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

IN THE MATTER OF THE APPLICATION OF COG OPERATING LLC FOR DESIGNATION OF A NON-STANDARD OIL SPACING AND PRORATION UNIT AND FOR COMPULSORY POOLING, CHAVES COUNTY, NEW MEXICO

CASE NOS. 14203 and 14204

COG OPERATING LLC'S HEARING MEMORANDUM

COG Operating LLC, ("COG"), through its attorneys, Montgomery and Andrews, P. A., submits its Hearing Memorandum addressing factors relevant to contested compulsory pooling proceedings.

Background

COG has filed two applications, both seeking approval of non-standard 160-acre oil spacing and proration units and for compulsory pooling as follow:

Case No. 14203 (Taurus Federal Well No. 1): S/2 S/2 of Section 10, Township 15 South Range 31 East, NMPM.

In this unit, COG owns 50% of the working interest and Cimarex Energy Company owns (or purports to own) the remaining 50%.

Case No. 14204 (Taurus State Well No. 2): N/2 S/2 of Section 10, Township 15 South Range 31 East, NMPM.

Waive Notice

In this unit, COG also owns 50% of the working while Cimarex Energy Company owns (or purports to own) 50%.

In 2006, COG began its geological evaluation of the area.

In April 2007, COG began acquiring interests in the lands. On information and belief, yet to be verified, Cimarex did not acquire its interests until October 29, 2008. As of this date, Cimarex does not have record title interest.[1]

On September 17, 2007, following negotiations, COG executed its Surface Use Agreement for these well locations with the surface owner/tenant.

On September 26, 2007, COG submitted its APD to the BLM for the Taurus Federal No. 1 Well, which was approved on December 12, 2007.

On December 14, 2007, COG filed its APD for the Taurus State Com No. 2 Well with NMOCD, which was approved that same day.

On December 17, 2007, COG made well proposals for both wells to the proper interest owner of record, Chevron USA.

In January 2009, COG is scheduled to spud the first of these wells.

On September 28, 2008, COG filed its compulsory pooling applications for these lands.

[1] An applicant for compulsory pooling is required to make a well proposal to and notify only those interest owners of record at the time of filing the application for compulsory pooling. *See* Order No. R-10672-A De Novo; Case No. 11510, *Application of Branko, Inc., et al. To Reopen Case No. 10656.*

On October 28, 2008, late in the day, Cimarex filed two competing compulsory pooling applications for the same lands.[2] The Cimarex applications cannot be heard before December 4, 2009.

Cimarex has not made well proposals for these units. There is believed to be no dispute over well costs, geology, operator experience or competence, or the applicable risk penalties in these matters.

Applicable Division Precedent

Good Faith Negotiations.

Cimarex has made no effort to comply with the requirement that an applicant for compulsory pooling first make a good faith effort to obtain the voluntary participation of other interest owners.

> *"Whenever the operator of any oil or gas well shall dedicate lands comprising a standard spacing or proration unit to an oil or gas well, it shall be the obligation of the operator, if two or more separately owned tracts of land are embraced within the spacing or proration unit...to obtain voluntary agreements pooling said lands or interest or an order of the division pooling said lands."* NMSA 1978 §70-2-18 (emphasis added).

Applying this statute, the Oil Conservation Commission has said:

> *"It has long been the practice of the Commission to require parties to show good faith and diligence in proposing a well to other interest owners in the unit as a pre-requisite of a compulsory pooling order. See Morris, Richard, Compulsory Pooling of Oil and Gas Interests in New Mexico, 3 Nat Res. J. 316 (1963). The Oil and Gas Act may require such efforts. See NMSA 1978 §70-2-18(A)."* Order No. R-11663-C; Case No. 12635/12705, *Application of McElvain Oil & Gas Properties, Inc. for Compulsory Pooling, Rio Arriba County, New Mexico.*

[2] Case Numbers are not yet available.

These circumstances alone warrant the rejection of Cimarex's untimely efforts to thwart COG's pooling applications.

Compulsory Pooling Factors.

Firmly established Division precedent sets forth the applicable criteria for the determination of competing applications for compulsory pooling.

The most important consideration is geologic evidence as it relates to well location.

Further, good faith negotiation prior to pooling is a factor. Majority ownership and working interest control can be a "controlling factor" or a "critical factor" in such cases. (Findings 23, 24 and 25, Order No. R-10731-B, Case Nos. 11666 and 11677, *de novo*, *Application of KCS Medallion Resources, Inc. and Yates Petroleum Corporation for Compulsory Pooling;* Copy attached.) Geology, well location, well costs and the ability to operate are not at issue in this case and are consequently not significant factors in this case.

In the absence of other controlling factors, the party who originally developed the prospect, first developed the geologic data and initially sought to obtain voluntary agreement should be designated operator.

(Finding 21, Order No. R-10922, Case Nos. 11830 and 11833, *Application of Mewbourne Oil Company and Devon Energy Production Company for Compulsory Pooling*; Copy attached.)

Here, diligence and timeliness is determinative. As it first acquired its interests, first developed the prospect and geology, negotiated surface locations and damages, was first to make the well proposals, and first obtained regulatory approvals from the BLM and NMOCD, COG should be designated the operator of the proposed well and of the Unit.

For these reasons, COG is entitled to have its compulsory pooling and non-standard unit applications approved by the Division.

Respectfully submitted,

J. Scott Hall

Montgomery and Andrews
325 Paseo de Peralta
Santa Fe, NM 87501
Telephone No. (505) 982-3873
Fax No. (505) 982-4289

Attorneys for COG Operating, LLC

JSH/ww

Certificate of Service by Hand Delivery

James Bruce, Esq.
Attorney for Cimarex Energy Corporation

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

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

DE NOVO
CASE NO. 11666
CASE NO. 11677
Order No. R-10731-B

APPLICATION OF KCS MEDALLION RESOURCES, INC. (FORMERLY INTERCOAST OIL AND GAS COMPANY) FOR COMPULSORY POOLING AND UNORTHODOX GAS WELL LOCATION, EDDY COUNTY, NEW MEXICO.

