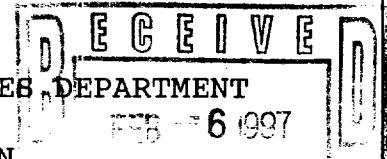


STATE OF NEW MEXICO
ENERGY, MINERALS AND NATURAL RESOURCES DEPARTMENT
OIL CONSERVATION DIVISION



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

CASE NO. 11,692

APPLICATION OF INTERCOAST OIL AND)
GAS COMPANY FOR COMPULSORY POOLING)
AND UNORTHODOX GAS WELL LOCATION,)
EDDY COUNTY, NEW MEXICO)

ORIGINAL

REPORTER'S TRANSCRIPT OF PROCEEDINGS

EXAMINER HEARING

BEFORE: DAVID R. CATANACH, Hearing Examiner

January 23rd, 1997

Santa Fe, New Mexico

This matter came on for hearing before the New Mexico Oil Conservation Division, DAVID R. CATANACH, Hearing Examiner, on Thursday, January 23rd, 1997, at the New Mexico Energy, Minerals and Natural Resources Department, Porter Hall, 2040 South Pacheco, Santa Fe, New Mexico, Steven T. Brenner, Certified Court Reporter No. 7 for the State of New Mexico.

* * *

I N D E X

January 23rd, 1997
 Examiner Hearing
 CASE NO. 11,692

	PAGE
APPEARANCES	3
APPLICANT'S WITNESSES:	
<u>RICK DEFFENBAUGH</u> (Landman)	
Direct Examination by Mr. Bruce	4
Examination by Examiner Catanach	12
Examination by Mr. Kellahin	13
Examination (Continued) by Examiner Catanach	14
<u>WILLIAM A. SIRUTA</u> (Geologist)	
Direct Examination by Mr. Bruce	16
Examination by Examiner Catanach	20
REPORTER'S CERTIFICATE	22

* * *

E X H I B I T S

Applicant's	Identified	Admitted
Exhibit 1	7	12
Exhibit 2	8	12
Exhibit 3	9	12
Exhibit 4	10	12
Exhibit 5	8	12
Exhibit 6	11	12
Exhibit 7	11	12
Exhibit 8	16	20
Exhibit 9	17	20
Exhibit 10	17	20
Exhibit 11	18	20
Exhibit 12	19	20

* * *

A P P E A R A N C E S

FOR THE APPLICANT:

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P.O. Box 2068
Santa Fe, New Mexico 87504-2068
By: JAMES G. BRUCE

FOR LOUIS DREYFUS NATURAL GAS CORPORATION:

KELLAHIN & KELLAHIN
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P.O. Box 2265
Santa Fe, New Mexico 87504-2265
By: W. THOMAS KELLAHIN

FOR PENWELL ENERGY, INC.:

CAMPBELL, CARR, BERGE and SHERIDAN, P.A.
Suite 1 - 110 N. Guadalupe
P.O. Box 2208
Santa Fe, New Mexico 87504-2208
By: WILLIAM F. CARR

* * *

1 WHEREUPON, the following proceedings were had at
2 12:20 p.m.:

3 EXAMINER CATANACH: At this time we'll call Case
4 Number 11,692, the Application of InterCoast Oil and Gas
5 Company for compulsory pooling and unorthodox gas well
6 location, Eddy County, New Mexico.

7 Call for appearances.

8 MR. BRUCE: Mr. Examiner, Jim Bruce from the
9 Hinkle law firm in Santa Fe, representing the Applicant.

10 I have two witnesses to be sworn.

11 EXAMINER CATANACH: Additional appearances?

12 MR. KELLAHIN: Mr. Examiner, I'm Tom Kellahin of
13 the Santa Fe law firm of Kellahin and Kellahin, appearing
14 on behalf of Louis Dreyfus Natural Gas Corporation.

15 EXAMINER CATANACH: Will the witnesses please
16 stand to be sworn in?

17 (Thereupon, the witnesses were sworn.)

18 RICK DEFFENBAUGH,
19 the witness herein, after having been first duly sworn upon
20 his oath, was examined and testified as follows:

21 DIRECT EXAMINATION

22 BY MR. BRUCE:

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

25 A. Yes, my name is David R. Deffenbaugh, that's

1 D-e-f-f-e-n-b-a-u-g-h. I go by Rick. I'm from Tulsa,
2 Oklahoma.

3 Q. Okay. What is your job?

4 A. I'm a senior landman for KCS Medallion Resources,
5 Inc., formerly InterCoast Oil and Gas Company.

6 Q. Have you previously testified before the Division
7 as a petroleum landman?

8 A. Yes, I have.

9 Q. And were your credentials as an expert petroleum
10 landman accepted as a matter of record?

11 A. Yes, they were.

12 Q. And are you familiar with the land matters
13 involved in this case?

14 A. I am.

15 Q. Mr. Deffenbaugh, before we begin, this
16 Application was filed under the name of InterCoast Oil and
17 Gas Company in December. You just mentioned the name
18 change. When was that effective?

