

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

RECEIVED

JAN 8 2004

Oil Conservation Division
CONTINUED AND DISMISSED CASE # 20 S. St. Francis Drive
Santa Fe, NM 87505

REPORTER'S TRANSCRIPT OF PROCEEDINGS

BEFORE: WILLIAM V. JONES, JR., Hearing Examiner

December 18th, 2003

Santa Fe, New Mexico

These matters came on for hearing before the New Mexico Oil Conservation Division, WILLIAM V. JONES, JR., Hearing Examiner, on Thursday, December 18th, 2003, at the New Mexico Energy, Minerals and Natural Resources Department, 1220 South Saint Francis Drive, Room 102, Santa Fe, New Mexico, Steven T. Brenner, Certified Court Reporter No. 7 for the State of New Mexico.

* * *

I N D E X

December 18th, 2003
Continued and Dismissed Cases

PAGE

REPORTER'S CERTIFICATE

4

* * *

1 WHEREUPON, the following proceedings were had at
2 8:15 a.m.:

3 EXAMINER JONES: Okay, we'll call the Examiner
4 Hearing on the December 18th, 2003, docket, Number 41-03,
5 to order and first call the continuances and dismissals.
6 And after done, maybe you can correct me or add any more
7 that you want to dismiss today.

8 So on the first page, Case 13,192 is dismissed;
9 and the second case, Case 13,193, is continued to January
10 8th.

11 MR. BRUCE: Mr. Examiner, I will present it, but
12 then I would ask that it be continued again.

13 EXAMINER JONES: Okay, okay. So we will hear
14 that one. You just told me that. Okay, and then Case
15 13,194 is continued to January the 8th.

16 On the next page, Case 13,185 is continued to
17 January 22nd; and Case 13,1375 is continued to February
18 5th.

19 And on page 3, Case 13,165 is continued to April
20 of 2004; and Case 13,177 is continued to January the 8th of
21 2004.

22 Any other corrections or changes?

23 (Thereupon, these proceedings were concluded at
24 8:16 a.m.)

I hereby certify that the foregoing is
a complete record of the proceedings in
the Examiner hearing of Case No. _____
heard by me on _____
* * *

Oil Conservation Division
STEVEN T. BRENNER, CCR
(505) 989-9317
Examiner

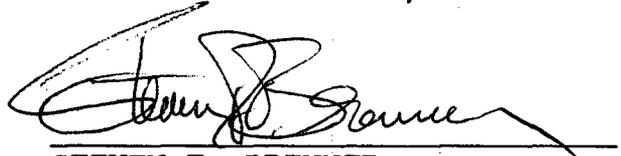
CERTIFICATE OF REPORTER

STATE OF NEW MEXICO)
) ss.
COUNTY OF SANTA FE)

I, Steven T. Brenner, Certified Court Reporter and Notary Public, HEREBY CERTIFY that the foregoing transcript of proceedings before the Oil Conservation Division was reported by me; that I transcribed my notes; and that the foregoing is a true and accurate record of the proceedings.

I FURTHER CERTIFY that I am not a relative or employee of any of the parties or attorneys involved in this matter and that I have no personal interest in the final disposition of this matter.

WITNESS MY HAND AND SEAL December 18th, 2003.



STEVEN T. BRENNER
CCR No. 7

My commission expires: October 16th, 2006

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:)
APPLICATION OF CHI ENERGY, INC., FOR)
COMPULSORY POOLING, EDDY COUNTY,)
NEW MEXICO)

CASE NO. 13,193

ORIGINAL

REPORTER'S TRANSCRIPT OF PROCEEDINGS

EXAMINER HEARING

RECEIVED

BEFORE: WILLIAM V. JONES, JR., Hearing Examiner

JAN 8 2004

December 18th, 2003

Santa Fe, New Mexico

Oil Conservation Division
1220 S. St. Francis Drive
Santa Fe, NM 87505

This matter came on for hearing before the New Mexico Oil Conservation Division, WILLIAM V. JONES, JR., Hearing Examiner, on Thursday, December 18th, 2003, at the New Mexico Energy, Minerals and Natural Resources Department, 1220 South Saint Francis Drive, Room 102, Santa Fe, New Mexico, Steven T. Brenner, Certified Court Reporter No. 7 for the State of New Mexico.

