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2006 AUG 15 PM 4 09

August 15, 2006

Hand delivered

Case 13777

Florene Davidson
Oil Conservation Division
1220 South St. Francis Drive
Santa Fe, New Mexico 87505

Dear Florene:

Enclosed for filing, on behalf of Cimarex Energy Co., are an original and one copy of an application for compulsory pooling, together with a proposed advertisement. The advertisement has also been e-mailed to the Division. Please set this matter for the September 14, 2006 Examiner hearing.

A pre-hearing statement is also enclosed. Thank you.

Very truly yours,

James Bruce

Attorney for Cimarex Energy Co.

PERSONS BEING POOLED

Bruce W. Crockett
1611 Jackson Street
Roswell, New Mexico 88201

Dr. James Obed Baker (wife Vera)
9337 Redondo Dr.
Dallas, Texas

Fred T. Schooler
P.O. Box 843
Midland, Texas

Occidental Permain Ltd.
(formerly Altura Energy, Ltd.)
P.O. Box 4294
Houston, Texas 77210

Randall Pettigrew
8986 Hialena Cr. South
North Richland Hills, Texas 76180

Richard Pettigrew
2812 Pinewood Dr.
League City, Texas 77573

Frank S. Hayford
Apt. 35
2770 19th Street
San Francisco, CA 94132

M. K. Bennett

The Blanco Company
P.O. Box 1698
Roswell, New Mexico 88202

BEFORE THE NEW MEXICO OIL CONSERVATION DIVISION

2006 AUG 15 PM 4 09

APPLICATION OF CIMAREX ENERGY CO. FOR COMPULSORY POOLING, LEA COUNTY, NEW MEXICO.

Case No. 13777

APPLICATION

(OGRD 215099)

Cimarex Energy Co. applies for an order pooling all mineral interests in the Wolfcamp formation underlying the SW¼NW¼ and NW¼SW¼ of Section 21, Township 15 South, Range 36 East, N.M.P.M., Lea County, New Mexico, and in support thereof, states:

1. Applicant is an interest owner in the SW¼NW¼ and NW¼SW¼ of Section 21, and has the right to drill a well thereon.

30-025-37925

2. Applicant proposes to drill its Caudill South "21" Fee Well No. 2H to a depth sufficient to test the Wolfcamp formation, and seeks to dedicate the SW¼NW¼ and NW¼SW¼ of Section 21 to the well to form a standard 80 acre oil spacing unit (project area) for any formations and/or pools developed on 40 acre spacing within that vertical extent, including the Caudill-Permo Upper Penn Pool. The well will be a horizontal well, with a surface location 2000 feet from the south line and 940 feet from the west line of the section and a terminus located 1650 feet from the north line and 940 feet from the west line of the section.

3. Applicant has in good faith sought to obtain the voluntary joinder of all other mineral interest owners in the SW¼NW¼ and NW¼SW¼ of Section 21 for the purposes set forth herein.

4. Although applicant attempted to obtain voluntary agreements from all mineral interest owners to participate in the drilling of the well or to otherwise commit their interests to the well, certain interest owners have failed or refused to join in dedicating their interests.

Therefore, applicant seeks an order pooling all mineral interest owners in the SW¼NW¼ and NW¼SW¼ of Section 21, pursuant to NMSA 1978 §70-2-17.

5. The pooling of all mineral interests underlying the SW¼NW¼ and NW¼SW¼ of Section 21 will prevent the drilling of unnecessary wells, prevent waste, and protect correlative rights.

WHEREFORE, applicant requests that, after notice and hearing, the Division enter its order:

A. Pooling all mineral interests in the SW¼NW¼ and NW¼SW¼ of Section 21 in the Wolfcamp formation;

B. Designating applicant as operator of the well;

C. Considering the cost of drilling and completing the well, and allocating the cost among the well's working interest owners;

D. Approving actual operating charges and costs charged for supervision, together with a provision adjusting the rates pursuant to the COPAS accounting procedure; and

E. Setting a 200% charge for the risk involved in drilling and completing the well in the event a working interest owner elects not to participate in the well.

Respectfully submitted,

James Bruce
Post Office Box 1056
Santa Fe, New Mexico 87504
(505) 982-2043

Attorney for Cimarex Energy Co.

