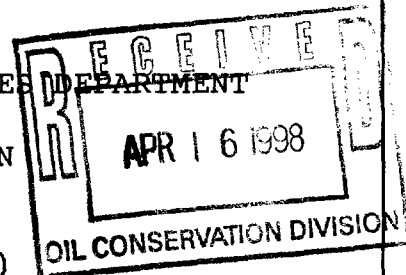


STATE OF NEW MEXICO
 ENERGY, MINERALS AND NATURAL RESOURCES DEPARTMENT
 OIL CONSERVATION DIVISION



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

CASE NO. 11,957

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

ORIGINAL

REPORTER'S TRANSCRIPT OF PROCEEDINGS

EXAMINER HEARING

BEFORE: DAVID R. CATANACH, Hearing Examiner

April 2nd, 1998

Santa Fe, New Mexico

This matter came on for hearing before the New Mexico Oil Conservation Division, DAVID R. CATANACH, Hearing Examiner, on Thursday, April 2nd, 1998, 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

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Examiner Hearing
CASE NO. 11,957

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* * *

A P P E A R A N C E S

FOR THE DIVISION:

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FOR THE APPLICANT:

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* * *

1 WHEREUPON, the following proceedings were had at
2 10:10 a.m.:

3 EXAMINER CATANACH: And at this time we'll call
4 Case 11,957.

5 MR. CARROLL: Application of Chi Energy, Inc.,
6 for compulsory pooling, Eddy County, New Mexico.

7 EXAMINER CATANACH: Call for appearances in this
8 case.

9 MR. BRUCE: Mr. Examiner, Jim Bruce of Santa Fe,
10 representing the Applicant. I have one witnesses.

11 EXAMINER CATANACH: Additional appearances?
12 Okay.

13 (Thereupon, the witness was sworn.)

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

17 DIRECT EXAMINATION

18 BY MR. BRUCE:

19 Q. Would you please state your name and city of
20 residence?

21 A. John Qualls, Midland, Texas.

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

23 A. Chi Energy, Inc., petroleum geologist.

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

1 A. Yes.

2 Q. And are you familiar with the geologic matters
3 involved in this case?

4 A. Yes.

5 MR. BRUCE: Mr. Examiner, I tender Mr. Qualls as
6 an expert petroleum geologist.

7 EXAMINER CATANACH: He is so qualified.

8 Q. (By Mr. Bruce) Mr. Qualls, are you also familiar
9 with the land matters in this case?

10 A. Yes.

11 Q. And did you handle those personally?

12 A. Yes, sir.

13 Q. Okay. What does Chi Energy seek in this case?

14 A. We seek an order pooling the northwest quarter of
15 the northeast quarter of Section 21, 24 South, 28 East,
16 from the surface to the base of the Bone Spring formation
17 for all pools or formations spaced on 40 acres.

18 Q. What is Exhibit 1?

19 A. Exhibit 1 is a land plat outlining the proposed
20 well unit. The well is in an orthodox location, 990 feet
21 from the north line, 1980 feet from the east line.

22 Q. And this is a re-entry; is that correct?

23 A. Yes, sir.

24 Q. What is the leasehold ownership of the northwest
25 quarter, northeast quarter of the section? And I refer you

1 to your Exhibit 2.

2 A. The leasehold ownership, 93.75 percent of the 40
3 acres, which is 37.5 net acres of the 40 gross, is owned by
4 Chi Energy, Inc.

5 Q. And what about the other 2.5 mineral acres?

6 A. There's a 2.5-acre unleased mineral interest
7 owned by Frank P. Atha. We seek to pool only Mr. Atha.

8 Q. Okay. Now, let's discuss your efforts to obtain
9 the voluntary joinder of Mr. Atha. You have been able to
10 contact him -- I mean, you've been able to locate him --

11 A. Yes, sir.

12 Q. -- is that correct?

13 A. We have located him in California.

14 Q. Regarding your efforts, could you go through
15 Exhibit 3 and discuss his attitude toward the oil and gas
16 business?

17 A. Yes, sir. Exhibit 3 is a -- on the first page is
18 a certified receipt where we sent Mr. Atha a certified
19 letter explaining the re-entry of the Pardue Farms 21. In
20 this letter we included an AFE reflecting the cost, asking
21 him to please participate or join in the re-entry of this
22 well.

23 Q. And that letter was refused by Mr. Atha?

24 A. Yes, sir.

25 Q. Now, he is a -- Again, he is an unleased mineral

1 interest owner; is that correct?