* * *

I N D E X

December 18th, 2003
Examiner Hearing
CASE NO. 13,193

	PAGE
APPEARANCES	3
APPLICANT'S WITNESSES:	
<u>JOHN QUALLS</u> (Landman/Geologist)	
Direct Examination by Mr. Bruce	4
Examination by Examiner Jones	11
REPORTER'S CERTIFICATE	14

* * *

E X H I B I T S

Applicant's	Identified	Admitted
Exhibit 1	5	11
Exhibit 2	6	11
Exhibit 3	6	11
Exhibit 4	8	11
Exhibit 5	8	11
Exhibit 6	(does not exist)	
Exhibit 7	(does not exist)	
Exhibit 8	10	11
Exhibit 9	10	11

* * *

A P P E A R A N C E S

FOR THE DIVISION:

GAIL MacQUESTEN
Deputy General Counsel
Energy, Minerals and Natural Resources Department
1220 South St. Francis Drive
Santa Fe, New Mexico 87505

FOR THE APPLICANT:

JAMES G. BRUCE
Attorney at Law
P.O. Box 1056
Santa Fe, New Mexico 87504

* * *

1 WHEREUPON, the following proceedings were had at
2 8:16 a.m.:

3 EXAMINER JONES: Okay, with that we'll go ahead
4 and call Case 13,193, Application of Chi Energy,
5 Incorporated, for compulsory pooling, Eddy County, New
6 Mexico. Call for appearances.

7 MR. BRUCE: Mr. Examiner, Jim Bruce of Santa Fe
8 representing the Applicant. I have one witness.

9 EXAMINER JONES: Any other appearances? There
10 being none, will the witness please stand to be sworn?

11 (Thereupon, the witness was sworn.)

12 JOHN W. QUALLS,
13 the witness herein, after having been first duly sworn upon
14 his oath, was examined and testified as follows:

15 DIRECT EXAMINATION

16 BY MR. BRUCE:

17 Q. Would you please state your name and city of
18 residence for the record?

19 A. John Qualls, Midland, Texas.

20 Q. Who do you work for?

21 A. Chi Energy, Inc.

22 Q. And what's your job with Chi?

23 A. Landman.

24 Q. Have you previously testified before the Division
25 as a petroleum landman?

1 A. Yes.

2 Q. And were your credentials as an expert accepted
3 as a matter of record?

4 A. Yes.

5 Q. And are you familiar with the land matters
6 involved in this Application?

7 A. Yes.

8 MR. BRUCE: Mr. Examiner, I'd tender Mr. Qualls
9 as an expert petroleum landman.

10 EXAMINER JONES: Mr. Qualls is so qualified.

11 Q. (By Mr. Bruce) Mr. Qualls, what does Chi Energy
12 seek in this case?

13 A. We seek an order pooling the south half of
14 Section 3, 22 South, 26 East, from the surface to the base
15 of the Morrow formation for all pools or formations spaced
16 on 320 acres. We also seek to pool the southwest quarter
17 for 160-acre units and the southwest quarter, southwest
18 quarter for 40-acre units.

19 Q. What is Exhibit 1?

20 A. Exhibit 1 is a land plat outlining the proposed
21 well unit. The well is at an orthodox location 990 from
22 the south and 990 from the west.

23 Q. What type of interests are you seeking to pool in
24 this case?

25 A. We seek to pool a number of unleased mineral

1 owners.

2 Q. Referring to Exhibit 2, could you describe
3 briefly the problem in obtaining leases in the south half
4 of Section 3?

5 A. Exhibit 2 is a plat of the south half of Section
6 3. Most of the acreage is residential subdivisions. There
7 are approximately 105 tracts of land, most of which are a
8 few tenths of an acre in size. Many of these interest
9 owners disappeared decades ago and could not be located.

10 Q. Some of the -- oftentimes the minerals were
11 severed and the mineral owners just -- or can't be found?

12 A. Yes, sir.

13 Q. Okay. What percentage of the south half of
14 Section 3 has Chi leased?

15 A. We obtained 61 leases from mineral owners
16 covering approximately 85 percent of the mineral interest.
17 In addition, we have verbal commitments for leases covering
18 additional 5 to 10 percent of the minerals. The remainder
19 is unleased.