APPLICATION OF YATES PETROLEUM CORPORATION FOR COMPULSORY POOLING AND AN UNORTHODOX GAS WELL LOCATION, EDDY COUNTY, NEW MEXICO.

ORDER OF THE COMMISSION

BY THE COMMISSION:

This cause came on for hearing at 9:00 a.m. on February 13, 1997, at Santa Fe, New Mexico, before the Oil Conservation Commission, hereinafter referred to as the "Commission."

NOW, on this 28th day of February, 1997, the Commission, a quorum being present, having considered the testimony, the record, and being fully advised in the premises,

FINDS THAT:

(1) Due public notice having been given as required by law, the Commission has jurisdiction of this cause and the subject matter thereof.

(2) Case Nos. 11666 and 11677 were consolidated at the time of the hearing for the purpose of testimony, and, inasmuch as approval of one application would necessarily require denial of the other, one order should be entered for both cases.

(3) The applicant in Case No. 11666, KCS Medallion Resources, Inc. ("Medallion") formerly known as InterCoast Oil and Gas Company, seeks an order pooling all mineral interests from the surface to the base of the Morrow formation underlying the E/2 of Section 20, Township 20 South, Range 28 East, NMPM, Eddy County, New Mexico, thereby forming a standard 320-acre gas spacing and proration unit for any and all formations and/or pools spaced on 320 acres within said vertical extent, which presently includes but is not necessarily limited to the Burton Flat-Morrow Gas Pool and the Undesignated West Burton Flat-Atoka Gas Pool. Said unit is to be dedicated to the applicant's proposed State of New Mexico "20" Well No. 1 to be drilled at an unorthodox gas well location 990 feet from the North and East lines (Unit A) of Section 20.

(4) The applicant in Case No. 11677, Yates Petroleum Corporation ("Yates"), seeks an order pooling all mineral interests from the surface to the base of the Morrow formation underlying the E/2 of Section 20, Township 20 South, Range 28 East, NMPM, Eddy County, New Mexico, thereby forming a standard 320-acre gas spacing and proration unit for any and all formations and/or pools spaced on 320 acres within said vertical extent, which presently includes but is not necessarily limited to the Burton Flat-Morrow Gas Pool and the Undesignated West Burton Flat-Atoka Gas Pool. Said unit is to be dedicated to the applicant's proposed Stonewall "AQK" State Com Well No. 1 to be drilled at an unorthodox gas well location 990 feet from the North and East lines (Unit A) of Section 20.

(5) The subject wells and proration unit are located within the Burton Flat-Morrow Gas Pool and within one mile of the West Burton Flat-Atoka Gas Pool, both of which are currently governed by Rule No. 104.C. of the Division Rules and Regulations which require standard 320-acre gas spacing and proration units with wells to be located no closer than 1650 feet from the end boundary nor closer than 660 feet from the side boundary of the proration unit nor closer than 330 feet from any quarter-quarter section line or subdivision inner boundary.

(6) Both Yates and Medallion have the right to drill within the proposed spacing unit and both seek to be named operator of their respective wells and the subject proration unit.

(7) Yates and Medallion have conducted negotiations prior to the hearing but have been unable to reach a voluntary agreement as to which company will drill and operate the well within the spacing unit.

(8) According to evidence and testimony presented by both parties, the primary objective within the wellbore is the Morrow formation with other formations comprising secondary objectives.

(9) Both Yates and Medallion are in agreement that the well which will ultimately develop the subject proration unit should be located at the unorthodox gas well location requested by both parties. In support of this request, both parties presented geologic evidence and testimony at the Examiner hearing which indicates that a well at the proposed unorthodox location should penetrate the Upper and Lower Morrow sand intervals in an area of greater net sand thickness than a well drilled at a standard gas well location thereon, thereby increasing the likelihood of obtaining commercial gas production. Since both parties agreed on the proposed location, prospect geology, as it relates to the proposed well location, should not be a factor in deciding this case.

(10) Oxy U.S.A. Inc., the affected offset operator to the north of the proposed location, did not appear at the hearing in opposition or otherwise object to the proposed unorthodox gas well location. No other offset operator and or interest owner appeared at the hearing in opposition to the proposed unorthodox gas well location.

(11) Approval of the proposed unorthodox gas well location will afford the operator within the E/2 of Section 20 the opportunity to produce its just and equitable share of the gas in the Burton Flat-Morrow Gas Pool, prevent the economic loss caused by the drilling of unnecessary wells, avoid the augmentation of risk arising from the drilling of an excessive number of wells and otherwise prevent waste and protect correlative rights.

(12) Both Yates and Medallion submitted AFE's for the drilling of their respective wells within the subject spacing unit. The AFE's are not substantially different and should not be a factor in deciding these cases.

(13) The overhead rates proposed by Yates and Medallion are not substantially different and also should not be a factor in deciding these cases.

(14) Both parties proposed that a risk penalty of 200 percent be assessed against those interest owners who do not participate in the drilling of a well within the subject spacing unit.

(15) A brief description of the chronology of events leading up to the hearing in these cases is summarized as follows:

By letter dated August 30, 1996, Medallion sought a farmout from Yates in Section 20 in order to drill an 11,250 foot Morrow test at a location 990 feet from the North and East lines (Unit A). The proposal did not specify which spacing unit will be utilized;

September 17, 1996--By phone conversation Yates informed Medallion of its desire not to farmout the subject acreage;

September 26, 1996--Medallion filed compulsory pooling application seeking a N/2 spacing unit in Section 20 for a well to be drilled in Unit A. Yates received notice of Medallion's compulsory pooling application on September 30, 1996. A hearing was set for October 17, 1996;

By letter dated October 1, 1996, complete with operating agreement and AFE, Medallion formally proposed the drilling of its well in Unit A of Section 20. Yates received Medallion's letter October 9, 1996. Medallion's hearing was postponed until November 7, 1996, to allow Yates the opportunity to review the proposal;

