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& SHERIDAN, P.A.
LAWYERS

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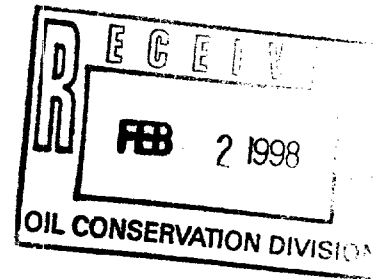
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February 2, 1998

HAND DELIVERED

Michael E. Stogner
Chief Hearing Examiner
Oil Conservation Division
New Mexico Department of Energy, Minerals
and Natural Resources
2040 South Pacheco Street
Santa Fe, New Mexico 87505



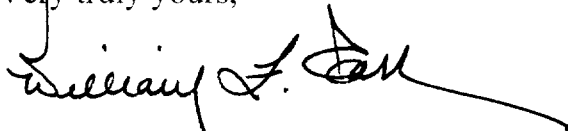
Re: ***Oil Conservation Division Case No. 11912:
Application of Maralo, Inc. for an Unorthodox Oil Well Location, Eddy
County, New Mexico***

Dear Mr. Stogner:

Pursuant to your request following the January 22, 1998 hearing in the above-captioned case, I am enclosing on behalf of Texaco Exploration and Production Inc. proposed orders (1) denying said application and (2) imposing a production penalty.

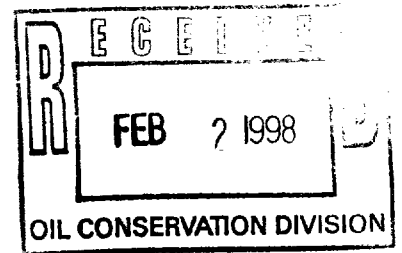
If you need anything further from Texaco to proceed with your consideration of this matter, please advise.

Very truly yours,



WILLIAM F. CARR

cc: Jim Bruce, Esq. (w/enclosures)
D. Bruce Pope, Esq. (w/enclosures)
David Sleeper (w/enclosures)
Dave Uhl (w/enclosures)



Option One: Denial of Application

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. 11912
ORDER NO. R-_____

APPLICATION OF MARALO, INC.
FOR AN UNORTHODOX OIL WELL
LOCATION, EDDY COUNTY, NEW MEXICO.

TEXACO EXPLORATION AND PRODUCTION INC.'S
PROPOSED ORDER OF THE DIVISION

BY THE DIVISION:

This cause came on for hearing at 8:15 a.m. on January 22, 1998, at Santa Fe, New Mexico, before Examiner Michael E. Stogner.

NOW, on this ____ day of January, 1998, the Division Director, having considered the testimony, the record, and the recommendation 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) The applicant, Maralo, Inc. ("Maralo"), seeks approval to drill its Gold Rush "30" Well No. 8 at an unorthodox oil well location 2310 feet from the South line and 2600 feet from the East line (Unit J) of Section 30, Township 23 South, Range 30 East, NMPM, Eddy County, New Mexico, to test the Delaware formation, Southwest Forty-Niner Ridge-

Delaware Pool (Bell Canyon interval) and the Nash Draw-Brushy Canyon Pool. The NW/4 SE/4 of Section 30 is to be dedicated to the subject well forming a standard 40-acre oil spacing and proration unit.

(3) Both the Southwest Forty-Niner Ridge-Delaware Pool and the Nash Draw-Brushy Canyon Pool are developed under rules which provide for wells to be drilled 330 feet from the outer boundary of the dedicated spacing or proration unit.

(4) The proposed well location is 40 feet from the western boundary of the Maralo spacing unit which is 290 feet closer to the boundary of the dedicated spacing and proration unit than permitted by Division rules. As such, this location encroaches on the NE/4 SW/4 of Section 30 which is operated by Texaco Exploration and Production Inc. ("Texaco").

(5) The NE/4 SW/4 of Section 30 is dedicated to the Remuda Basin State "30" Well No. 3 which is located 790 feet from the eastern boundary of the Texaco spacing and proration unit.

(6) Texaco appeared at the hearing and presented evidence in opposition to the application of Maralo.

(7) Maralo presented testimony and evidence which showed that:

- (a) the proposed Maralo unorthodox well location is on a federal lease and is only 40 feet from a State of New Mexico lease operated by Texaco;
- (b) the Bureau of Land Management would not approve a standard well location on the NW/4 SE/4 of Section 30 because of conflicts with archaeology and Cave/Karst on this 40-acre spacing and proration unit and no agreement to mitigate the archeological sites had been reached with the BLM;
- (c) the Brushy Canyon "D" Sand (Loving Sand), which it represents is the primary objective in its proposed well, is present under the eastern portion of the offsetting Texaco spacing and proration unit but not present at the location of the Texaco Remuda Basin State "30" Well No. 3 located thereon;

- (d) Delaware wells in this area experience sharp decline rates after first production;
- (e) Maralo was unable to form a working interest unit for the development of this acreage; and
- (f) Maralo estimates that a directionally drilled well from its requested surface location to a standard bottomhole location would result in a rate of return on its investment of only 20.49% which Maralo considers to render the project economically infeasible (See, Maralo Exhibit No. 13).