20 Q. Is Exhibit 3 a list of all the owners currently
21 unleased?

22 A. Yes.

23 Q. And it contains addresses where you had them,
24 correct?

25 A. Yes, sir.

1 Q. And are efforts ongoing to lease these people?

2 A. Yes, they are.

3 Q. Okay, now -- And if leases are obtained from any
4 of these people, will you notify the Division that those
5 owners aren't subject to the pooling?

6 A. Yes.

7 Q. Okay. Now let's discuss your efforts to obtain
8 the voluntary joinder of these interest owners. What steps
9 did you take to lease these people?

10 A. Starting about two or three years ago, Tierra Oil
11 Company started leasing the south half of Section 3.
12 Checked the county records and other available records and
13 leased those interest owners that it could. It also bought
14 some of the minerals. Tierra then signed the leases to us
15 or leased its interest to us.

16 Q. And have contacts been ongoing from two or three
17 years ago to the present?

18 A. Yes.

19 Q. Even recently, some letters have been sent out to
20 the interest owners?

21 A. Yes, sir.

22 Q. Now, did most of these people indicate that they
23 wanted to lease rather than participate in the well?

24 A. Yes, sir.

25 Q. And so leases were sent to them?

1 A. Yes, sir.

2 Q. Together with bonus payments --

3 A. Right.

4 Q. -- correct?

5 And does Exhibit 4 contain copies of the
6 correspondence with these interest owners?

7 A. Yes.

8 Q. In going through the records, what type of
9 records were searched by Tierra and by Chi to locate these
10 people?

11 A. The records of the County Clerk, the County Tax
12 Assessor, phone records and Internet searches.

13 Q. In your opinion, has Chi Energy made a good-faith
14 effort to obtain the voluntary joinder of the interest
15 owners in the well or to locate all interest owners?

16 A. Yes.

17 Q. Would you identify Exhibit 5 and describe the
18 cost of the well?

19 A. Exhibit 5 is a copy of the AFE for the well. It
20 is a 12,000-foot test with an estimated dryhole cost of
21 \$939,000 and a completed well cost of \$1.4 million.

22 Q. And are these costs in line with the costs of
23 other wells drilled to this depth in this area of Eddy
24 County?

25 A. Yes.

1 Q. Do you request that Chi Operating, Inc., be
2 designated operator of the well?

3 A. Yes.

4 Q. And do you have a recommendation for the amounts
5 which Chi Energy should be paid for supervision and
6 administrative expenses?

7 A. Yes, we request that \$6000 a month be allowed for
8 a drilling well and \$600 a month be allowed for a producing
9 well.

10 Q. And are these amounts equivalent to those
11 normally charged by Chi and other operators in this area
12 for wells of this depth?

13 A. Yes.

14 Q. And do you request that these rates be adjusted
15 periodically as provided by the COPAS accounting procedure?

16 A. Yes.

17 Q. Does Chi request that the maximum cost-plus-200-
18 percent risk charge be assessed against nonconsenting
19 owners?

20 A. Yes.

21 Q. And although under the Division's Rules, Mr.
22 Qualls, geology isn't necessary, you did bring it along.
23 Are those exhibits submitted as Exhibits 8 and 9?

24 A. Yes, sir.

25 Q. I'll have you go over those briefly, Mr. Qualls.

1 But first, have you also qualified before the Division as
2 an expert petroleum engineer?

3 A. Geologist.

4 Q. Or geologist, excuse me.

5 A. Yes.

6 Q. Yes. Would you just look at Exhibits 8 and 9 and
7 just briefly, since we have them, discuss what the target
8 zone is for your proposed well?

9 A. Exhibit 8 is a structure map on top of the lower
10 Morrow clastics. You see the location there. We're just
11 trying to get in a good spot, structurally high, and
12 hopefully we'll hit some of those lower Morrow sands.

13 Q. And looking at the isopach map, is the Morrow out
14 there fairly limited, at least as you move to the east,
15 there's not many Morrow wells?

16 A. Yes.

17 Q. And you believe this supports the cost-plus-200-
18 percent risk charge?

19 A. Yes, sir.

20 MR. BRUCE: Mr. Examiner, as I indicated before
21 the hearing I forgot to bring my notice exhibits with me,
22 but I am asking that the case be continued to January 8th
23 so that I can provide those exhibits for you.