October 24, 1996--Yates informed Medallion that it preferred a different well location in the N/2 of Section 20;

By letter dated October 29, 1996, complete with operating agreement and AFE, Yates proposed the drilling of the Stonewall "DD" State Com Well No. 3 at a location 990 feet from the North and West lines (Unit D) of Section 20 to the interest owners in the Stonewall Unit. The proposed spacing unit was the N/2. By letter dated October 31, 1996, Yates made the same proposal to Medallion;

November 7, 1996--Yates and Medallion met in Artesia to discuss development of Section 20. Each company insisted on drilling its respective well location. Both companies agreed that developing Section 20 with stand-up E/2 and W/2 spacing units would allow both wells to be drilled and agreed to pursue management approval of this option;

By letter dated November 11, 1996, Medallion formally proposed to drill a well within Unit A (990 feet from the North and East lines) within a stand-up proration unit comprising the E/2 of Section 20;

November 12, 1996--Medallion filed a compulsory pooling application for proposed E/2 spacing unit;

November 13, 1996--By phone conversation, Yates informed Medallion that it agrees to develop Section 20 with stand up proration units but proposed that it be allowed to drill both wells. Medallion responded that it desires to drill and operate the well in the E/2;

By letter dated November 14, 1996, Yates formally proposed the drilling of the Stonewall "DD" State Com Well No. 3 on a W/2 spacing unit to the "Stonewall Unit" interest owners;

By letter dated November 22, 1996, Yates formally proposed to Medallion the drilling of the Stonewall "AQK" State Com Well No. 1 at a location 990 feet from the North and East lines (Unit A) of Section 20. The proposed spacing unit is the E/2;

November 26, 1996--Yates filed an application for the compulsory pooling of the E/2 of Section 20;

December 2-13, 1996--Ongoing discussions between the parties.

December 19, 1996--Competing pooling applications of Yates in Case 11677 and Medallion in Case 11666 came up for hearing before Division Examiner David R. Catanach.

January 13, 1997--The Division entered Order No. R-10731 granting the application of Medallion and denying the companion application of Yates. Order No. R-10731 pooled the E/2 of Section 20, Township 20 South, Range 28 East, NMPM, Eddy County, New Mexico, designated Medallion operator of the well, and provided that the well shall be commenced on or before April 15, 1997.

January 21, 1997--Yates filed an Application for Hearing De Novo. At that time the next Commission hearing was scheduled for February 13, 1997.

January 21, 1997--Medallion had obtained an extension of their farmout.

January 24, 1997--Yates requested a Stay of Division Order No. R-10709 to enable it to have the Commission review these competing pooling applications in a de novo hearing prior to Medallion commencing to drill the well. Medallion objected to the stay.

January 31, 1997--The Division Director denied the Stay because, among other things, granting the "Stay" would delay the drilling of the well which would risk the loss of valuable farmout rights. See Order No. R-10731-A.

February 8, 1997--Medallion moved a drilling rig on location and commenced drilling State of New Mexico "20" Well No. 1.

(16) Land testimony presented by both parties in this case, which is generally in agreement, indicates that:

a) 100 percent of the SE/4 and 5 percent of the NE/4 of Section 20 are subject to an existing unit agreement, the Stonewall Unit Agreement, in which Yates is the operator;

b) Yates Petroleum Corporation, Yates Drilling Company, Abo Petroleum Corporation and Myco Industries, Inc., (the "Yates Group") collectively own 37.7 percent of the proposed spacing unit. In addition, Yates testified that by virtue of the Stonewall Unit Agreement, it controls an additional 14.765 percent of the proposed spacing unit;

c) the 95 percent working interest in the NE/4 of Section 20 which is not subject to the Stonewall Unit Agreement is owned approximately as follows:

Kerr-McGee Corporation----------48 percent
Diamond Head Properties, L.P.------47 percent

d) by virtue of a farmout agreement with Kerr-McGee Corporation, Medallion will "earn" approximately 24.101 percent of the proposed spacing unit. Under the terms of the farmout agreement, a well must be commenced by February 17, 1997, or the farmout agreement will expire. Land testimony by Medallion further indicates that the subject farmout agreement will remain in effect even if Yates is named operator of the well and unit, provided however, such well must be commenced by the drilling deadline described above.

(17) Diamond Head Properties, L.P. submitted correspondence to the Division in these cases on December 12, 1996, in which it stated that it will remain neutral as to its preference of operator and that it will most likely join in the drilling of the well in the E/2 of Section 20 regardless of who operates.

(18) Interest ownership within the spacing unit is summarized as follows:

Yates Petroleum Corporation	19.635%
Yates Drilling Company	7.742%
Abo Petroleum Corporation	2.581%
Myco Industries, Inc.	7.742%
Stonewall Unit Owners (Other than the Yates Group)	14.765%
Medallion	24.101%
Diamond Head Properties, L.P.	23.416%

(19) Yates and the Yates Group own approximately 19.635 percent and 37.7 percent, respectively, within the spacing unit. Medallion, by virtue of the farmout agreement with Kerr McGee, will earn 24.101 percent of the spacing unit upon the drilling of a well in the E/2 of Section 20.

(20) Yates testified that if named operator of the subject spacing unit, it will take over the position and contract obligations of Medallion as operator and continue drilling the State of New Mexico "20" Well No. 1 without interruption.

(21) Yates contends it should be allowed to operate the State of New Mexico "20" Well No. 1 and operate the E/2 of Section 20 for the following reasons:

a) collectively, the Yates Group owns a larger percentage of the spacing unit than Medallion--37.7 percent to 24.101 percent;

b) Yates has the support of several of the interest owners in the Stonewall Unit, while Medallion has been unable to secure the support of any of these interest owners;

c) Yates has drilled and operated twenty-one wells in the Stonewall Unit since 1973;

d) the Stonewall Unit area is very complex and as operator, Yates is the most familiar with it and best able to deal with the land, accounting and distribution of production proceeds.

