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MAY 01 2003

OIL CONSERVATION
DIVISION

David -

A copy of the proposed order I ~~will~~
e-mailed to you.

Jim Bruce
(on behalf of Pam Kellachin)

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MAY 01 2003

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. 13048

APPLICATION OF DEVON ENERGY PRODUCTION
COMPANY, L.P. FOR COMPULSORY POOLING,
LEA COUNTY, NEW MEXICO.

APPLICATION OF EGL RESOURCES, INC.
FOR COMPULSORY POOLING,
LEA COUNTY, NEW MEXICO

CASE NO. 13049

ORDER NO. ----

**DEVON'S PROPOSED
ORDER OF THE DIVISION**

BY THE DIVISION:

This case came on for hearing at 8:15 a.m. on April 10, 2003, at Santa Fe, New Mexico, before Examiner David K. Brooks.

NOW, on this ___ day of April, 2003, 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 these cases and of the subject matter.

(2) Devon Energy Production Company ("Devon") seeks an order pooling all uncommitted mineral interests from the base of the Morrow formation to the base of the Devonian formation underlying the N/2 of Section 4, Township 23 South, Range 34 East, NMPM, Lea County, New Mexico, to form a standard 320-acre gas spacing and proration unit ("GPU") for all formations or pools spaced on 320-acres within this vertical extent.

(3) EGL Resources, Inc. ("EGL") seeks an order pooling all uncommitted mineral interests from the base of the Morrow formation to the base of the Devonian formation underlying all of Section 4, Township 23 South, Range 34 East, NMPM, Lea County, New Mexico, to form a 640-acre gas spacing and proration unit ("GPU") to be dedicated to the North Bell Lake Devonian Gas Pool.

(4) Robert E. Landreth ("Landreth") appeared in support of EGL's application and in opposition to Devon.

(5) Both applicants seek to reenter Devon's Rio Blanco "4" Federal Com Well No. 1 (**API#30-025-34515**) located in Unit F of Section 4 and deepen it to the Devonian formation. This well is currently dedicated by the Division to a standard 320-acre GPU for any production from the Antelope Ridge Atoka-Morrow Gas Pools.

(6) Devon filed a Motion to Dismiss the EGL application because EGL is mistakenly attempting to pool a 640-acre GPU in violation of Division rules.

(7) EGL filed a Motion to Dismiss the Devon application based upon its contention that Section 4 is subject to the Special Rules and Regulations for the North Bell Lake Devonian Rule and therefore requires 640-acre GPU.

(8) Because these cases involve a dispute over a 320-acre GPU versus a 640-acre GPU, they were consolidated for purposes of hearing. The granting of one application will require the denial of the other.

(9) Because of the acreage dispute the parties have not been able to reach a voluntary agreement and the issuance of the compulsory pooling order by the Division is necessary.

DEVONIAN WELL SPACING FOR SECTION 4

(10) This dispute about the applicable Division well spacing rule for a Devonian well requires the Division to interpret its own rules and render a legal opinion based on current Division Rules: (a) The special Rules and Regulations for the North Bell Lake Devonian Gas Pool "the Pool Rules"(Order R-4624) and (b) "Wild cat Well Rules" (Division Rule 104(1)(b)).

(11) The Pool Rules require 640-acre GPUs, but those rules are limited to any well completed "within one mile" of the outer boundary of the pool.

(12) The eastern most boundary of this pool is exactly one mile from the western edge of Section 4.

(13) Because the well is located more than one mile from this pool's boundary the well is not "within one mile" and the Division should find that these special Pool rules to do not apply to this well.

(14) In addition, the western side of Section 4 is exactly one mile from the eastern outer boundary of this pool, the Division should find that the well should be classified as a "Wildcat Well" in accordance with Division Rules 104(1)(b) because it is a distance of one mile or more from the outer boundary of this pool.

DEVELOPMENT OF THE DEVONIAN

(15) Devon and Landreth each contend that they were pursuing developing their own plans for testing the Devonian formation in Section 4.

(16) The evidence demonstrates that:

(a) By February 7, 2001, Devon had an approved Authority for Expenditure (AFE") for the acquisition of 133 square miles of Western/Geco 3-D seismic data that would include Section 4.