19 A. January 2nd of 1997.

20 Q. Okay. And it's still the same company, it's just
21 a name change?

22 A. That's correct.

23 Q. Briefly, what does InterCoast seek in this case?

24 A. We seek an order from the Commission pooling the
25 acreage in Section 29 of 22 South, 26 East, Eddy County,

1 New Mexico, from the surface to the base of the Morrow as
2 follows: The west half for formations spaced on 320 acres
3 and the northwest quarter spaced -- for formations spaced
4 on 160 acres.

5 We also request the approval of an unorthodox
6 location for a well to be drilled at 1715 feet from the
7 north line and 1160 feet from the west line.

8 Q. Mr. Deffenbaugh, that's a change from the
9 originally proposed well location; is that not?

10 A. That is correct.

11 Q. What was the location that was advertised?

12 A. The original location was 1650 from the north
13 line by 510 feet from the west line.

14 Q. Okay. So the location that will actually be
15 drilled is less unorthodox than advertised?

16 A. That's correct.

17 EXAMINER CATANACH: Can you give me that location
18 again, the new location?

19 THE WITNESS: Yes, sir, 1715 from the north by
20 1160 from the west.

21 EXAMINER CATANACH: Okay.

22 Q. (By Mr. Bruce) And the geologist will discuss
23 the reasons for the unorthodox location?

24 A. Yes.

25 Q. Okay, why don't you refer to Exhibits 1 and 2 and

1 identify them for the Examiner and discuss their contents.

2 A. Exhibit Number 1 is just a plat showing the west
3 half of Section 29, being the proposed unit. The colors
4 basically represent individual tracts within the west half.

5 You can see the green tract represents the north
6 half northwest. That's owned by KCS Medallion, formerly
7 InterCoast.

8 The orange tract represents the southeast
9 northwest. That is a tract owned 100 percent by Penwell
10 Energy, Inc.

11 The three red tracts, being the southwest of the
12 northwest quarter, the northeast of the southwest quarter,
13 and the southwest quarter of the southwest quarter, are
14 owned by Louis Dreyfus, seventy-five point -- actually that
15 should be 75.22 percent; Santa Fe Energy Resources, Inc.,
16 with 13.27 percent; and there's about 11.51 percent of that
17 120 acres that has not been committed to leasing formally
18 yet.

19 The blue tracts represent 80 acres, being the
20 northwest southwest and the southeast southwest that is
21 owned 85 percent by Louis Dreyfus, 15 percent by Santa Fe
22 Energy Resources, Inc.

23 Then in the upper right-hand corner, if you will,
24 what would be the northeast quarter of this section, you
25 can see a breakout of the working interest ownership for

1 the unit.

2 Q. Okay, and Exhibit 2 is submitted merely to show
3 the offset operators to your proposed well?

4 A. That's correct.

5 Q. For notification purposes, for the unorthodox
6 location?

7 A. That's correct.

8 Q. Okay. Now, let's skip down a little bit, Mr.
9 Deffenbaugh, to Exhibit 5. Skip Exhibits 3 and 4 now.
10 Does this exhibit represent the leaseholder mineral owners
11 in the west half of Section 29?

12 A. Yes, it does.

13 Q. And other than the ones listed on Exhibit 1 --
14 This listing would include those who have -- who are
15 unleased; is that correct?

16 A. That's correct. Going through this list if you
17 would, the -- Louis Dreyfus has the 49.45 percent.

18 Penwell has the 12.5 percent.

19 Santa Fe Energy Resources has their 8.73 percent.

20 This party listed as SASI Minerals Company is
21 actually Republic Royalty Company. They have 3.48 percent.
22 That interest is an unleased mineral interest.

23 Dodge Jones Foundation has a .55 percent interest
24 that remains unleased.

25 The Fasken Foundation executed a lease that has

1 been placed of record now to Louis Dreyfus, and that
2 interest has been credited to the percentage that I show in
3 my Exhibit 1.