(8) Maralo recommends no production penalty be imposed on a well completed in the Brushy Canyon interval because, based on the Maralo interpretation, this sand was not present under most of the NE/4 SW/4 of Section 30. Maralo agreed that an appropriate penalty should be assessed against a well in the Bell Canyon interval but made no specific recommendation as to what this penalty should be.

(9) Texaco's evidence includes an Archeological Site Map (Texaco Exhibit 2) which shows few archeological sites in the area of the proposed Maralo well and Isopach Maps of the Brushy Canyon "D" Sand (Loving Sand) and the Bell Canyon C7 Sand (Texaco Exhibits 3 and 4). These Isopach Maps show that each of the Delaware Sands which are the primary objectives in the proposed Maralo well are continuous and extend under the 40-acre oil spacing unit which Texaco operates in the NE/4 SW/4 of Section 30.

(10) The Isopach Map of the Bell Canyon C7 Sand also demonstrates that the Maralo proposed unorthodox location is in a thicker portion of this reservoir than a standard location.

(11) Texaco testified that in order to protect its correlative rights, the proposed Maralo Gold Rush "30" Federal Well No. 8 should be either denied or assessed a production penalty of 88% (12% allowable) being the footage encroachment from a standard location towards the offsetting Texaco operated tract (290 feet closer than a standard 330 foot set back).

(12) A well at the Maralo proposed unorthodox location is only 40 feet from the

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ORDER NO. R-_____

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western boundary of the NW/4 SE/4 and therefore gains a substantial advantage on the offsetting Texaco spacing and proration unit in the Brushy Canyon and the Bell Canyon intervals of the Delaware formation. A well at this location should be approved only if subject to a substantial production penalty.

(13) A penalty of 88% would result in the well not being drilled and is in fact the same as a denial of the application.

(14) An unorthodox oil well location 2310 feet from the South line and 2600 feet from the East line of said Section 30 would impair the correlative rights of Texaco. Furthermore, Texaco could only protect its spacing and proration unit from drainage by drilling an offset well 40 feet from the common line between these spacing units which would result in an inefficient spacing pattern in the Delaware formation and wasteful drilling practices. Therefore the application should be **denied**.

IT IS THEREFORE ORDERED THAT:

(1) The application of Maralo, Inc. for an unorthodox oil well location for its Gold Rush "30" Federal Well No. 8 to be drilled 2310 feet from the South line and 2600 feet from the East line of Section 30, Township 23 South, Range 30 East, NMPM, Eddy County, New Mexico is hereby **denied**.

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

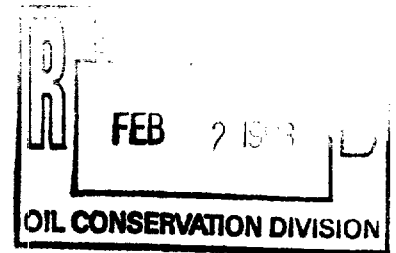
DONE at Santa Fe, New Mexico, on the day and year hereinabove designated.

STATE OF NEW MEXICO
OIL CONSERVATION DIVISION

KATHLEEN A. GARLAND
Acting Director

S E A L

Option Two: Imposition of a Production Penalty



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. 11912
ORDER NO. R-_____

APPLICATION OF MARALO INC. FOR
AN UNORTHODOX OIL WELL
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TEXACO EXPLORATION AND PRODUCTION INC.'S
PROPOSED ORDER OF THE DIVISION

BY THE DIVISION:

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NOW, on this ____ day of January, 1998, the Division Director, having considered the testimony, the record, and the recommendation 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) The applicant, Maralo Inc. ("Maralo"), seeks approval to drill its Gold Rush "30" Federal Well No. 8 at an unorthodox oil well location 2310 feet from the South line and 2600 feet from the East line (Unit J) of Section 30, Township 23 South, Range 30 East, NMPM, Eddy County, New Mexico, to test the Delaware formation, Southwest Forty-Niner

Ridge-Delaware Pool (Bell Canyon) and the Nash Draw-Brushy Canyon Pool. The NW/4 SE/4 of Section 30 is to be dedicated to the subject well forming a standard 40-acre oil spacing and proration unit.

(3) Both the Southwest Forty-Niner Ridge-Delaware Pool and the Nash Draw-Brushy Canyon Pool are developed pursuant to rules which provide for wells to be drilled 330 feet from the outer boundary of the dedicated 40-acre spacing or proration unit.

(4) The proposed well location is 40 feet from the western boundary of the Maralo spacing unit which is 290 feet closer to the boundary of the dedicated spacing and proration unit than permitted by Division rules. As such, this location encroaches on the NE/4 SW/4 of Section 30 which is operated by Texaco Exploration and Production Inc. ("Texaco").

