the public interest.

The operating and production requirements now imposed by the Commission will result in the wells that are the subject of the Bass and Devon applications not being drilled and reserves under the subject fee leases will be left in the ground and wasted. The public's interest in securing the development of the minerals resources of this State justifies secretarial review under Section 70-2-26.

II.

STATE REGULATION TO ASSURE THE CONSERVATION OF THE STATE'S OIL, GAS AND MINERAL RESOURCES IS IN THE PUBLIC INTEREST.

A. ORDER NOS. R-12402-A AND R-12403-A CONTRAVENE THE PUBLIC INTEREST FOR THE COMMISSION ABDICATES TO THE BUREAU OF LAND MANAGEMENT AND THE STATE LAND OFFICE ITS DUTY TO CONSERVE THE MINERALS OF THIS STATE.

The Commission's new interpretation of R-111-P fundamentally changes the way these resources are regulated. It requires more than the mutual agreement of all mineral

[6] Bass and Devon presented evidence from expert drilling engineers that a vertical well is the only way to test all potentially productive formations. Drilling from alternate locations would require the drilling of directional and horizontal well bores which cannot intersect and produce the reserves from each potentially productive formation under these 40-acre tracts. See Tr. 81 (Testimony of Dannels), Tr. 148 (Testimony of Blount) and are economically impossible to drill. Tr. 102 (Testimony of Dannels), Tr. 163 (Testimony of Blount).

owners in a lease to approve the drilling of a well thereon and it abandons the procedural safeguards and required standards of proof announced in NM Potash.

The Commission orders in these cases ignore its statutory duties to prevent the waste of oil and gas. Instead it abdicates these responsibilities to the State Land Office and the Bureau of Land Management in direct violation of its duties under the Oil and Gas Act. It would be bad public policy to allow this conflict between these two resources to be finally decided by a Commission that does not exercise its statutory authority to prevent the waste of both resources but, instead, merely accepts decisions made by other agencies based on information that is not available to the Commission or the parties.

As noted above, Order No. R-111-P authorizes the creation of LMR's based on data submitted to the State Land Office for state and fee lands and to the BLM for federal lands that is kept confidential and not shared with either the owner of the oil and gas interests or the Division or Commission. Even though the determination of a LMR, when applied by the Division to an operator, can prevent the oil and gas reserves from ever being developed.

To carry out the duties assigned to it by statute, in the past, the Commission did not accept the determination of another agency but also: (1) called for the production to affected oil and gas operators of data used by the potash lessee to support a LMR determination;[7] (2) adopted additional procedural safeguards and announced standards of proof that would have to be met before an oil and gas owner could be denied the right to drill; and (3) required the potash lessee provide "hard facts," not mere "conjecture," that reserves would be lost and mine safety compromised.

The new Commission policy fails to prevent waste or protect the correlative rights of the owners of oil and gas minerals interests – including the State. It no longer requires that potash operators meet the Commission-announced standards of proof and establish that waste will not occur - it merely accepts decisions made by other agencies. Under this new interpretation, the interest of potash operators and the State are at risk and may be denied by a system that permits mineral interests to be taken by *ex parte* proceedings between the potash lessees and the BLM or the State Land Office. Oil and gas operators and the State are excluded from these meetings and these decisions reached based on information the oil and gas operator may not see. Furthermore, the owners of oil and gas interests now have no forum in which they can effectively challenge the taking of their property. The new Commission interpretation represents a blanket denial of the rights of oil and gas owners to produce reserves - thereby causing waste.

The Secretary should exercise her authority to review these orders because they reject prior Commission-ordered procedures that protect the owners of each mineral resource in a tract and with these orders the Commission relinquishes its statutory duty to prevent waste to other government agencies.

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7 "When the designation of an LMR by a Potash operator may prevent an oil and gas operator from accessing its property, the oil and gas operator must be given the opportunity to review the geologic basis for the designation, with appropriate restrictions to protect the confidentiality of the data, in order to make a meaningful challenge." (Order No. R-9650-A and R-9651-A, Finding 7).

B. The Commission's refusal to conserve mineral development on state lands in favor of potential future development of minerals on federal lands violates the Oil and Gas Act.

The public has an interest in the conservation of natural resources. To protect the public interest, NMSA §70-2-26 authorizes the Secretary to call Commission orders before her for hearing where they have been entered without due regard for the conservation of the **state's** oil, gas and mineral resources. (Emphasis Added).

The rules that govern the development of oil, gas and potash in New Mexico are based on the ownership of the lands. While the rules adopted by Order R-111-P apply to State lands and are designed to assure the maximum conservation of all state resources,[8] federal lands are not subject to Order R-111-P and are separately administered under rules promulgated by the BLM.