PROPOSED ADVERTISEMENT

Case No. 13777 **: Application of Cimarex Energy Co. for compulsory pooling, Lea County, New Mexico.** Cimarex Energy Co. seeks an order pooling all mineral interests in the Wolfcamp formation underlying the SW/4NW/4 and NW/4SW/4 of Section 21, Township 15 South, Range 36 East, NMPM, to form an 80-acre oil spacing unit (project area) for any and all formations or pools developed on 40-acre spacing within that vertical extent, including the Caudill-Permo Upper Penn Pool. The unit is to be dedicated to the Caudill South "21" Fee Well No. 2H, a horizontal well to be drilled at a surface location 2000 feet from the south line and 940 feet from the west line with a terminus located 1650 feet from the north line and 940 feet from the west line of Section 21. Also to be considered will be the cost of drilling and completing the well and the allocation of the cost thereof, as well as actual operating costs and charges for supervision, designation of applicant as operator of the well, and a 200% charge for the risk involved in drilling and completing the well. The unit is located approximately 4-1/2 miles north-northeast of Lovington, New Mexico.

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

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

CASE NO. 13777
ORDER NO. R-12682

APPLICATION OF CIMAREX ENERGY COMPANY FOR COMPULSORY POOLING, LEA COUNTY, NEW MEXICO

ORDER OF THE DIVISION

BY THE DIVISION:

This case came on for hearing at 8:15 a.m. on September 14, 2006 before Examiner William V. Jones.

NOW, on this ___ day of December, 2006, the Division Director, having considered the testimony, the record and the recommendations of the Examiner,

FINDS THAT:

(1) This is a case of first impression for the Oil Conservation Division.

(2) Cimarex Energy Company ("applicant" or "Cimarex") seeks an order pooling all uncommitted mineral interests in the Wolfcamp formation underlying the SW/4 NW/4 and NW/4 SW/4 of Section 21, Township 15 South, Range 36 East, NMPM, Lea County, New Mexico, for any and all pools developed on 40-acre spacing within that vertical extent, including but not limited to the Caudill-Permo Upper Penn Pool (10830).

(3) As allowed in Division Rule 111, the applicant intends to form an 80-acre "project area" by combining two contiguous 40-acre spacing and proration units for purposes of drilling a horizontal well. Applicant seeks an order pooling the entire 80-acre project area.

(4) The Oil and Gas Act authorizes the Division to pool interests "in a spacing or proration unit." NMSA 1978 Sec. 70-2-17.C, as amended. Although this statute does not authorize the Division to pool an area larger than a spacing or proration unit, the Division has authority to create a non-standard spacing unit, larger than the standard unit for a particular pool, and pool all interests in the non-standard unit. *Rutter & Wilbanks Corp. v. OCC,* 87 NM 286, 532 P2d 582 (1975).

(5) Rule 111 authorizes the creation of a project area but does not purport to authorize compulsory pooling of the area so created.

(6) For the Division to create a non-standard unit as contemplated in this application, the applicant should present evidence demonstrating that doing so will prevent waste and protect correlative rights. No such evidence was offered at the hearing on this matter.

(6) In addition, where the unit sought to be created is larger than the normal spacing unit for the pool, pooling provisions in lease forms in common use (the particular leases are not in evidence) might not be construed to authorize the lessee to pool the royalty interest without joinder of the royalty owners. Accordingly, the royalty owners should be notified of this proceeding and afforded an opportunity for a hearing.

IT IS THEREFORE ORDERED THAT:

(1) The application of Cimarex Energy Company in this case shall be set for re-hearing on the next available Division Examiner Docket more than 20 days after the issuance of this order.

(2) Applicant shall notify all owners of all interests in the oil and gas in and under the area sought to be pooled.

(3) Applicant shall be afforded and opportunity, at the re-hearing, to show, by appropriate technical evidence, that the establishment of the proposed unit will prevent waste and will not impair correlative rights.

(4) Jurisdiction of this case is retained for the entry of such further orders as the Division may deem necessary.

DONE at Santa Fe, New Mexico, on the day and year hereinabove designated.