4 MATT-TEX, L.L.P., has a .11 percent interest that
5 remains unleased.

6 Randy Geiselman is a party that has leased to
7 Louis Dreyfus and has been credited in their total.

8 John A. Matthews, Jr., has a .06 percent.

9 Andrews Royalty, Inc., has a .03 percent.

10 And then the first three trusts of Mary Ralph
11 Lowe have all leased to Louis Dreyfus.

12 And the last interests, being Julia Jones
13 Matthews, represents .08 percent that is also unleased at
14 this time.

15 Q. Okay. Now, let's discuss the efforts to obtain
16 the voluntary joinder of the parties. Could you refer to
17 Exhibit 3 and identify that for the Examiner?

18 A. Yes, this is a copy of the original proposal, the
19 formal proposal letter that we sent out, dated November
20 8th, 1996. We actually began acquisition activity in about
21 July of 1996 and made contacts through a contract broker
22 for the acquisition of these various interests within the
23 unit.

24 But this basically represents the formal proposal
25 letter that was sent to all the parties that we had not

1 reached agreement with at that time.

2 Q. Subsequent to this letter, did you have any
3 additional phone calls or correspondence with the parties?

4 A. Yes, numerous phone calls to the various parties
5 and, in fact, those parties are continuing to negotiate.
6 We continue to negotiate with all of the remaining interest
7 owners that have not been committed and actually expect to
8 have an agreement reached with them, but we just don't have
9 those formalized as yet.

10 Q. Okay, what is Exhibit 4?

11 A. Exhibit 4 is a letter that was sent to the
12 parties who we had not obtained voluntary agreement with,
13 notifying them of the change of location.

14 Q. Okay. And also a revision to the AFE costs?

15 A. That's correct.

16 Q. Okay. Now, if these parties lease their
17 interests or come to terms on an operating agreement, will
18 you notify the Division so that they do not need to be
19 pooled?

20 A. Yes.

21 Q. In your opinion, has InterCoast, now KCS
22 Medallion, made a good-faith effort to obtain the voluntary
23 joinder of all interest owners in the well?

24 A. Yes, we have.

25 Q. What is Exhibit 6, Mr. Deffenbaugh?

1 A. Exhibit 6 is KCS's authorization for
2 expenditures, showing the cost to drill and complete the
3 McKittrick 29-1 well as proposed.

4 Q. Is this cost in line with the cost charged by
5 other operators for wells of this depth in this area of the
6 county?

7 A. Yes, it is.

8 Q. And do you have a recommendation for the amounts
9 which should be charged for overhead expenses?

10 A. Yes, we would recommend a drilling rate of \$5828
11 and a producing rate of \$546.

12 Q. And are these amounts you have recommended in
13 line with those charged by other operators in this area?

14 A. Yes, they are, and also based on the Ernst and
15 Young 1995 drilling survey.

16 Q. Were the interest owners in this well notified of
17 this hearing?

18 A. Yes, they were. Exhibit 7 is an affidavit of
19 notice with the copies of the notice letter and certified
20 return receipts attached.

21 Q. And this notice letter also notified the offset
22 operators of the proposed unorthodox location; is that
23 correct?

24 A. That is correct.

25 Q. Okay. Were Exhibits 1 through 7 prepared by you

1 or under your supervision or compiled from company business
2 records?

3 A. Yes, they were.

4 Q. And in your opinion, is the granting of this
5 Application in the interests of conservation and the
6 prevention of waste?

7 A. Yes, they are.

8 Q. One final question, Mr. Deffenbaugh: Do you
9 request expedited approval of this Application?

10 A. Yes, we do. We have a lease expiration February
11 28th, 1997, on a portion of our interest.

12 Q. Okay. You must spud the well by then?

13 A. That's correct.

14 Q. Mr. Examiner -- Whoops, one final thing, Mr.
15 Deffenbaugh: In your opinion is the granting of this
16 Application in the interests of conservation and the
17 prevention of waste?

18 A. Yes, it is.

19 MR. BRUCE: Mr. Examiner, we would move the
20 admission of Applicant's Exhibits 1 through 7 at this time.

21 EXAMINER CATANACH: Exhibits 1 through 7 will be
22 admitted as evidence.

23 EXAMINATION

24 BY EXAMINER CATANACH:

25 Q. I'm sorry, what was the spud date on that?

1 A. Well, we have an expiration of 2-28-97, February
2 28th, 1997.

3 MR. KELLAHIN: Excuse me, Mr. Examiner, I have a
4 couple questions.

5 EXAMINER CATANACH: I'm sorry, go ahead, Mr.
6 Kellahin.

7 EXAMINATION

8 BY MR. KELLAHIN:

9 Q. Mr. Deffenbaugh, what is the status of your
10 negotiations with Santa Fe Energy Resources?

11 A. With Santa Fe?

12 Q. Yes, sir.

13 A. The negotiations with them have stemmed through
14 Louis Dreyfus.

15 Dreyfus has an operating agreement signed by
16 Santa Fe, and we are in agreement with Louis Dreyfus as
17 well and expect fully to have our operating agreement
18 finalized.