2 A. Correct.

3 Q. And your letter is dated March 5, 1998. Did you
4 have other contacts with him?

5 A. Yes, this was initiated -- We started talking to
6 him, oh, I believe it was July of 1997. We would call, he
7 would hang up. I've got a couple of documented phone
8 calls. January 15th of 1998 he hung up, and March 1st of
9 1998 he hung up.

10 Q. Did you try to contact him personally out in
11 California?

12 A. We hired a broker in Los Angeles that went to his
13 place of residence last Thursday, took a lease, took a
14 draft, took check, cash, just to try to tell him what we're
15 doing, how we're doing it. He wouldn't open the door. He
16 said, Go away if it has anything to do with the oil
17 business.

18 Q. And in fact, you had sent him a letter back in
19 October requesting him to execute a lease, did you not?

20 A. Yes, I sent him a draft, a lease, along with this
21 letter, back in October of 1997. This was never returned.

22 Q. That was -- And this is the last item as part of
23 Exhibit 3; is that correct?

24 A. Yes, sir.

25 Q. This was sent regular mail; is that correct?

1 A. Yes, sir.

2 Q. But he has refused to accept any certified
3 mailings?

4 A. Yes, sir.

5 Q. In your opinion, has Chi Energy made a good-faith
6 effort to obtain the voluntary joinder of Mr. Atha in the
7 well?

8 A. Yes.

9 Q. Would you please identify Exhibit 4 and discuss
10 the cost of the proposed re-entry?

11 A. Exhibit 4 is a copy of the AFE for the proposed
12 re-entry. It's a 7800-foot Bone Springs re-entry with an
13 estimated dryhole cost of \$106,500 and a completed well
14 cost of \$227,500.

15 Q. Are these costs in line with the costs of other
16 wells re-entered to this depth in this area of the county?

17 A. Yes, sir.

18 Q. Does Chi Energy request that it be designated
19 operator of the well?

20 A. Yes, sir.

21 Q. Do you have a recommendation for the amounts
22 which Chi Energy should be paid for supervision and
23 administrative expenses?

24 A. We request that \$4500 a month be allowed for a
25 drilling well and \$450 a month be allowed for a producing

1 well.

2 Q. And are these amounts equivalent normally charged
3 by Chi and other operators for Bone Spring wells in this
4 area?

5 A. Yes, sir.

6 Q. Now, was Mr. Atha notified of this hearing?

7 A. Yes, sir.

8 Q. And is Exhibit 5 my affidavit of notice?

9 A. Yes, sir.

10 MR. BRUCE: Mr. Examiner, I'd have you note that
11 my notice letter by certified mail was refused by Mr. Atha.
12 Anticipating that, I also sent the back page of that
13 Exhibit 5. I sent Mr. Atha a letter by first class mail.
14 That letter was not returned, so I presume it was received
15 by him.

16 Q. Now, Mr. Qualls, let's discuss the geology of the
17 prospect. What is the primary zone?

18 A. The primary zone is the Bone Springs first sand.

19 Q. And what is Exhibit 9 -- Excuse me, 6?

20 A. Six? Exhibit 6 is a type log of a well we
21 propose to re-enter. It's a compensated neutron formation
22 density log, scale of 100 feet equals 2.5 inches.

23 You'll notice at the top of -- We have the top of
24 the Bone Springs first sand indicated. Our structure
25 marker, which we make -- we make a map off the base of the

1 shale right there -- that's the base of the shale, which is
2 very identifiable in the area. It can be followed
3 extensively.

4 The density porosity is the dark line, the solid
5 line. The neutron porosity is the dotted line. I have
6 colored in red our net porosity greater than 12 percent,
7 and the yellow just indicates our zone of interest.

8 Q. Okay. What about water in this prospect?

9 A. We calculated this to be about 40 percent water
10 saturation.

11 Q. Is that fairly high?

12 A. Fairly high. It's borderline.

13 Q. Adds to the risk of the well?

14 A. Yes, sir.

15 Q. What is Exhibit 7?

16 A. Exhibit 7 is a structure map of the proposed
17 location and the acres that we have in the area. It's done
18 on the Bone Spring first sand marker, contour interval is
19 50 feet. The shale marker is always present, and that's
20 what we map in this zone.

21 If you'll notice, outlined in yellow is our total
22 acres that we have in this prospect. The outline in red is
23 the proposed well. The structure mapping shows a gentle
24 nose or regional dipping kind of to the southeast.

25 Q. Let's move on to your Exhibit 8 and discuss what

1 you hope to hit in this well.

2 A. Okay. Exhibit 8 is an isopach map, what we're
3 calling the Owen Mesa sand, which is the first Bone Springs
4 sand. Again, it's a contour map. Our porosity is mapped
5 on greater than 12 percent. Contour interval is 25 feet.
6 The scale is 1 to 2000.