(22) Medallion contends that it is an experienced operator and due to the fact that it took the initiative in developing the prospect and was the moving force in getting the well drilled, it should be allowed to operate its State of New Mexico "20" Well No. 1 and operate the E/2 of Section 20.

(23) An evaluation of the evidence, testimony and information obtained from Division records indicates that:

a) within the Stonewall Unit area, which encompasses all or portions of Sections 19, 20, 29 and 30, Yates has drilled five wells to a depth sufficient to produce the Morrow formation. Most of the drilling and production from the Burton Flat-Morrow Gas Pool within the Stonewall Unit area occurred during the period from approximately 1973 to 1987, and, with the exception of the Stonewall "EP" State Well No. 1, located in Unit N of Section 19, which is currently an active producing well in the Morrow formation, all of the other wells have been plugged and abandoned;

b) even though Yates has had the opportunity to develop the N/2 or E/2 of Section 20 in the Burton Flat-Morrow Gas Pool since 1973, it apparently chose not to do so until such time as Medallion, on September 3, 1996, sought a farmout of its acreage in Section 20;

c) as a result of the agreement reached with Medallion to develop Section 20 with stand-up proration units, Yates will have the opportunity to develop the W/2 of this section by drilling its Stonewall "DD" State Com Well No. 3 in Unit D;

d) there is a fairly significant difference in interest ownership in the E/2 of Section 20 between the "Yates Group" and Medallion with Medallion controlling 24.1% by virtue of its Kerr-McGee farmout and Yates controlling 37.7% by virtue of its relationship with the "Yates Group." The uncommitted acreage as to operational preference is owned by Diamond Head Properties, L.P. which comprises 23.4% of the proration unit and should be credited to the account of Medallion for purposes of deciding the party controlling majority interest. It was because of the efforts of Medallion that this acreage will be participating in the well that is being drilled. Yates on the other hand should be credited with the Stonewall Unit's 14.8% of the spacing unit because they are operators of that unit and have the support of the majority of interest owners in the unit. Incorporating these two credits the breakdown of proration unit control is as follows: Medallion 47.5% and Yates 52.5%;

e) the controlling percentage under a 160 or 40 acre proration unit would be different from the controlling percentage under the subject 320 acre unit. If the State of New Mexico "20" Well No. 1 was completed from the Delaware, Bone Spring or Strawn formation the resultant proration unit would probably be 40 or 160 acres depending upon whether it is an oil or Permian gas completion. Paying interest for these completions would be different than paying interest under the 320 acre proration unit and would reflect acreage ownership under the assigned 40 or 160 acres. In analyzing which parties have the most at stake in drilling the well, additional weight must be given to secondary objectives and the resultant ownership under those prospective proration units. The breakdown of interest under 40 or 160 acre proration units under the currently drilling State of New Mexico "20" Well No. 1 is as follows: Yates (Stonewall Unit) 5% and Medallion 95%;

f) the most important consideration in awarding operations to competing interest owners is geologic evidence as it relates to well location and recovery of oil and gas and associated risk. Since Yates and Medallion agree on geology and location, this is not a factor;

g) good faith negotiation prior to force pooling is a factor. If the force pooling party does not negotiate in good faith, the application is denied and the applicant is instructed to try to negotiate an agreement prior to refiling the force pooling application. Both Yates and Medallion conducted adequate discussions prior to filing competing force pooling applications, so this is not a factor in awarding operations;

h) both parties stipulated that 200% was the appropriate risk factor for non-consulting working interest owners pooled under this order so this is not a factor in awarding operations;

i) both parties are capable of operating the property prudently so this is not a factor in awarding operations;

j) differences in AFE's (well cost estimates) and other operational criteria are not significant factors in awarding operations and have only minor significance in evaluating an operator's ability to prudently operate the property.

(24) In the absence of compelling factors such as geologic and prospect differences, ability to operate prudently, or any reason why one operator would economically recover more oil or gas by virtue of being awarded operations than the other, "working interest control," as defined and modified by findings 23 (d), and (e) should be the controlling factor in awarding operations.

(25) Since the adjusted "working interest control" under the proration unit was relatively even, Medallion 47.5% to Yates 52.5%, the fact that Medallion would have 95% of the "working interest control" over completions in all formations spaced on 40 or 160 acres should be the critical factor in deciding who operates the State of New Mexico "20" Well No. 1 and the proposed spacing unit.

(26) Medallion should be designated operator of the State of New Mexico "20" Well No. 1 and the proposed spacing unit.

(27) The application of Yates Petroleum Corporation in this case should be denied.

(28) To avoid the drilling of unnecessary wells, to protect correlative rights, to avoid waste, and to afford to the owner of each interest in said unit the opportunity to recover or receive without unnecessary expense his just and fair share of the production in any pool completion resulting from this order, the application of Medallion Resources, Inc. should be approved by pooling all mineral interests, whatever they may be, within the E/2 of Section 20.

(29) Any non-consenting working interest owner should be afforded the opportunity to pay his share of estimated well costs to the operator in lieu of paying his share of reasonable well costs out of production.

(30) Any non-consenting working interest owner who does not pay his share of estimated well costs should have withheld from production his share of the reasonable well costs plus an additional 200 percent thereof as a reasonable charge for the risk involved in the drilling of the well.

(31) Any non-consenting working interest owner should be afforded the opportunity to object to the actual well costs but actual well costs should be adopted as the reasonable well costs in the absence of such objection.

(32) Following determination of reasonable well costs, any non-consenting working interest owner who has paid his share of estimated costs should pay to the operator any amount that reasonable well costs exceed estimated well costs and should receive from the operator any amount that paid estimated well costs exceed reasonable well costs.

(33) $5819.00 per month while drilling and $564.00 per month while producing should be fixed as reasonable charges for supervision (combined fixed rates); the operator should be authorized to withhold from production the proportionate share of such supervision charges attributable to each non-consenting working interest, and in addition thereto, the operator should be authorized to withhold from production the proportionate share of actual expenditures required for operating the subject well, not in excess of what are reasonable, attributable to each non-consenting working interest.