STATE OF NEW MEXICO
OIL CONSERVATION DIVISION

MARK E. FESMIRE, P.E.
Director

S E A L

DWJ 11/28/06 Draft

DRC 11/29

See attached memo DB 11/29

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

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

12/1/06

CASE NO. 13777
ORDER NO. R-

APPLICATION OF CIMAREX ENERGY COMPANY FOR COMPULSORY POOLING, LEA COUNTY, NEW MEXICO

ORDER OF THE DIVISION

BY THE DIVISION:

This case came on for hearing at 8:15 a.m. on September 14, 2006 before Examiner William V. Jones.

NOW, on this ___ day of December, 2006, the Division Director, having considered the testimony, the record and the recommendations of the Examiner,

FINDS THAT:

(1) Due public notice has been given, and the Division has jurisdiction of this case and of the subject matter.

(2) Cimarex Energy Company ("applicant" or "Cimarex") seeks an order pooling all uncommitted mineral interests in the Wolfcamp formation underlying the SW/4 NW/4 and NW/4 SW/4 of Section 21, Township 15 South, Range 36 East, NMPM, Lea County, New Mexico, for any and all pools developed on 40-acre spacing within that vertical extent, including but not limited to the Caudill-Permo Upper Penn Pool (10830).

(3) The applicant intends to file form C-102 with the district office of the Division and form an 80-acre "Project Area" consisting of the aforementioned two standard 40-acre oil spacing and proration units.

(4) The applicant proposes to dedicate this Project Area to its proposed horizontal Caudill South 21 Fee Well No. 2H (API No. 30-025-37925), "the proposed well." The proposed well will first be drilled vertically to 10617 feet in the NW/4 SW/4 of Section 21 at a standard location 2000 feet from the South line and 940 feet from the West line, then will be deviated north and drilled horizontally to a standard bottom hole location, with a measured depth of 12100

feet, in the SW/4 NW/4 of Section 21, 1650 feet from the North line and 940 feet from the West line.

(5) Cimarex presented testimony by affidavit from a Landman at the hearing as follows:

(a) Applicant seeks to pool unsigned mineral owners within the SW/4 NW/4 of Section 21 who either cannot be located or have failed to respond to lease offers and well proposals.

(b) Applicant has made a good faith effort to locate and sign all owners within this Project Area.

(c) Applicant has the right to drill within both the NW/4 SW/4 and the SW/4 NW/4 of Section 21.

(d) Applicant has drilled other Wolfcamp wells near this Project Area and seeks to increase the productivity of the Wolfcamp through a horizontal completion.

(e) Acreage from both 40-acre tracts will be contributing to the well's production.

(f) Revenue will be allocated to the owners based on each owner's percentage of acreage within the Project Area.

(6) No other parties entered an appearance in this case.

(7) As allowed in Division Rule 111, the applicant intends to form an 80-acre "Project Area" by combining two contiguous spacing and proration units for purposes of drilling a horizontal well. This 80-acre Project Area is needed in order to efficiently utilize the latest horizontal drilling technology and to recover more oil reserves than would otherwise be recovered from drilling vertical wells. Formation of this Project Area and pooling of interests within this Project Area will prevent waste and protect correlative rights.

(8) Two or more separately owned tracts are embraced within the Project Area, and/or there are royalty interests and/or undivided interests in oil and gas minerals in one or more tracts included in the unit that are separately owned.

(9) Applicant is an owner of an oil and gas working interest within both 40-acre spacing and proration units within this Project Area. Applicant has the right to drill and proposes to drill the proposed well to a common source of supply within this Project Area.

(10) There are interest owners in this Project Area that have yet not agreed to pool their interests.

(11) The applicant should be designated as the operator of the proposed well and of this Project Area.

(12) Reasonable charges for supervision (combined fixed rates) should be fixed at $6000 per month while drilling and $600 per month while producing, provided that these rates should be adjusted annually pursuant to Section III.1.A.3. of the COPAS form titled "*Accounting Procedure-Joint Operations.*"

(13) To avoid the drilling of unnecessary wells, protect correlative rights, prevent waste and afford to the owner of each interest in this Project Area the opportunity to recover or receive without unnecessary expense its just and fair share of hydrocarbons, this application should be approved by pooling all uncommitted mineral interests, whatever they may be, within this Project Area.