7 The sand that we're looking for, this represents
8 a deep-water density flow, which is trending more or less
9 northeast-southwest. The production, the best production
10 in these wells, comes from the center of the channels where
11 the coarser grains are located. As you can see, the flow
12 is roughly northeast-southwest in this.

13 Q. Now, looking at this map, there's a Bone Spring
14 producer to the north. Who operates that?

15 A. Chi Energy operates that.

16 Q. Okay. And then moving slightly to the south,
17 there's a dry hole with the number 16 by it. What was that
18 well?

19 A. We re-entered that well. That was the Silver
20 Bullet Number 1.

21 The 16 in the parentheses, it was a log -- It was
22 hard to determine exactly what kind of net sand we had,
23 what kind of net porosity. And that is a dry hole.

24 Q. Okay, even though you had 16 feet of sand,
25 obviously, you need more than that?

1 A. Yes, sir.

2 Q. In looking at your map, perhaps drilling a little
3 bit to the south would actually be a better location; would
4 that be correct?

5 A. We did propose a well to be drilled in the south.
6 Then we got to looking at this. We can renter this well
7 economically. If we do make a well here, we are going to
8 drill a well due south of this one.

9 Q. What penalty do you recommend if Mr. Atha goes
10 nonconsent in the well?

11 A. Cost plus 200 percent.

12 Q. And do you believe that's justified with the
13 geologic risk for this prospect?

14 A. Yes, sir, I do.

15 Q. Were Exhibits 1 through 8 prepared by you or
16 under your supervision or compiled from company records?

17 A. Yes, sir.

18 Q. And in your opinion is the granting of Chi
19 Energy's Application in the interests of conservation and
20 the prevention of waste?

21 A. Yes, sir.

22 MR. BRUCE: Mr. Examiner, I'd move the admission
23 of Exhibits 1 through 8.

24 EXAMINER CATANACH: Exhibits 1 through 8 will be
25 admitted as evidence.

EXAMINATION

BY EXAMINER CATANACH:

Q. Mr. Qualls, this was an existing wellbore that was drilled to what depth?

A. It was a Morrow test. I don't have the exact depth with me. I believe it was somewhere around 11,000 feet, if I'm not mistaken.

Q. Was casing set in this well?

A. Yes, there is some casing in it, there's some 9 5/8 in through it. There's a bridge plug down at 7800 feet, and that's what we're proposing to go in and touch that bridge plug, clean the wellbore out and then come back up to 7300 and perforate.

Q. The interest you're pooling is 2.5 percent; is that correct?

A. Two and a half net mineral acres. It's actually 6.25 percent of the well.

Q. Okay. Mr. Qualls, in terms of actually re-entering the wellbore, do you see that as being very risky in terms of mechanically re-entering the wellbore?

A. I do. We re-entered both those wells to the north, the Zima, which is the one in green, circled in green, was a re-entry. We had little mechanical problem with that.

The Silver Bullet, which is just below it, the

1 one we discussed -- it had 16 net feet of porosity -- we
 2 had some mechanical difficulties. I know we got our tubing
 3 stuck in it, we had to go in there and wash and fish. It
 4 took about three days to get that out, at extreme cost.
 5 You just don't know till you get in there and start
 6 drilling through these plugs and start seeing what you find
 7 in the hole, as to what it's going to cost. But I believe
 8 it is a risk just to get to our objective.

9 Q. Sometimes the Division reduces the risk penalty
 10 because the well's already been drilled. Is that a real
 11 concern that you might have?

12 A. To reduce the risk penalty? No, I don't think
 13 so.

14 Q. It's not a big concern?

15 A. No, sir. I mean, we would like to get the
 16 maximum penalty if we could, but we don't have to live by
 17 it.

18 EXAMINER CATANACH: Okay. I have nothing
 19 further, Mr. Bruce.

20 MR. BRUCE: I have nothing further, Mr. Examiner.

21 EXAMINER CATANACH: There being nothing further
 22 in this case, Case 11,957 will be taken under advisement.

23 (Thereupon, these proceedings were concluded at
 24 10:26 a.m.)

25 I do hereby certify that the foregoing is
 a complete record of the proceedings in
 * * the Examiner hearing of Case No. 11957
 heard by me on April 2 1981

STEVEN T. BRENNER, CCR Steven T. Brenner, Examiner
 (505) 989-9317 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 April 6th, 1998.



STEVEN T. BRENNER
CCR No. 7

My commission expires: October 14, 1998