(b) On May 11, 2001, Landreth, based upon conventional geology and two 2-D seismic lines, submitted to Devon a proposal for the re-entry of the Rio Blanco "4" Federal Com Well No. 1 to be deepened to the Devonian.

(c) It is obvious that Devon did not intent to proceed with considering Landreth's proposed re-entry until Devon had evaluated its 3-D data.

(d) By July 2002, Devon had completed it acquisition and was ready to study its 3-D seismic data.

(e) In 1994, Landreth obtained his first working interest to Section 4 and was a working interest owner in the drilling of the Rio Blanco "4" Federal Com Well No. 1, that, , was drilled in 1998 to the Morrow formation.

(f) Despite having an interest in Section 4 since 1994, Landreth waited until September 20, 2002 to send a letter to Richard Winchester of Devon proposing this re-entry to Mr. Winchester and in doing so failed to bring to Mr. Winchester's attention an earlier proposal to Ken Gray of Devon.

(g) By September 20, 2002, Landreth and EGL had 75% of the Working interest Ownership (“WIO”) in the N/2 and 87.5% of the WIO in all of Section 4, **but instead** of relying upon their majority interest, their interpretation of the geology as justification to compulsory pool Devon’s interest, Landreth tried various strategies to obtain Devon’s 3-D seismic data; was unwilling to proceed to drill based upon his 2-D seismic interpretation; and wanted to trade part of his interest to Devon in order to obtain and review Devon’s 3-D seismic data without paying for it. Also, in the Fall of 2002, EGL sent an agent/employee to WesternGeco’s office in Midland, Texas, representing to WesternGeco that they had received Devon’s permission to review the 3D under Devon’s license agreement with WesternGeco – a misrepresentation on EGL’s part to gain access to the 3D data at Devon’s expense.

(h) By February 14, 2003, Landreth had taken Devon’s draft proposal and carefully reviewed it, making various changes, but did not change Devon’s plan to dedicate the N/2 of Section 4 to the re-entry. Instead, Landreth wanted Devon to: make 8 sections of 3-D seismic data available to Landreth when the agreement was signed, allow Landreth to split his interest so that part was a carried interest. Landreth also included as a proposed change, a requirement that Devon drill no closer than 1,320’ FSL of Section 33, T22S-R34E, clearly an illegal location in the N. Bell Lake Devonian pool in which lease line spacing is 1,650’ (See Devon’s Exhibit 19 and 21).

(16) On January 27, 2003, the BLM had approved Devon’s sundry notice to whip stock the wellbore and deepen it to the Devonian, classified as a wildcat well under NMOCD rules.

(17) By March 7, 2003, Devon filed its application for compulsory pooling having:

- (a) engaged in detailed and exhaustive negotiations with Landreth and EGL;
- (b) tried without success to form a 640-acre working interest owner unit pursuant to a Joint Operating Agreement;
- (c) forwarded a formal well proposal, including an AFE determined from a well design approved by all parties.

(18) On March 13, 2003, Richard Winchester of Devon met with Wes Perry of EGL but Landreth refused to meet unless Devon agreed to a 640-acre spacing unit for the Rio Blanco Federal “4” Com Well No. 1.

(19) On March 27, 2003, the OCD-Hobbs confirmed that the Rio Blanco "4" Federal Com Well No. 1 is a "Wildcat" Devonian well.

GEOLOGIC EVIDENCE

(20) Based upon the geologic and geophysical evidenced presented by the parties the Division finds that:

- (a) Devon's 3-d geophysical data is superior to the Landreth/EGL 2-d data because 3-d seismic better images the subsurface and properly locates subsurface features due to closely spaced subsurface data points. Devon showed a sample of its 3-d data (Exhibit A2) and believes this is excellent quality seismic for imaging the Devonian formation and mapping deep structures. The Landreth/EGL data was not submitted, and can be presumed to be far inferior to the 3-d data used by Devon.
- (b) The 3-d seismic data used by Devon is commercially available from WesternGeco, and Landreth/EGL could have licensed and used this data set for their interpretation.
- (c) Because the Devon 3-d seismic data is superior to the Landreth/EGL 2-d seismic data, the Devon structural interpretation is superior to, and more reliable than, the Landreth/EGL interpretation. The Devon 3-d interpretation shows that the prospective section 4 structure is clearly separated from the North Bell Lake structure by two north-south trending faults and a syncline. The presence, position, and offset on these faults is defined by the 3-d seismic every 110 feet. In contrast, The Landreth/EGL interpretation shows a single north-south trending fault on the east side of the North Bell Lake structure, and another fault, trending east-west, on the north end of the prospective section 4 structure. The Landreth/EGL interpretation as a whole, and especially the interpretation of faults, is unreliable because their seismic control is limited to close proximity to their less reliable 2-d seismic data. Extrapolation beyond the data is speculative interpretation and probably self-serving.
- (d) The Devon interpretation fits the regional interpretation of Devonian producing structures depicted on Exhibit B1. Existing fields are distinct, relatively simple and compact, structural closures associated with north-south trending faults. The Landreth/EGL interpretation of a large sprawling structure with multiple crests and a critical east-west trending

fault and extensive common gas-water contact clearly does not fit into the regional context. No explanation has been offered for this anomalous and unreasonable interpretation.

- (a) The Rio Blanco Well No. 1 constitutes a wildcat well in the Devonian formation.
- (b) The Devonian underlying Section 4 is not an extension of the North Bell Lake Devonian Pool underlying Section 6.

(21) Devon's 3-D seismic interpretation is the best structural map of the Devonian formation in this area because, as listed above, Devon used the superior data set for its interpretation and demonstrated excellent ties between the 3-d data and well control. The Landreth/EGL group have not shown the quality of their seismic data or the quality of the ties between their seismic data and well control, which can be presumed to be far inferior the data and well ties used by Devon. The result of this is an inferior and unreliable interpretation, which is anomalous and unreasonable compared to nearby Devonian fields. Mr. Landreth repeatedly attempted to validate parts of the Landreth/EGL interpretation by referencing the Devon interpretation.

(22) Landreth interpretation is flawed because:

- (a) Landreth's Structure map shows Section 6, 5, 4 and 18 all to be within the same Devonian reservoir, while Devon's 3-D seismic data conclusively demonstrates that section 4 is not so connected.
- (b) Devon's exhibit B-1 shows the Antelope Ridge field to be about the same size as the Bell Lake North field. Although Antelope Ridge field was drilled on 640 acre spacing, the Devonian structure map (Exhibit B-1) shows that it was effectively drilled on 320 acre and 160 acre spacing with an average spacing of 200 acres. The field has recovered 39 BCF to date, demonstrating that multiple wells enabling higher field recovery are not detrimental. Landreth, in his testimony, agreed with this observation.
- (c) Devon models the Devonian reservoir to be heterogeneous with fracturing and secondary porosity. This can lead to complicated water coning problems and unrecovered gas reserves due to inefficient drainage. Closer spaced drilling can more effectively drain these Devonian reservoirs. Landreth, in his testimony, agreed with this observation.
- (d) Landreth could not demonstrate the outline of his calculated 824 acre drainage radius for the Bell Lake North #6 well. This is suspect in that

more original gas in place could have existed at Bell Lake North field. Evidence from the Landreth Exhibits #8 & #9 show that large amounts of original gas-in-place exist. The Amerada #2 and #3 wells encountered a higher gas-water-contact than that of the Bell Lake North #6 well. The Amerada #3 well DST'd at rates of 4.6 mmcf/d and 1344 bwpd. This well encountered gas saturated reservoir, unfortunately, it was also water saturated due to inefficient production and water coning into the Bell Lake North #6 well. Very likely, if drilling had taken place on spacing less than 640 acres water coning could have been mitigated, waste prevented and incremental gas reserves recovered.

- (e) Landreth testified that he did not attempt any calculations regarding the size/volume and reservoir potential of the Devonian Rio Blanco prospect because there were too many unknowns. Yet, his assumption on the location and structure position of the gas water contact is just as speculative. He has no subsurface control.

AFE and Wellbore Mechanics

(23) Devon has demonstrated that its AFE and Wellbore plan have been carefully and meticulously prepared, and are fair and reasonable, and should be approved by the Division. Landreth and EGL testified that Devon's AFE was reasonable in all material aspects.

SUMMARY

(24) If Landreth really believes his own interpretation, it is difficult for the Division to understand why Landreth waited for the 9 years (Interest in the N/2 NW/4 acquired in March, 1994) to cause a Devonian formation well to be drilled in the same reservoir that included a well that produced more than 31 BFC of gas.