IT IS THEREFORE ORDERED THAT:

(1) Pursuant to the application of Cimarex Energy Company, all uncommitted mineral interests are hereby pooled in the Wolfcamp formation underlying the SW/4 NW/4 and NW/4 SW/4 of Section 21, Township 15 South, Range 36 East, NMPM, Lea County, New Mexico, for any and all pools developed on 40-acre spacing within that vertical extent, including but not limited to the Caudill-Permo Upper Penn Pool (10830).

Cimarex shall submit form C-102 and otherwise apply to the district office of the Division to form an 80-acre "Project Area" consisting of the aforementioned two standard 40-acre oil spacing and proration units. This Project Area shall be dedicated to the applicant's proposed horizontal Caudill South 21 Fee Well No. 2H (API No. 30-025-37925), "the proposed well."

The proposed well shall be drilled at a standard surface location within the NW/4 SW/4 of Section 21 horizontally to a standard bottom hole location within the SW/4 NW/4 of Section 21. The well shall be drilled to the Wolfcamp formation and shall be oriented horizontally in order to produce oil from the Wolfcamp formation within the Project Area.

(2) Cimarex Energy Company (OGRD 215099) is hereby designated as the operator of the proposed well and of the Project Area.

(3) The operator of the Project Area shall commence drilling the proposed well on or before March 31, 2007, and shall thereafter continue drilling the well with due diligence to test the Wolfcamp formation.

(4) In the event the operator does not commence drilling the proposed well on or before March 31, 2007, Ordering Paragraph (1) shall be of no effect, unless the operator obtains a time extension from the Division Director for good cause.

(5) Should the subject well not be drilled and completed within 120 days after commencement thereof, Ordering Paragraph (1) shall be of no further effect, and the Project Area created by this Order shall terminate unless the operator appears before the Division Director and obtains an extension of time to complete the well for good cause demonstrated by satisfactory evidence.

(6) Upon final plugging and abandonment of the Caudill South 21 Fee Well No. 2H, the pooled Project Area created by this Order shall terminate, unless this order has been amended to authorize further operations.

(7) After pooling, uncommitted working interest owners are referred to as pooled working interest owners. ("Pooled working interest owners" are owners of working interests in the Project Area, including unleased mineral interests, who are not parties to an operating agreement governing the Project Area.)

(8) After the effective date of this order, the operator shall furnish the Division and each known pooled working interest owner in the Project Area an itemized schedule of estimated costs of drilling, completing and equipping the proposed well ("well costs").

(9) Within 30 days from the date the schedule of estimated well costs is furnished, any pooled working interest owner shall have the right to pay its share of estimated well costs to the operator in lieu of paying its share of reasonable well costs out of production as hereinafter provided, and any such owner who pays its share of estimated well costs as provided above shall remain liable for operating costs but shall not be liable for risk charges. Pooled working interest owners who elect not to pay their share of estimated well costs as provided in this paragraph shall thereafter be referred to as "non-consenting working interest owners."

(10) The operator shall furnish the Division and each known pooled working interest owner (including non-consenting working interest owners) an itemized schedule of actual well costs within 90 days following completion of the proposed well. If no objection to the actual well costs is received by the Division, and the Division has not objected within 45 days following receipt of the schedule, the actual well costs shall be deemed to be the reasonable well costs. If there is an objection to actual well costs within the 45-day period, the Division will determine reasonable well costs after public notice and hearing.

(11) Within 60 days following determination of reasonable well costs, any pooled working interest owner who has paid its share of estimated well costs in advance as provided above shall pay to the operator its share of the amount that reasonable well costs exceed estimated well costs and shall receive from the operator its share of the amount that estimated well costs exceed reasonable well costs.

(12) The operator is hereby authorized to withhold the following costs and charges from production:

(a) the proportionate share of reasonable well costs attributable to each non-consenting working interest owner who has not paid its share of estimated well costs within 30 days from the date the schedule of estimated well costs is furnished; and

(b) as a charge for the risk involved in drilling the well, 200 percent of the above costs.

(13) The operator shall distribute the costs and charges withheld from production, proportionately, to the parties who advanced the well costs.

