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March 23, 2001

HAND DELIVERED

Mr. Michael E. Stogner
Hearing Examiner
Oil Conservation Division
New Mexico Department of Energy,
Minerals and Natural Resources
1220 South Saint Francis Drive
Santa Fe, New Mexico 87504

Re: Case 12587: Amended application of Sapient Energy Corp for an unorthodox well location and (i) two non-standard 160-acre spacing units, or in the alternative, (ii) one non-standard 160-acre spacing and proration unit, Lea County, New Mexico.

Case 12605: Application of Sapient Energy Corporation for Special Pool Rules, Lea County, New Mexico.

Dear Mr. Stogner:

Enclosed in hard copy and on disc is the Proposed Order of the Division of Chevron U.S.A. Production Company and Conoco Inc. in the above-referenced cases.

As you know, these cases involve the Sapient Bertha J. Barber Well No. 12 ("Barber 12 Well") located 330 feet from the North line and 660 feet from the East line of Section 7, Township 20 South, Range 37 East, NMPM, Lea County, New Mexico. This well is at an unorthodox gas well location. The spacing unit which Sapient proposes for the well (the E/2 E/2 of Section 7) is non-standard and excludes Chevron and Conoco acreage which should be included in a standard spacing unit for it is acreage which is being drained by this well. Neither the unorthodox location nor the spacing unit have been approved by the Division. Chevron and Conoco have objected to the proposed non-standard unit.

At the March 1, 2001 Examiner Hearing, Chevron requested that the Barber 12 Well be shut in. Chevron renews that request with this letter and asks the Division to order Sapient to immediately shut in the well. Chevron requests that the Division further order that the well remain shut in until

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Letter to Michael Stogner

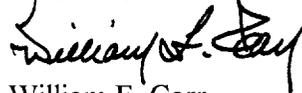
March 23, 2001

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it is in full compliance with Division Rules and that the past production from the well – which was obtained in violation of Division rules – be reallocated to the interest owners in the NE/4 of Section 7, Township 20 South, Range 37 East, NMPM, Lea County, New Mexico. Findings 18 through 21 of the enclosed Proposed Order identify the Division rules which Sapient has violated – and continues to violate – by producing this well at an unorthodox location on an unapproved non-standard spacing and proration unit.

Your attention to this request is appreciated.

Very truly yours,



William F. Carr

Attorney for Chevron U.S.A.
Production Company

cc: W. Thomas Kellahin, Esq.

Tim Denny
Abel Lobato
Chevron U.S.A. Production Company

Charlie Rule
Bruce Wiley
Rob Lowe
Conoco Inc.

**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:**

**AMENDED APPLICATION OF SAPIENT
ENERGY CORP FOR AN UNORTHODOX
WELL LOCATION AND (i) TWO NON-
STANDARD 160-ACRE SPACING UNITS, OR IN
THE ALTERNATIVE, (ii) ONE NON-STANDARD
160-ACRE SPACING AND PRORATION UNIT,
LEA COUNTY, NEW MEXICO.**

CASE NO. 12587

**APPLICATION OF SAPIENT ENERGY
CORPORATION FOR SPECIAL POOL
RULES, LEA COUNTY, NEW MEXICO.**

CASE NO. 12605

ORDER NO. R-_____

**PROPOSED ORDER OF THE DIVISION OF
CHEVRON U.S.A. PRODUCTION COMPANY AND CONOCO INC.**

BY THE DIVISION:

These cases came on for hearing at 8:15 o'clock a. m. on March 1, 2001, at Santa Fe, New Mexico, before Examiner Michael E. Stogner.

NOW, on this ____ day of March, 2001, 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 these causes and the subject matters thereof.

(2) In Case 12587, Sapient Energy Corporation ("Sapient") seeks approval of an unorthodox well location for its Bertha J. Barber Well No. 12 ("Barber 12 Well") which is located at an unorthodox gas well location 330 feet from the North line and 660 feet from the East line of

CASE NOS. 12015 AND 12017

ORDER NO. R-

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Section 7, Township 20 South, Range 37 East, NMPM, to be dedicated to a non-standard 160-acre gas spacing and proration unit consisting of either (i) the E/2 E/2 of this section, or in the alternative, (ii) the E/2 NE/4 of Section 7 and the W/2 NW/4 of Section 8 for production from the West Monument-Tubb Gas Pool retroactive to September 9, 1999, the date of first production from the Tubb formation. In addition, should the Division approve a non-standard 160-acre spacing and proration unit comprised of the E/2 E/2 of Section 7, then the applicant seeks the approval of a second non-standard 160-acre spacing and proration unit consisting of the W/2 E/2 of this section.

(3) In Case 12605, Sapient seeks the promulgation of special pool rules for the West Monument-Tubb Gas Pool including provisions for 80-acre spacing units and designated well locations.

(4) Each application addresses the same factual issues and the cases were consolidated at the time of hearing.

(5) At the hearing, Sapient requested that its application for the creation of a non-standard spacing and proration unit comprised of the E/2 NE/4 of Section 7 and the W/2 NW/4 of Section 8 be dismissed.