(34) All proceeds from production from the subject well which are not disbursed for any reason should be placed in escrow to be paid to the true owner thereof upon demand and proof of ownership.

(35) Upon the failure of the operator of said pooled unit to commence the drilling of the well to which said unit is dedicated on or before April 15, 1997, the order pooling said unit should become null and void and of no effect whatsoever.

(36) Should all the parties to this forced pooling order reach voluntary agreement subsequent to entry of this order, the portion of the order concerning the compulsory pooling of the subject proration unit shall thereafter be of no further effect.

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

IT IS THEREFORE ORDERED THAT:

(1) The application of Yates Petroleum Corporation in Case No. 11677 for an order pooling all mineral interests from the surface to the base of the Morrow formation underlying the E/2 of Section 20, Township 20 South, Range 28 East, NMPM, Eddy County, New Mexico, thereby forming a standard 320-acre gas spacing and proration unit for any and all formations and/or pools spaced on 320 acres within said vertical extent, which presently includes but is not necessarily limited to the Burton Flat-Morrow Gas Pool and the Undesignated West Burton Flat-Atoka Gas Pool, said unit to be dedicated to the applicant's proposed Stonewall "AQK" State Com Well No. 1 to be drilled at an unorthodox gas well location 990 feet from the North and East lines (Unit A) of Section 20, is hereby denied.

(2) The application of Medallion in Case No. 11666 for an order pooling all mineral interests from the surface to the base of the Morrow formation underlying the E/2 of Section 20, Township 20 South, Range 28 East, NMPM, Eddy County, New Mexico, thereby forming a standard 320-acre gas spacing and proration unit for any and all formations and/or pools spaced on 320 acres within said vertical extent, which presently includes but is not necessarily limited to the Burton Flat-Morrow Gas Pool and the Undesignated West Burton Flat-Atoka Gas Pool, said unit to be dedicated to the applicant's proposed Medallion State of New Mexico "20" Well No. 1 to be drilled at an unorthodox gas well location 990 feet from the North and East lines (Unit A) of Section 20, is hereby approved.

PROVIDED HOWEVER THAT, the operator of said unit shall commence the drilling of said well on or before the 15th day of April, 1997, and shall thereafter continue the drilling of said well with due diligence to a depth sufficient to test the Morrow formation.

PROVIDED FURTHER THAT, in the event said operator does not commence the drilling of said well on or before the 15th day of April, 1997, Ordering Paragraph No. (1) of this order shall be null and void and of no effect whatsoever, unless said operator obtains a time extension from the Division Director for good cause shown.

PROVIDED FURTHER THAT, should said well not be drilled to completion, or abandonment, within 120 days after commencement thereof, said operator shall appear before the Division Director and show cause why Ordering Paragraph No. (1) of this order should not be rescinded.

(2) KCS Medallion Resources, Inc. is hereby designated the operator of the State of New Mexico "20" Well No. 1 and subject proration unit.

(3) Within 30 days from the date the schedule of estimated well costs is furnished to him, any non-consenting working interest owner shall have the right to pay his share of estimated well costs to the operator in lieu of paying his share of reasonable well costs out of production, and any such owner who pays his share of estimated well costs as provided above shall remain liable for operating costs but shall not be liable for risk charges. Since the State of New Mexico "20" Well No. 1 is currently drilling the election time to participate is extended to March 7, 1997

(4) The operator shall furnish the Division and each known working interest owner an itemized schedule of actual well costs within 90 days following completion of the 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 said schedule, the actual well costs shall be the reasonable well costs; provided however, if there is objection to actual well costs within said 45-day period the Division will determine reasonable well costs after public notice and hearing.

(5) Within 60 days following determination of reasonable well costs, any non-consenting working interest owner who has paid his share of estimated well costs in advance as provided above shall pay to the operator his pro rata share of the amount that reasonable well costs exceed estimated well costs and shall receive from the operator his pro rata share of the amount that estimated well costs exceed reasonable well costs.

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

(A) The pro rata share of reasonable well costs attributable to each non-consenting working interest owner who has not paid his share of estimated well costs by March 7, 1997.

(B) As a charge for the risk involved in the drilling of the well, 200 percent of the pro rata share of reasonable well costs attributable to each non-consenting working interest owner who has not paid his share of estimated well costs by March 7, 1997.

(7) The operator shall distribute said costs and charges withheld from production to the parties who advanced the well costs.

(8) $5819.00 per month while drilling and $564.00 per month while producing are hereby fixed as reasonable charges for supervision (combined fixed rates); the operator is hereby authorized to withhold from production the proportionate share of such supervision charges attributable to each non-consenting working interest, and in addition thereto, the operator is hereby authorized to withhold from production the proportionate share of actual expenditures required for operating such well, not in excess of what are reasonable, attributable to each non-consenting working interest.

(9) 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 the terms of this order.

(10) Any well costs or charges which are to be paid out of production shall be withheld only from the working interest's share of production, and no costs or charges shall be withheld from production attributable to royalty interests.

(11) All proceeds from production from the subject well which are not disbursed for any reason shall immediately be placed in escrow in Eddy 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 said escrow agent within 30 days from the date of first deposit with said escrow agent.

(12) Should all the parties to this forced pooling order reach voluntary agreement subsequent to entry of this order, the portion of the order concerning the compulsory pooling of the subject proration unit shall thereafter be of no further effect.

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

(14) Jurisdiction is hereby retained for the entry of such further orders as the Commission may deem necessary.

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

STATE OF NEW MEXICO
OIL CONSERVATION COMMISSION

JAMI BAILEY, Member

WILLIAM W. WEISS, Member

WILLIAM J. LEMAY, Chairman

S E A L

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. 11830
CASE NO. 11833
Order No. R-10922

APPLICATION OF MEWBOURNE OIL COMPANY FOR COMPULSORY POOLING, EDDY COUNTY, NEW MEXICO.

APPLICATION OF DEVON ENERGY CORPORATION (NEVADA) FOR COMPULSORY POOLING, EDDY COUNTY, NEW MEXICO.