19 One thing I guess I did not go through is that
20 Dreyfus, InterCoast, Penwell and Santa Fe Energy Resources
21 all will be participants -- we believe will be participants
22 at this time, and it's merely a formalization of the
23 contracts necessary to finalize the -- well, we just need
24 the executed agreements completed to set that forth, and we
25 will advise the Commission as to when that occurs.

1 Q. That was my question. It wasn't clear to the
2 Examiner, perhaps, that --

3 A. Right, I agree.

4 Q. -- all of these parties, with the exception of
5 the unleased interests, were moving forward towards a
6 contractual solution by which they could all agree on
7 participation in the spacing unit for the well.

8 A. Yes, sir, that's the case.

9 MR. KELLAHIN: Thank you, Mr. Examiner.

10 EXAMINATION (Continued)

11 BY EXAMINER CATANACH:

12 Q. So the only interest owners you anticipate
13 pooling are the ones that -- the smaller interest owners
14 that you've discussed with me?

15 A. Well, we would like to list everyone as a pooled
16 party until we reach formal agreement.

17 But even as to those unleased interests, we more
18 than likely will reach -- we are in negotiations and have
19 been continuously with them.

20 They have a very onerous lease form that we're
21 working through paragraph by paragraph, if you will, and I
22 expect and fully intend to have an agreement even with
23 those parties, so that we will be able to also advise that
24 they would be released.

25 Q. Okay. Do you wish to -- Within this compulsory

1 pooling order, do you wish to have the name remain
2 InterCoast, or do you wish that you --

3 A. I believe we'd like to see the name listed as we
4 are. That's a question I guess I'd defer to counsel as to
5 how we would handle.

6 But technically when we filed this Application,
7 we were InterCoast Oil and Gas Company, and as of January
8 2nd, 1997, we are now KCS Medallion Resources, Inc.

9 I think we would probably like to have it issued
10 in KCS Medallion Resources, Inc.

11 MR. BRUCE: Yes, Mr. Examiner, there was no
12 change in the corporation.

13 It's still the same corporation; it's merely a
14 corporate name change.

15 EXAMINER CATANACH: I have nothing further.

16 MR. BRUCE: Call Mr. Siruta to the stand.

17 MR. CARR: Mr. Catanach, with your permission I'd
18 like the record to reflect that our firm has entered its
19 appearance in this matter for Penwell.

20 MR. BRUCE: I object, Mr. Examiner.

21 EXAMINER CATANACH: We will allow you to do that,
22 Mr. Carr.

23 MR. CARR: Thank you, Mr. Catanach.

24 EXAMINER CATANACH: We will not allow Mr. Bruce
25 to object to that.

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WILLIAM A. SIRUTA,

the witness herein, after having been first duly sworn upon his oath, was examined and testified as follows:

DIRECT EXAMINATION

BY MR. BRUCE:

Q. Mr. Siruta, would you state your full name and city of residence for the record?

A. William A. Siruta, and I live in Midland, Texas.

Q. Who do you work for and in what capacity?

A. I'm a geologist with KCS Medallion Resources, Inc.

Q. Have you previously testified before the Division as a petroleum geologist?

A. Yes, I have.

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

A. Yes.

Q. And are you familiar with the geologic matters pertaining to this Application?

A. Yes.

MR. BRUCE: Mr. Examiner, I tender Mr. Siruta as an expert geologist.

EXAMINER CATANACH: He is so qualified.

Q. (By Mr. Bruce) Mr. Siruta, would you refer to your Exhibit 8 and identify it for the Examiner and discuss

1 the primary zone of interest in your proposed well?

2 A. This is a production map of the area where our
3 prospect is located. At the -- Nearby each well you'll see
4 indicated three letters, like MOR or STR. The MOR are the
5 Morrow wells; the STR are the Strawn wells.

6 The first number is the cumulative production to
7 date of the well, gas production. The second number is the
8 condensate or oil production to date. And the number below
9 that is the daily rate.

10 And also on this map we have the unit identified
11 as a hachured area and the proposed location as a red dot,
12 and our cross-section is indicated by the dashed line.