(14) Reasonable charges for supervision (combined fixed rates) are hereby fixed at $6000 per month while drilling and $600 per month while producing, provided that these rates shall be adjusted annually pursuant to Section III.1.A.3. of the COPAS form titled "*Accounting Procedure-Joint Operations.*" The operator is authorized to withhold from production the proportionate share of both the supervision charges and the actual expenditures required for operating the well, not in excess of what is reasonable, attributable to pooled working interest owners.

(15) Except as provided above, all proceeds from production from the proposed well that are not disbursed for any reason shall be placed in escrow in Lea County, New Mexico, to be paid to the true owner thereof upon demand and proof of ownership. The operator shall notify

the Division of the name and address of the escrow agent within 30 days from the date of first deposit with the escrow agent.

(16) Any unleased mineral interest shall be considered a seven-eighths (7/8) working interest and a one-eighth (1/8) royalty interest for the purpose of allocating costs and charges under this order. Any well costs or charges that are to be paid out of production shall be withheld only from the working interests' share of production, and no costs or charges shall be withheld from production attributable to royalty interests.

(17) Should all the parties to this compulsory pooling order reach voluntary agreement subsequent to entry of this order, the forced pooling provisions of this order shall thereafter be of no further effect.

(18) The operator of the well and Project Area shall notify the Division in writing of the subsequent voluntary agreement of all parties subject to the forced pooling provisions of this order.

(19) Jurisdiction of this case is retained for the entry of such further orders as the Division may deem necessary.

DONE at Santa Fe, New Mexico, on the day and year hereinabove designated.

STATE OF NEW MEXICO
OIL CONSERVATION DIVISION

MARK E. FESMIRE, P.E.
Director

S E A L

MEMORANDUM

To: Hon. William V. Jones
(and anyone else who may be concerned herewith)

From: David K. Brooks

Date: November 29, 2006

Re: Case No. 13777, Application of Cimarex Energy Company for Compulsory Pooling

Note I have read this Memo and agree that more Geological Testimony is needed and more NOTICE should be provided or Determination of UNIFORM ownership. WJ Jones 11/29/06

ON THE IMPORTANCE OF LEGAL CONUNDRUMS or
WHO GAVE US THE RIGHT TO DO THIS?

Facts

Cimarex seeks to force pool an 80-acre project area for a horizontal well. The project area is to be formed pursuant to Rule 111 and consists of two contiguous 40-acre oil units in different quarter sections.

Does OCD have authority to force pool a project area consisting of more than one unit?

I think the answer in substance is yes, although there may be a little room for uncertainty. NMSA Section 70-2-17, which is the source of the Division's compulsory pooling authority, expressly confines that authority to a particular spacing or proration unit. However, the Supreme Court, in *Rutter & Wilbanks Corp. v. OCC,* 87 NM 286, 532 P2d 582 (1975), held that the OCC had power to create a non-standard spacing unit that was larger than a standard unit for the pool, and then force pool that non-standard unit. In that case, the Commission, confronted with an 820-acre section, created two stand-up non-standard units, each consisting of approximately 410 acres, and force pooled each of the units. An owner whose interest was limited to a tract in the southern part of the section challenged the order, contending that, in a pool spaced on 320 acres, the Commission could not force pool a unit larger than 320 acres. Citing the predecessor of NMSA Section 70-2-18.C, which specifically authorizes non-standard spacing units, the Court said:

> Recognizing the Commission's power to pool separately owned tracts "within a spacing or proration unit," as well as its concomitant authority to establish oversize non-standard spacing units, it would be absurd to hold the Commission does not have authority to pool separately owned tracts within a oversize non-standard spacing unit. 87 NM at 289.

Rutter & Wilbanks is, perhaps, not necessarily dispositive of the question posed, because a question may remain whether Rule 111 is intended as an exercise of OCD's authority to

establish non-standard spacing units. Rule 111 does not, in specific terms, provide that a project area is, itself, a spacing unit. Rather it states that a project area may consist of one or more spacing units. And it does not purport to deal with how production may be shared among owners within the project area.