ORDER OF THE DIVISION

BY THE DIVISION:

This cause came on for hearing at 8:15 a.m. on October 9, 1997, at Santa Fe, New Mexico, before Examiner David R. Catanach.

NOW, on this 24th day of November, 1997, the Division Director, having considered the testimony, the record, and the recommendations of the Examiner, and being fully advised in the premises,

FINDS THAT:

(1) Due public notice having been given as required by law, the Division has jurisdiction of this cause and the subject matter thereof.

(2) Division Case Nos. 11830 and 11833 were consolidated at the time of the hearing for the purpose of testimony, and, inasmuch as approval of one application would necessarily require denial of the other, one order should be entered for both cases.

(3) The applicant in Case No. 11830, Mewbourne Oil Company (Mewbourne), seeks an order pooling all mineral interests from the surface to the base of the Morrow formation underlying the S/2 of Section 15, Township 21 South, Range 26 East, NMPM, Eddy County, New Mexico, and in the following manner:

the S/2 thereby forming a standard 320-acre gas spacing and proration unit for any and all formations and/or pools spaced on 320 acres within said vertical extent, which presently includes but is not necessarily limited to the Undesignated Avalon-Morrow Gas Pool, Undesignated Avalon-Strawn Gas Pool, Undesignated Avalon-Atoka Gas Pool and the Undesignated Avalon-Upper Pennsylvanian Gas Pool;

the SW/4 thereby forming a standard 160-acre spacing and proration unit for any and all formations and/or pools spaced on 160 acres within said vertical extent;

the E/2 SW/4 thereby forming a standard 80-acre oil spacing and proration unit for any and all formations and/or pools spaced on 80 acres within said vertical extent; and,

the NE/4 SW/4 thereby forming a standard 40-acre oil spacing and proration unit for any and all formations and/or pools spaced on 40 acres within said vertical extent.

Said units are to be dedicated to its proposed Carlsbad "15" Federal Com Well No. 1 to be drilled at a standard location 1980 feet from the South line and 1850 feet from the West line (Unit K) of Section 15.

(4) The applicant in Case No. 11833, Devon Energy Corporation (Nevada), (Devon), seeks an order pooling all mineral interests from the surface to the base of the Morrow formation underlying the S/2 of Section 15, Township 21 South, Range 26 East, NMPM, Eddy County, New Mexico, and in the following manner:

the S/2 thereby forming a standard 320-acre gas spacing and proration unit for any and all formations and/or pools spaced on 320 acres within said vertical extent, which presently includes but is not necessarily limited to the Undesignated Avalon-Morrow Gas Pool, Undesignated Avalon-Strawn Gas Pool, Undesignated Avalon-Atoka Gas Pool and the Undesignated Avalon-Upper Pennsylvanian Gas Pool;

the SW/4 thereby forming a standard 160-acre spacing and proration unit for any and all formations and/or pools spaced on 160 acres within said vertical extent.

Said units are to be dedicated to its proposed Carlsbad 15 "K" Federal Com Well No. 1 to be drilled at a standard location 1980 feet from the South line and 1850 feet from the West line (Unit K) of Section 15.

(5) Subsequent to the hearing it was determined that neither Mewbourne's proposed Carlsbad "15" Federal Com Well No. 1 nor the proposed 80-acre spacing and proration unit comprising the E/2 SW/4 of Section 15 are located within one mile of an existing pool spaced on 80 acres.

(6) At the hearing it was also determined that Mewbourne does not own any interest in the NE/4 SW/4 of Section 15, and thus is unable to pool this tract to form a standard 40-acre oil spacing and proration unit.

(7) The portion of Mewbourne's application seeking the compulsory pooling of the E/2 SW/4 and NE/4 SW/4 of Section 15, thereby forming standard 80-acre and 40-acre spacing and proration units, respectively, should be dismissed.

(8) The proposed wells and 320-acre proration units are located within one mile of numerous gas pools, namely the Avalon-Morrow Gas Pool, Avalon-Atoka Gas Pool, Avalon-Strawn Gas Pool and Avalon-Upper Pennsylvanian Gas Pool. All of the subject pools are currently governed by Rule No. 104.C. of the Division General Rules and Regulations which require standard 320-acre gas spacing and proration units with wells to be located no closer than 1650 feet from the end boundary nor closer than 660 feet from the side boundary of the proration unit nor closer than 330 feet from any quarter-quarter section line or subdivision inner boundary.

(9) Both Mewbourne and Devon have the right to drill within the proposed spacing units and both seek to be named operator of their respective wells and the subject proration units.

(10) Mewbourne and Devon have conducted negotiations prior to the hearing but have been unable to reach a voluntary agreement as to which company will drill and operate the well within the spacing units.

(11) According to evidence and testimony presented by both parties, the primary objective within the wellbore is the Strawn formation. Secondary objectives include the Morrow, Atoka and Upper Pennsylvanian intervals.

(12) Both Mewbourne and Devon are in agreement that the well which will ultimately develop the subject proration units should be located at the standard gas well location requested by both parties.

(13) Both Mewbourne and Devon submitted AFE's for the drilling of their respective wells within the subject spacing units. The AFE's are not substantially different.

(14) Both Mewbourne and Devon proposed overhead rates of $6000.00 per month while drilling and $600.00 per month while producing.

(15) Both parties proposed that a risk penalty of 200 percent be assessed against those interest owners who do not participate in the drilling of a well within the subject spacing units.