(5) The NE/4 SW/4 of Section 30 is dedicated to the Remuda Basin State "30" Well No. 3 which is located 790 feet from the eastern boundary of the Texaco spacing and proration unit.

(6) Texaco appeared at the hearing in opposition to the application of Maralo.

(7) Maralo presented testimony and evidence which showed that:

- (a) the proposed Maralo unorthodox well location is on a federal lease and is only 40 feet from a State of New Mexico lease operated by Texaco;
- (b) the Bureau of Land Management would not approve a standard well location on the NW/4 SE/4 of Section 30 because of conflicts with archaeology and Cave/Karst on this 40-acre spacing and proration unit and no agreement to mitigate the archeological sites had been reached with the BLM;
- (c) the Brushy Canyon "D" Sand (Loving Sand), which it represents is the primary objective in its proposed well, is present under the eastern portion of the offsetting Texaco spacing and proration unit but not present at the location of the Texaco Remuda Basin State "30" Well No. 3 located thereon;

- (d) Delaware wells in this area experience sharp decline rates after first production;
- (e) Maralo was unable to form a working interest unit for the development of this acreage; and
- (f) Maralo estimates that a directionally drilled well from its requested surface location to a standard bottomhole location would result in a rate of return on its investment of only 20.49% which Maralo considers to render the project economically infeasible (See, Maralo Exhibit No. 13).

(8) Maralo recommends no production penalty be imposed on a well completed in the Brushy Canyon interval because, based on the Maralo interpretation, this sand was not present under most of the NE/4 SW/4 of Section 30. Maralo agreed that an appropriate penalty should be assessed against a well in the Bell Canyon interval but made no specific recommendation as to what this penalty should be.

(9) Texaco's evidence includes an Archeological Site Map (Texaco Exhibit 2) which shows few archeological sites in the area of the proposed Maralo well and Isopach Maps of the Brushy Canyon "D" Sand (Loving Sand) and the Bell Canyon C7 Sand (Texaco Exhibits 3 and 4). These Isopach Maps show that each of the Delaware Sands which are the primary objectives in the proposed Maralo well are continuous and extend under the 40-acre oil spacing unit which Texaco operates in the NE/4 SW/4 of Section 30.

(10) The Isopach Map of the Bell Canyon C7 Sand also demonstrates that the Maralo proposed unorthodox location is in a thicker portion of this reservoir than a standard location.

(11) A well at the Maralo proposed unorthodox location is only 40 feet from the western boundary of the NW/4 SE/4 and therefore gains a substantial advantage on the offsetting Texaco spacing and proration unit in the Brushy Canyon and the Bell Canyon intervals of the Delaware formation.

(12) Texaco testified that in order to protect its correlative rights, the proposed

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ORDER NO. R-_____

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Maralo Gold Rush "30" Federal Well No. 8 should be assessed a production penalty of 88% (12% allowable) being the footage encroachment from a standard location towards the offsetting Texaco operated tract (290 feet closer than a standard 330 foot set back).

(13) To protect the correlative rights of Texaco, an 88% production penalty (12% allowable) should be imposed on the Gold Rush "30" Federal Well No. 8 since it is 88% closer to the offsetting Texaco spacing and proration unit than authorized by Division rules.

(14) Texaco requested that any penalty be applied to the number of days in each production month because the application of a penalty to the production allowable set by Division Rules soon is diluted by the rapid decline of Delaware wells in this area and can in some cases become no penalty at all.

(15) The production penalty for the Gold Rush "30" Federal Well No. 8 should be applied to the number of days in each production month as follows:

$$\frac{12\% \text{ Allowable}}{\text{Month}} \times \text{Days in Production} = \text{Days Allowed to Produce}$$

The well's daily production will be limited to the daily pool allowable.

(16) The application of a penalty to the number of days in each production month will eliminate unnecessary well tests, will avoid inaccuracies that may occur in the utilization of other methods for the imposition of production penalties and should be approved.

(17) Approval of the proposed unorthodox location, subject to the above-described production penalty, will afford the applicant the opportunity to produce its just and equitable share of the oil in the affected pool and will otherwise prevent waste and protect correlative right.

IT IS THEREFORE ORDERED THAT:

(1) The applicant, Maralo. Inc. is hereby authorized to drill its Gold Rush "30" Federal Well No. 8 at an unorthodox oil well location 2310 feet from the South line and 2600 feet from the East line of Section 30, Township 23 South, Range 30 East, NMPM, Eddy

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ORDER NO. R-_____

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County, New Mexico, to test the Delaware formation, Southwest Forty-Niner Ridge Delaware Pool and the Nash Draw-Brushy Canyon Pool.

(2) The NW/4 SE/4 of Section 30 shall be dedicated to the subject well forming a standard 40-acre oil spacing and proration unit for said pool.

(3) The Gold Rush "30" Federal Well No. 8 is hereby assessed a production penalty of 88% (12% allowable). The production penalty shall be applied to the number of producing days in each production month and the well's daily production will be limited to the daily pool allowable.

(4) 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

KATHLEEN A. GARLAND
Acting Director

S E A L