(25) The approval of Devon's application will:

- (a) allow Landreth and EGL to have the benefit of Devon's 3-D seismic interpretation for the N/2 of Section 4 without having paid for it;
- (b) provide an opportunity to Landreth and EGL who hold 100% of the WIO in the S/2 of Section 4 to re-enter the Rio Blanco 4 Federal #2 Well or drill a second well based upon Devon's results with the Rio Blanco 4 Federal Com #1 Well;

(c) provide Landreth and EGL with the choice of sharing with Devon the risk of the re-entry and the rewards, or to require Devon to carry Landreth and EGL's WIO interest;

CONCLUSION

(26) To avoid the drilling of unnecessary wells, protect correlative rights, prevent waste and afford to the owner of each interest in the Unit 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 interests, whatever they may be, in the oil and gas within the Unit.

(27) The application of Devon should be granted and the application of EGL should be denied.

(28) Devon should be designated the operator of the proposed well and of the Unit.

(29) Any pooled working interest owner who does not pay its share of estimated well costs should have withheld from production its share of reasonable well costs plus an additional 200% thereof as a reasonable charge for the risk involved in drilling the well.

(30) Reasonable charges for supervision (combined fixed rates) should be fixed at \$5,000 per month while drilling and \$500 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*."

IT IS THEREFORE ORDERED THAT:

(1) Devon Energy Production Company ("Devon") seeks an order pooling all uncommitted mineral interests from the base of the Morrow formation to the base of the Devonian formation underlying the N/2 of Section 4, Township 23 South, Range 34 East, NMPM, Lea County, New Mexico, to form a standard 320-acre gas spacing and proration unit (the "GPU") for all formations or pools spaced on 320-acres within this vertical extent is hereby **GRANTED**.

(2) EGL Resources, Inc. ("EGL") seeks an order pooling all uncommitted mineral interests from the base of the Morrow formation to the based of the Devonian formation underlying all of Section 4, Township 23 South, Range 34 East, NMPM, Lea County, New Mexico, to form a 640-acre gas spacing and proration unit (the "GPU") to be dedicated to the North Bell Lake Devonian Gas Pool is hereby **DENIED**.

(3) The Rio Blanco "4" Federal Com Well No. 1 is a Wildcat Devonian Well dedicated to a standard 320-acre gas spacing unit.

(4) Devon, as the Division approved operator of this well and spacing unit shall commence drilling the proposed well on or before October 1, 2003, and shall thereafter continue drilling the well with due diligence to test the Devonian formation.

(5) In the event the operator does not commence drilling the proposed well on or before October 1, 2003, Ordering Paragraph (1) shall be of no effect, unless the operator obtains a time extension from the Division Director for good cause.

(6) Should the proposed well, or its replacement, not be drilled to completion, or be abandoned, within 120 days after commencement thereof, the operator shall appear before the Division Director and show cause why Ordering Paragraph (1) should not be rescinded.

(7) Upon final plugging and abandonment of the proposed well, the pooled unit created by this Order shall terminate, unless this order has been amended to authorize further operations.

(8) Devon is hereby designated the operator of the proposed well and of the Unit.

(9) 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 Unit, including unleased mineral interests, who are not parties to an operating agreement governing the Unit.) After the effective date of this order, the operator shall furnish the Division and each known pooled working interest owner in the Unit an itemized schedule of estimated costs of drilling, completing and equipping the proposed well ("well costs").

(10) 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 wells costs as provided in this paragraph shall thereafter be referred to as "non-consenting working interest owners."

(11) 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.

(12) Within 60 days following determination of reasonable well costs, any pooled working interest owner who has paid its share of estimated 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 the amount, if any, that the estimated well costs it has paid exceed its share of reasonable well costs.

(13) 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; and

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

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

(15) Reasonable charges for supervision (combined fixed rates) are hereby fixed at \$5,000 per month while drilling and \$500 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 are reasonable, attributable to pooled working interest owners.

(16) Except as provided in Ordering Paragraphs (11) and (13) above, all proceeds from production from the 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.

(17) 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.

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

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

(20) 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

LORI WROTENBERY
Director S E A L