13 Q. And what you're aiming for is some of this better
14 Morrow production to the north or to the west of your
15 proposed well?

16 A. Yeah, really the two key wells that we're keying
17 off of are the two wells in 20.

18 Q. Okay, let's move on to your Exhibit 9. Would you
19 identify that for the examiner?

20 A. Exhibit 9 is the structure map on the lower
21 Morrow. And again, it has the same symbols on it.
22 Basically, it's showing dip to the southeast.

23 Q. Okay. Would you now refer to your Exhibit 10,
24 discuss it and identify the elements of risk involved in
25 drilling this well?

1 A. This is a net isopach of what we call the middle
2 Morrow green sand. The net -- It's a net of porosity
3 greater than or equal to 8 percent.

4 You can see that the two wells that were -- or
5 actually three wells that we're keying on, the two wells in
6 20, the one in the north has 30 feet, the one in the
7 southwest quarter has 21 feet, and the well in the north
8 half of 30 has 14 feet. We believe that system has a
9 possibility of us continuing to the south.

10 We have good well control to the north; but as
11 you can see, as you go to the south you really have no
12 other wells that exhibit any appreciable thickness of sand.
13 I feel like the risk is that this sand could terminate in
14 Section 29, and we may not find any sand, or we may be
15 depleted if we find the sand.

16 Q. Okay, what is Exhibit 11?

17 A. It's a cross-section, just briefly illustrating
18 the main Morrow pay. This -- What we call middle Morrow
19 green sand has been colored in yellow, and it basically
20 shows how the sand develops in here. It thickens and
21 thins, shale units enclosed within the sand.

22 Q. Okay. Now, if any party to this order goes
23 nonconsent, what penalty would you recommend against such
24 an owner?

25 A. I'd recommend cost plus 200 percent.

1 Q. Now, we have an unorthodox well location. Would
2 you identify your Exhibit 12 and discuss the reasons for
3 that unorthodox location?

4 A. Exhibit 12 is a topographic map of the area. And
5 if you'll look where we have our location indicated on here
6 with a red dot, the next contour lines just above that, as
7 you go to the west, from that point on to the west the
8 surface is a very rocky, hard surface that would have to be
9 dynamited to really accommodate a location.

10 So we moved as little as we could to the east to
11 find a fairly flat spot that has more of a surface that
12 will let us lay a location out.

13 Q. Now, the original location, which was 510 feet
14 from the west line, was that also based on topographic
15 reasons?

16 A. Yes, it was --

17 Q. Okay.

18 A. -- initially.

19 Q. Okay. In your opinion, is the granting of this
20 Application in the interests of conservation, the
21 prevention of waste and the protection of correlative
22 rights?

23 A. Yes.

24 Q. And were Exhibits 8 through 12 prepared by you or
25 under your direction?

1 A. Yes.

2 MR. BRUCE: Mr. Examiner, we would move the
3 admission of InterCoast, or KCS Medallion's, Exhibits 8
4 through 12.

5 EXAMINER CATANACH: Exhibits 8 through 12 will be
6 admitted as evidence.

7 EXAMINATION

8 BY EXAMINER CATANACH:

9 Q. This unorthodox location doesn't crowd any of the
10 outer boundaries of the proration unit, does it?

11 A. No, it crowds the quarter-quarter boundary.

12 Q. And that's the closest -- Considering the
13 topographic situation, that's the closest you could come to
14 a standard location?

15 A. Yes, it is.

16 Q. The primary target is the middle Morrow; is that
17 correct?

18 A. Well, that's what we call it out here, middle
19 Morrow. It's the Morrow sands that are above the massive
20 shale unit out here.

21 Q. And you've had a well in the east half of Section
22 29 that was nonproductive in this interval?

23 A. That's correct. There are other Morrow sands
24 that pay here, but the real key and most productive sand is
25 this middle Morrow green sand.

1 EXAMINER CATANACH: I have nothing further.

2 MR. BRUCE: That's all I have in this case, Mr.
3 Examiner.

4 EXAMINER CATANACH: Okay, there being nothing
5 further in this case, Case 11,692 will be taken under
6 advisement.

7 (Thereupon, these proceedings were concluded at
8 12:44 p.m.)

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I do hereby certify that the foregoing is
a complete and correct transcript of the
the proceedings in Case No. 11692,
heard by me on January 23, 1997.
David R. Catanach, Examiner
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 January 27th, 1997.


 STEVEN T. BRENNER
 CCR No. 7

My commission expires: October 14, 1998