(16) The current ownership of the S/2 of Section 15 is summarized as follows:

Company	Acres	Description	% Working Interest
Mewbourne Oil Company	160.53	E/2 SE/4, SW/4 SE/4, SE/4 SW/4	50.08%
Devon Energy Corporation	160.00	W/2 SW/4, NE/4 SW/4, NW/4 SE/4	49.92%

(17) A brief description of the chronology of events leading up to the hearing in these cases is summarized as follows:

November, 1996--Mewbourne begins a geologic study of this general area. Mewbourne currently owns no interest in Township 21 South, Range 26 East;

February, 1997--Mewbourne acquires Hallwood Petroleum Corporation's interest within the NW/4 of Section 21, Township 21 South, Range 26 East. Mewbourne's intent in acquiring this acreage is to utilize an existing well on this tract, being the Ocotillo Hills Well No. 2, to test the Strawn formation;

By letter dated March 10, 1997, Mewbourne offers to purchase Devon's interest in Sections 10, 15, 16, 20 and 21;

March 13, 1997--Mewbourne initiates meeting with Devon and proposes a joint venture to develop the Strawn formation within this area;

April 23, 1997--Devon meets with representatives of Carlow Corporation who own interest in the S/2 of Section 15. Devon discusses Strawn activity in the area and proposes a potential joint venture;

May 6, 1997--Devon meets with representatives of Carlow Corporation and proposes the formation of a 640-acre working interest unit in Section 15 which Devon proposes to operate. Carlow Corporation advises that it will evaluate proposal;

June 6, 1997--Mewbourne acquires the interest of Carlow Corporation in the S/2 of Section 15;

June 12, 1997--Mewbourne formally proposes to Devon and seeks its participation in the drilling of an 11,200 foot Morrow well within the S/2 of Section 15 at a tentative location of 1980 feet from the South line and 1650 feet from the West line (Unit K). Alternatively, Mewbourne seeks a farmout or acquisition of Devon's interest within the S/2 of Section 15;

June 16, 1997--By phone conversation, Devon advises Mewbourne that it wishes to operate the proposed well in Section 15;

June 17, 1997--Mewbourne files APD (Application to Drill) with the BLM for its proposed Carlsbad "15" Federal Com Well No. 1. BLM subsequently requests that Mewbourne move its proposed well 200 feet to the east due to topographic considerations;

June 24, 1997--Mewbourne advises Devon of its well location change

June 25, 1997--By phone conversation, Devon informs Mewbourne that it will propose the drilling of a well within the S/2 of Section 15 at the location Mewbourne has staked;

July 3, 1997--Devon agrees with Mewbourne's proposal to drill a well at a location 1980 feet from the South line and 1850 feet from the West line (Unit K) of Section 15. Devon submits its AFE and proposes to Mewbourne that it be allowed to drill and operate the well.
By letter dated July 14, 1997 Mewbourne reiterates its position to Devon that it proposes to drill and operate the Carlsbad "15" Federal Com Well No. 1;

July 24, 1997--Compulsory Pooling application filed by Mewbourne;

July 29, 1997--Compulsory Pooling application filed by Devon;

August-September, 1997--Continuing negotiations between Mewbourne and Devon.

(18) Devon contends that it should be named operator of the proposed well and spacing units inasmuch as Mewbourne has been unwilling to negotiate a voluntary agreement, and has exhibited aggressive and premature behavior in this process by staking the well location (on Devon's lease), filing an APD with the Bureau of Land Management, and filing compulsory pooling proceedings.

(19) Mewbourne contends that due to the fact that it developed the prospect, it should be allowed to drill its Carlsbad "15" Federal Com Well No. 1 and operate the S/2 of Section 15.

(20) The evidence and testimony presented in these cases indicates that:

a) the potential for producing the well in a formation above the Pennsylvanian appears to be minimal. Interest ownership within the spacing units, which heavily favors Devon in a 160-acre and 40-acre scenario, should therefore not be a critical factor in deciding these cases;

b) well location, interest ownership within a 320-acre proration unit, well costs, overhead rates and risk penalty, all being equal or relatively equal, should not be factors in deciding these cases;

c) although Mewbourne has acted somewhat aggressive in staking the well location and obtaining the permits necessary to drill a well within the S/2 of Section 15, it appears that a voluntary agreement for the drilling of a well within the S/2 of Section 15 would not likely have been reached due to the fact that both Mewbourne and Devon have remained, from the date of the first well proposal by Mewbourne (June 12, 1997), intent on being named operator of the well and units;

d) negotiations between Mewbourne and Devon have been ongoing from March, 1997 through September, 1997;

e) the potential for Strawn development in this area increased in July, 1994, at which time Yates Petroleum Corporation recompleted its Lake Shore "XH" Federal Well No. 1, located in Section 11, Township 21 South, Range 26 East, from the Atoka/Morrow interval to the Strawn formation;

f) although Devon had the opportunity to develop Section 15 in the Strawn formation since 1994, it apparently chose not to do so until such time as Mewbourne sought a farmout or acquisition of its acreage for that purpose;

(21) In the absence of other compelling factors, the operatorship of the S/2 of Section 15 should be awarded to the operator who originally developed the Strawn prospect, developed the geologic data necessary to determine the optimum well location, and initially sought to obtain farmout or voluntary agreement to drill its well.

(22) Mewbourne Oil Company should be designated operator of its proposed well and the proposed spacing units.

(23) The application of Devon Energy Corporation in this case should be denied.

(24) To avoid the drilling of unnecessary wells, to protect correlative rights, to avoid waste, and to afford to the owner of each interest in said units the opportunity to recover or receive without unnecessary expense his just and fair share of the production in any pool completion resulting from this order, the application of Mewbourne Oil Company should be approved by pooling all mineral interests, whatever they may be, within the S/2 and SW/4 of Section 15.

(25) Any non-consenting working interest owner should be afforded the opportunity to pay his share of estimated well costs to the operator in lieu of paying his share of reasonable well costs out of production.

(26) Any non-consenting working interest owner who does not pay his share of estimated well costs should have withheld from production his share of the reasonable well costs plus an additional 200 percent thereof as a reasonable charge for the risk involved in the drilling of the well.

(27) Any non-consenting working interest owner should be afforded the opportunity to object to the actual well costs but actual well costs should be adopted as the reasonable well costs in the absence of such objection.

(28) Following determination of reasonable well costs, any non-consenting working interest owner who has paid his share of estimated costs should pay to the operator any amount that reasonable well costs exceed estimated well costs and should receive from the operator any amount that paid estimated well costs exceed reasonable well costs.