Nevertheless, if there were no procedural or practical objections to consider, I would opine that Rule 111 does, in substance, provide for non-standard spacing units, and that compulsory pooling of a project area larger than one standard unit is ok. I believe that probably was, in substance, the intent of Rule 111.

Procedural Objections

1. Evidence. If this were a contested case before the Commission, I think it clearly would be an abuse of discretion to enter the proposed order on this record. We have broad discretionary power to create non-standard units, but I think the exercise of that power reasonably must require a finding that the non-standard unit will prevent waste and not impair correlative rights. Since there is no technical evidence in this case, there would be no basis for such a finding. This, however, is not a contested proceeding. The noticed parties can challenge it only by filing a de novo application before the Commission, and, if they do that, the Commission will decide on the record made there. So our order, even if technically erroneous, could not be legally challenged unless there are affected parties that were not noticed.

2. Notice. Are there any persons who are or may be adversely affected who have not been noticed? I cannot answer that question from the record in this case. This case was presented on affidavit, without live testimony, and the landman's affidavit does not identify the working interest owners other than the unleased mineral interest owners who are identified as the persons sought to be force pooled. Jim Bruce stated (Tr. 10) that he believed that Cimarex is the only working interest owner.

We do not, however, know anything about royalty owners. We do not know who they are, or whether there interest extends to the entirety of the proposed project area, or only a part thereof. Rule 1210 does not require notice to royalty owners if their royalty is "subject to a pooling or unitization clause." Ordinarily such a clause would authorize the lessee, as a matter of contract law, to pool the royalty owner's interest without the royalty owner's consent. That would not necessarily be the case on these facts. The authority of the working interest owner to commit royalties to a larger than standard unit for the purpose of drilling a horizontal well cannot be regarded as a foregone conclusion, and likely depends on the particular language of the applicable lease provisions. *See Browning Oil Co. v. Luecke*, 38 SW3d 625, 149 O&GR 127 (Tex App - Austin 2001) (Royalty owners not contractually bound to unit created for horizontal well on particular facts, even though unit was authorized by TXRRC rules). Since the royalty owners were not notified of the OCD proceeding, if they are not bound contractually, and perhaps even if they are, our order would be void as to them to the extent they were adversely affected. *Uhden v. NMOCC*, 112 NM 528, 817 P2d 721 (1991) (Order increasing size of spacing unit was void as to royalty owners who were not notified of the proceeding.). I note that Rule 111, perhaps unfortunately, does not require any notice of an application to establish a project

area, except to BLM or SLO if federal or state lands are affected. This fact, however, would not preclude applicability of *Uhden* since that decision was based on constitutional due process.

For these reasons, I would recommend, as a minimum, that counsel be asked to supplement the record with evidence establishing, if such is the case, that royalty ownership, other than the unleased interests, is uniform throughout the proposed project area. If that is not the case, the matter should be set for rehearing, and notice should be given to the royalty owners concerned, as well as a record made setting forth who has what leases, and who are the affected royalty owners.

Practical Considerations

My second concern is more a policy issue than a legal issue. It could be argued that the unleased mineral owners who were the named respondents in this case are entitled to somewhat more solicitude from the OCD than would be active operators, and that despite the fact that they have not filed objections or appeared at the hearing, we should require some technical evidence to establish that their correlative rights will not be adversely affected. This would require a rehearing regardless of whether there are additional parties who should be noticed. As I have suggested before, I am inclined to leave policy decisions to the policy makers, *i.e.,* the Bureau Chief or the Division Director.

December 05, 2006

Mark:

This is one of those areas where no clear direction is provided either by the Statutes or the rules. This type of case has never come up before in compulsory pooling applications, so that any order we issue in this case will be precedent-setting. Therefore, I suggest we should err on the side of caution. Let us send this case back to the next available Division hearing to enable the applicant conduct an extensive and exhaustive due process and present additional technical evidence and testimony in this case. Our objective here is to prevent WASTE and protect CORRELATIVE RIGHTS . We would have done our job if both objectives are met (**emphasis added**).

Richard

~~What Does David Say?~~

Remand for Davids Findings - Also re-notice to make sure Royalty owners have opportunity to be Heard.

Richard, David ? & Will - Lets Meet Prior to X-Mas to discuss force pooling Horiz locations and How we will standardize decisions

MEF