Commission Order Nos. R-12402-A and R-12403-A violate the statutory charge to the Commission to protect the State's mineral interests for they prevent and thereby waste mineral production from fee lands under its jurisdiction in favor of potential future development of minerals under federal lands that are not subject to the Oil and Gas Act nor to Order No. R-111-P.

With these orders, the Commission has determined that "While the proposed location is on fee land, where life-of-mine reserves are not designated, the location is still less than one-half mile from Mosaic's life-of mine reserves located on federal lands. Therefore, Order R-111-P prohibits approval of Bass's APD." Order No. R-12402-A, Finding 43. Identical language appears in the Devon order. Order No. R-12303-A, Finding 46. This is a complete reversal of the decision in the NM Potash cases where the Division found that "denying Yates the opportunity to access for the purpose of recovering oil and gas under the state oil and gas lease in order to provide a buffer for the development of potash on an adjacent federal tract would be confiscation of both Yates' and the State's oil and gas rights without compensation." Order Nos. R-9650-A and R-9651-A, Finding 11.

With these orders, the Commission abandons its statutory mandate to prevent the waste of oil and gas resources under state and fee lands. Instead Order Nos. R-12402-A and R-12403-A prevent the development of the minerals on the subject fee tracts to protect potential mineral development on federal lands. Pursuant to the Commission's new policy, owners of interests not within the jurisdiction of the Commission, are permitted to prevent the development of minerals on fee and, presumably, state lands. These Commission orders are in clear violation of the Oil and Gas Act and fall squarely within the provisions of NMSA § 70-2-26, which authorizes the Secretary to call Commission orders before her for hearing where they have been entered without "due

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[8] "The objective of these Rules and Regulations is to prevent waste, protect correlative rights, assure maximum conservation of oil, gas and potash resources in New Mexico, and permit the economic recovery of oil, gas and potash minerals in the area hereinafter defined." (Order No. R-111-P, Rule A) (Emphasis added).

regard for the conservation of the **state's** oil, gas and mineral resources." (Emphasis Added).

III.
ORDER NOS. R-12402-A AND R-12403-A CREATE CONFUSION IN THE REGULATION OF OIL, GAS AND OTHER MINERALS AND DISCOURAGE DEVELOPMENT OF THE STATE'S OIL, GAS AND MINERAL INTERESTS IN CONTRAVENTION OF THE PUBLIC INTEREST.

The Commission orders denying the applications of Bass and Devon change the long-standing Division and Commission interpretation of the provisions of R-111-P. These provisions and interpretations were relied on by the oil and gas industry as it developed its strategy for the development of oil and gas resources in the Potash Area. The new interpretation raises questions that, until answered, create uncertainty and confusion concerning the development of the oil, gas and potash in the Potash Area and impact all other issues in the subject cases. This confusion will discourage the development of the State's oil, gas and mineral interests and therefore contravene the public interest. The following questions need to be clarified and only the Secretary can do so.

WHAT LANDS ARE COVERED BY R-111-P?

Under the Commission's new interpretation of the Potash Rules it is unclear how R-111-P applies to state, federal and fee lands and how the Commission is interpreting its jurisdiction in the Potash Area.

Federal Lands: Federal lands are not subject to Order No. R-111-P for these lands are regulated by the BLM pursuant to Sec. of Inter. Order, Oct. 12, 1986 (51 Fed. Reg. 39425). However, the Commission reverses its prior interpretation of its jurisdiction[9] and now cites R-111-P to deny the development of the resources under fee lands to provide protection for those who desire to develop potash on offsetting federal lands. (Orders R-12402-A and R-12403-A, Finding 43).

Do the Potash Rules apply to federal lands? By acting to protect potential future potash development on federal lands under the jurisdiction of the BLM, has the Commission acted outside its jurisdiction? In so doing, has it caused waste of oil and gas in contravention of the public interest?

Fee Lands: Under the new Commission interpretation of its rules, it is unclear if the Potash Rules apply to fee lands? It is now unclear if fee lands are subject to R-111-P. Ordering paragraph G(3) of R-111-P provides that drilling applications on state and fee land "will be processed by the Division." However, Potash Rule G(1)(b), which addresses the approval of LMR's, only applies to federal and state land and even the

[9] In R-12402-A (Finding 43), the Commission finds that in order to protect federal lands, a different mineral estate will not be developed. However, Order R-9650-A/9651-A, addressed this very issue and found that denying the recovery of the oil and gas under an oil and gas lease "in order to provide a buffer for the development of potash on an adjacent federal tract would be confiscation of....oil and gas rights without compensation." See Finding 9.

Division observed in the Noranda order, that there is no process under this rule for approval of a LMR on fee lands. (Order No. R-9990, Finding 1).