(29) $6000.00 per month while drilling and $600.00 per month while producing should be fixed as reasonable charges for supervision (combined fixed rates); the operator should be authorized to withhold from production the proportionate share of such supervision charges attributable to each non-consenting working interest, and in addition thereto, the operator should be authorized to withhold from production the proportionate share of actual expenditures required for operating the subject well, not in excess of what are reasonable, attributable to each non-consenting working interest.

(30) All proceeds from production from the subject well which are not disbursed for any reason should be placed in escrow to be paid to the true owner thereof upon demand and proof of ownership.

(31) Upon the failure of the operator of said pooled units to commence the drilling of the well to which said units are dedicated on or before March 1, 1998, the order pooling said units should become null and void and of no effect whatsoever.

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

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

IT IS THEREFORE ORDERED THAT:

(1) The application of Devon Energy Corporation (Nevada) in Case No. 11833 for an order pooling all mineral interests from the surface to the base of the Morrow formation underlying the S/2 and SW/4 of Section 15, Township 21 South, Range 26 East, NMPM, Eddy County, New Mexico, thereby forming standard 320-acre and 160-acre spacing and proration units, said units to be dedicated to its proposed Carlsbad 15 "K" Federal Com Well No. 1 to be drilled at a standard location 1980 feet from the South line and 1850 feet from the West line (Unit K) of Section 15, is hereby denied.

(2) The application of Mewbourne Oil Company in Case No. 11830 for an order pooling all mineral interests from the surface to the base of the Morrow formation underlying the S/2 of Section 15, Township 21 South, Range 26 East, NMPM, Eddy County, New Mexico, in the following manner is hereby approved:

the S/2 thereby forming a standard 320-acre gas spacing and proration unit for any and all formations and/or pools spaced on 320 acres within said vertical extent, which presently includes but is not necessarily limited to the Undesignated Avalon-Morrow Gas Pool, Undesignated Avalon-Strawn Gas Pool, Undesignated Avalon-Atoka Gas Pool and the Undesignated Avalon-Upper Pennsylvanian Gas Pool; and,

the SW/4 thereby forming a standard 160-acre spacing and proration unit for any and all formations and/or pools spaced on 160 acres within said vertical extent.

Said units shall be dedicated to its Carlsbad "15" Federal Com Well No. 1 to be drilled at a standard location 1980 feet from the South line and 1850 feet from the West line (Unit K) of Section 15.

PROVIDED HOWEVER THAT, the operator of said units shall commence the drilling of said well on or before the 1st day of March, 1998, and shall thereafter continue the drilling of said well with due diligence to a depth sufficient to test the Morrow formation.

PROVIDED FURTHER THAT, in the event said operator does not commence the drilling of said well on or before the 1st day of March, 1998, Ordering Paragraph No. (1) of this order shall be null and void and of no effect whatsoever, unless said operator obtains a time extension from the Division Director for good cause shown.

PROVIDED FURTHER THAT, should said well not be drilled to completion, or abandonment, within 120 days after commencement thereof, said operator shall appear before the Division Director and show cause why Ordering Paragraph No. (2) of this order should not be rescinded.

(3) Mewbourne Oil Company is hereby designated the operator of the Carlsbad "15" Federal Com Well No. 1 and subject proration units.

(4) After the effective date of this order and within 90 days prior to commencing said well, the operator shall furnish the Division and each known working interest owner in the subject units an itemized schedule of estimated well costs.

(5) Within 30 days from the date the schedule of estimated well costs is furnished to him, any non-consenting working interest owner shall have the right to pay his share of estimated well costs to the operator in lieu of paying his share of reasonable well costs out of production, and any such owner who pays his share of estimated well costs as provided above shall remain liable for operating costs but shall not be liable for risk charges.

(6) The operator shall furnish the Division and each known working interest owner an itemized schedule of actual well costs within 90 days following completion of the 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 said schedule, the actual well costs shall be the reasonable well costs; provided however, if there is objection to actual well costs within said 45-day period the Division will determine reasonable well costs after public notice and hearing.

(7) Within 60 days following determination of reasonable well costs, any non-consenting working interest owner who has paid his share of estimated well costs in advance as provided above shall pay to the operator his pro rata share of the amount that reasonable well costs exceed estimated well costs and shall receive from the operator his pro rata share of the amount that estimated well costs exceed reasonable well costs.

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

(A) The pro rata share of reasonable well costs attributable to each non-consenting working interest owner who has not paid his share of estimated well costs within 30 days from the date the schedule of estimated well costs is furnished to him.

(B) As a charge for the risk involved in the drilling of the well, 200 percent of the pro rata share of reasonable well costs attributable to each non-consenting working interest owner who has not paid his share of estimated well costs within 30 days from the date the schedule of estimated well costs is furnished to him.

(9) The operator shall distribute said costs and charges withheld from production to the parties who advanced the well costs.

(10) $6000.00 per month while drilling and $600.00 per month while producing are hereby fixed as reasonable charges for supervision (combined fixed rates); the operator is hereby authorized to withhold from production the proportionate share of such supervision charges attributable to each non-consenting working interest, and in addition thereto, the operator is hereby authorized to withhold from production the proportionate share of actual expenditures required for operating such well, not in excess of what are reasonable, attributable to each non-consenting working interest.

(11) 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 the terms of this order.

(12) Any well costs or charges which are to be paid out of production shall be withheld only from the working interest's share of production, and no costs or charges shall be withheld from production attributable to royalty interests.

(13) All proceeds from production from the subject well which are not disbursed for any reason shall immediately be placed in escrow in Eddy 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 said escrow agent within 30 days from the date of first deposit with said escrow agent.

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

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

(16) The portion of Mewbourne's application seeking the compulsory pooling of the E/2 SW/4 and NE/4 SW/4 of Section 15, thereby forming standard 80-acre and 40-acre spacing and proration units, respectively, is hereby dismissed.

(17) Jurisdiction is hereby 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

WILLIAM J. LEMAY
Director

S E A L