24 Q. (By Mr. Bruce) Mr. Qualls, were Exhibits 1
25 through 5 and 8 and 9 prepared by you or under your

1 supervision and compiled from company business records?

2 A. Yes.

3 Q. And in your opinion, is the granting of Chi
4 Energy's Application in the interests of conservation and
5 the prevention of waste?

6 A. Yes.

7 MR. BRUCE: Mr. Examiner, I move the admission of
8 Exhibits 1 through 5, 8 and 9.

9 EXAMINER JONES: Exhibits 1 through 5, 8 and 9
10 are admitted to evidence.

11 EXAMINATION

12 BY EXAMINER JONES:

13 Q. Mr. Qualls, the terms that you offered to these
14 mineral interest owners are pretty generous here, right, 15
15 percent?

16 A. Yes, sir.

17 Q. And you still couldn't get a rise out of them,
18 couldn't get them to --

19 A. Some of them have committed and said they'd do
20 something, but they just haven't pulled the trigger on it
21 yet. We've been pretty fair, I thought, out in that part
22 of the country for what we've offered them.

23 Q. And when did Tierra change over to Chi? Was it
24 -- What kind of a transfer was that?

25 A. They signed their leases and part of their

1 mineral interests that they had. It was about a year and a
2 half ago.

3 Q. A year and a half ago?

4 A. Roughly.

5 Q. So these notices, were these all under the name
6 of Tierra, or were under the name of Chi? I mean --

7 A. They're being sent out in Chi's behalf by Tierra.

8 Q. They were sent out on Chi's behalf?

9 A. By Tierra. Tierra is actually doing the leasing,
10 and then they will be assigned to --

11 Q. Oh, I see. I see, okay. And you've already got
12 an API number for this well, I notice?

13 A. Yes, sir.

14 Q. So it's already permitted, or at least in the
15 road to be permitted.

16 And you mentioned something about the southwest
17 southwest?

18 MR. BRUCE: Yeah, Mr. Examiner, when I filed the
19 Application I originally only filed it for 320-acre and
20 160-acre units. But in going through this there are a
21 couple of small unleased interests in the drill site, which
22 is the southwest of the southwest, so I amended the
23 Application and filed that on Tuesday. And I will give
24 notice of that to all the interest owners.

25 EXAMINER JONES: Okay.

1 MR. BRUCE: It's just to cover the unleased
2 interests. I couldn't find any 40-acre oil pools within a
3 mile, but --

4 EXAMINER JONES: Okay.

5 MR. BRUCE: -- better to be safe than sorry.

6 EXAMINER JONES: Okay, Gail, do you have any
7 questions?

8 MS. MacQUESTEN: No, thank you.

9 EXAMINER JONES: Okay. So you want to continue
10 this until January the 8th?

11 MR. BRUCE: January the 8th, and then ask that it
12 be taken under advisement at that time, after the notice is
13 submitted.

14 EXAMINER JONES: Okay, thank you very much, Mr.
15 qualls. And we'll continue this case until January the
16 8th, Case 13,193.

17 (Thereupon, these proceedings were concluded at
18 8:29 a.m.)

19 * * *

20 I do hereby certify that the foregoing is
21 a complete record of the proceedings in
22 the Examiner hearing of Case No. _____
23 heard by me on _____.

24 _____, Examiner
25 Oil Conservation Division

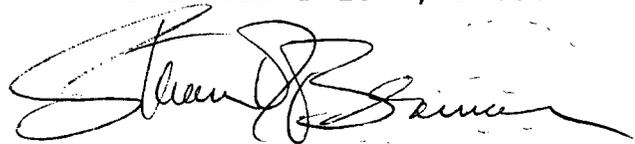
CERTIFICATE OF REPORTER

STATE OF NEW MEXICO)
) ss.
 COUNTY OF SANTA FE)

I, Steven T. Brenner, Certified Court Reporter and Notary Public, HEREBY CERTIFY that the foregoing transcript of proceedings before the Oil Conservation Division was reported by me; that I transcribed my notes; and that the foregoing is a true and accurate record of the proceedings.

I FURTHER CERTIFY that I am not a relative or employee of any of the parties or attorneys involved in this matter and that I have no personal interest in the final disposition of this matter.

WITNESS MY HAND AND SEAL December 18th, 2003.



STEVEN T. BRENNER
 CCR No. 7

My commission expires: October 16th, 2006