Furthermore, Mosaic's counsel also addressed this issue at the hearing and stated that at the time Order R-111-P was drafted and adopted, fee land was not considered.[10] Accordingly, there remains a real question as to whether or not Order R-111-P applies to fee lands. If it does not, the Commission's orders denying the applications to drill of Bass and Devon are not supported by R-111-P and should be approved.

This new interpretation of the rules creates issues that the Secretary must address. Until she does no one knows whether federal and fee lands will be subject to and regulated by R-111-P or how these interests can be developed or the owners of the mineral interests in these lands protected. The Secretary can only correct this problem with a hearing.

WHO MAY DEVELOP THESE MINERALS AND WHO MAY PREVENT DEVELOPMENT?

The new Commission interpretation writes out of R-111-P the provision that permits drilling where agreement is reached between the owners of the oil and gas interests and those who own the potash. No longer can an oil and gas operator drill if, as in the past, it has reached an agreement with the owners of the potash mineral rights under the lease. Now the Commission ignores the ownership of mineral interests and the character of the lands. Now owners of interests not within the jurisdiction of the Commission, are permitted to prevent the development of minerals on fee and, presumably, state lands.

This new policy takes from the fee owners like Stacy Mills and Kenneth Smith their right to develop the oil and gas rights under their lands for the foreseeable future and denies these owners access to these reserves because a potash company speculates that it may someday develop the potash reserves, if any, under these lands. Even where, as here, the potash operators have <u>failed to even lease the potash reserves.</u> This policy needs clarification.

TO DEVELOP MINERALS IN THE POTASH AREA, WHAT AGREEMENTS AND WAIVERS ARE NEEDED?

Although the Division has found that Order R-111-P does not authorize a potash lessee to designate a LMR over lands not leased to a potash lessee, the Commission's

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[10] Statement of Charles High: "I negotiated R-111-P, I wrote the industry agreement, I was there. And I will tell you that the idea of fee land never came up. No one ever had a clue about how fee would be handled under R-111-P. And when it did come up, the Snyder Ranch case (Noranda), we argued about how it was, we had one view of what it ought to do, and somebody else had another one. And the OCC – or the OCD made a decision as to how it would be handled. But that was never contemplated under R-111-P if what you would do if you had fee simple land, as opposed to State land or BLM land, which is – what 99-point whatever percent of the land down there. So there was never any consideration ever given to that." (Tr. at 236).

new interpretation prohibits drilling by Bass and Devon, because they are within a 1/2 mile buffer zone surrounding a LMR. This argument is in direct conflict with the terms of Rule G(3) of Order R-111-P quoted above which expressly include "buffer zones" in the area where wells can be drilled by agreement of the owners of the minerals under these tracts.

Under the Commission's new interpretation it is unclear what owners are required to enter agreements for the drilling of oil and gas well or waive objection thereto. This should be clarified by the Secretary.

IF A HEARING IS REQUIRED, WHO BEARS THE BURDEN OF PROOF?

In 1992, the Commission announced in the NM Potash cases what standard of proof it would require of a potash operator when it was opposing a proposed drilling location. These standards have been abandoned by the Commission in the Bass and Devon cases. No evidence was presented that complied with Commission-announced standards on the waste of potash or the safety issues that may result from the drilling of an oil and gas well in the Potash Area. These orders create confusion as to what must be presented by mineral owners in future cases and by whom must this evidence be presented. Furthermore, if the new interpretation places the burden of proof in these cases solely on the oil and gas industry, the Secretary must assure access to information needed to make the required showings.

CONCLUSION

These orders create a situation that require a re-examination of the regulatory scheme by the agency or forces oil and gas operators to seek review by the courts of the legal issues and ask the courts to return these matters to the agency for resolution.

With Order Nos. R-12402-A and R-12403-A, the Commission has reverted to the very problems that were of concern to and addressed by the Commission in the NM Potash and Noranda Cases. At that time, the Commission was convinced that rights were being impaired by the R-111-P regulation of these resources. It determined that further study was needed on the technical issues concerning the development of these competing resources, and that these rules needed to be examined in terms of current technologies. It called for study of the confidentiality issue and joint resources development. All of these problems still require further study.

However, further study will not help Stacy Mills, Kenneth Smith, Bass, Devon or the other interest owners in the subject spacing units. Their interests can only be protected by orders that permit these wells to be drilled because there is agreement between all owners – oil, gas, and potash - in the affected leases to do so. It is the duty of the Oil Conservation Commission to conserve – not waste – the oil and gas on state and fee lands. The only way to meet these statutory responsibilities and to regulate these resources in the public interest is to direct the Commission to, on the facts of these cases approve these Applications for Permits to Drill in accordance with the interpretation of these rules that has governed Division decisions for more than a decade.

Respectfully submitted,
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CERTIFICATE OF SERVICE

I certify that on August 13, 2006 I served a copy of the foregoing Memorandum Brief by Hand Delivery, Facsimile or by Overnight Delivery to:

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