(6) Chevron U.S.A. Production Company ("Chevron"), the offsetting operator to the North and a working interest owner in the W/2 W/2 of Section 7, and Conoco Inc. ("Conoco"), a working interest owner in the W/2 W/2 of Section 7, appeared and presented testimony in opposition to the applications of Sapient for the creation of non-standard spacing and proration units for the Barber 12 Well. Neither Chevron nor Conoco opposed the requested unorthodox gas well location for the Barber 12 Well.

BACKGROUND

(8) The Bertha J. Barber Well No. 12 was producing as an oil well at a standard oil well location 330 feet from the North line and 990 feet from the East line of Section 7, Township 20 South, Range 37 East, NMPM, until August 1999 when it was recompleted by Cross Timbers Oil Company ("Cross Timbers") in the Tubb formation as a gas well. In September 1999, Cross Timbers filed Division form C-102 which showed the well at an unorthodox gas well location on a non-standard spacing unit comprised of the E/2 E/2 of Section 7. No application for approval of this unorthodox gas well location nor the non-standard spacing unit dedicated thereto was made pursuant to Division rules nor was notice provided to the offsetting owners who are affected by this well and the acreage dedicated thereto.

FINDING: Interest owners in the W/2 NE/4 of Section 7 were not properly notified of the proposed unorthodox well location and non-standard gas spacing unit for the Barber 12 Well as required by Oil Conservation /Division Rules and were thereby denied an opportunity to object at the time the well was recompleted in the Tubb formation.

(9) On September 20, 1999, the Oil Conservation Division's office in Hobbs, New Mexico, approved Cross Timber's Sundry Notice (Form C-103) which contained the details of its recompletion of the Barber 12 Well at an unorthodox gas well location in the Tubb formation and identified a non-standard gas spacing and proration unit for this well comprised of the E/2 E/2 of Section 7.

(10) By Order No. R-11304, dated January 6, 2000, the Division created the West Monument-Tubb Gas Pool(effective February 1, 2000), designated the E/2 of Section 7 as the acreage to be included in the new pool and approved the Barber 12 Well as the discovery well for the pool.

(11) Falcon Creek Resources, Inc. acquired the Barber 12 Well from Cross Timbers on April 1, 2000 and Sapient acquired the well from Falcon Creek on July 14, 2000.

(12) In July 2000, following the recompletion of the Barber 12 Well in the Tubb formation, Chevron unsuccessfully attempted to recomplete the G. C. Mathews Well No. 6 located in the NE/4 SE/4 of Section 6 in the Tubb formation. *Testimony of Denny*

(13) In October, 2000, Chevron U.S.A. Production Company filed an application pursuant to Division Rule 104 seeking approval of a non-standard gas well location for its G. C. Mathews Well No. 12 which it proposed to recomplete in the Tubb formation at an unorthodox gas well location 330 feet from the South line and 990 feet from the East line of Section 6, Township 20 South, Range 37 East, NMPM. This well is a direct offset to the Sapient Barber 12 Well and, like the Barber 12 Well is 330 feet from the common boundary between the Chevron and Sapient spacing units. Although Chevron's proposed location was only as close to the common boundary between the Chevron and Sapient spacing units as the Sapient Barber 12 Well, Sapient objected to the proposed location. *Testimony of Perrin.*

(15) Because of the Sapient objection, the Chevron application was set for hearing before a Division examiner. The parties were asked to attempt to resolve the issues involving the development of the subject acreage but were unable to do so and the Chevron application was set for hearing on January 25, 2001.

(16) On January 24, 2001, Sapient withdrew its objection to the Chevron application and Chevron's application was approved administratively by Division Order NSL- 3752-A dated January

24, 2001. Due to the delays in obtaining Division approval of its application for administrative approval of the unorthodox location for the G. C. Mathews well No. 12, Chevron no longer has a rig available to recomplate the well and it has not been recompleted. The Sapient well continues to produce at unrestricted rates thereby gaining an advantage on the offsetting Chevron tract impairing the correlative rights of Chevron and the other interest owners in that acreage.

(17) On January 30, 2001, Sapient filed its Second Amended Application in this matter which was set for a special examiner hearing on March 1, 2001 as Cases 12587 and 12605.

SAPIENT'S WELL IS IN VIOLATION OF THE RULES AND REGULATIONS OF THE DIVISION AND MUST BE SHUT IN UNTIL THE WELL IS IN COMPLIANCE WITH DIVISION RULES AND THE PAST PRODUCTION FROM THE WELL IS REALLOCATED TO THE OWNERS OF THE RESERVES DRAINED BY THE WELL.

(18) Division Rule 104.B(2) provides that "if a well drilled as an oil well is completed as a gas well but does not conform to the applicable gas well location rules, the operator must apply for administrative approval for a non-standard location before the well can produce."

FINDING: Sapient and its predecessors have failed to apply for administrative approval of the non-standard location for its Bertha J. Barber Well No. 12, are in violation of Division Rule 104 B(2) and are illegally producing the Barber 12 Well. The well should not have been produced and it should be immediately shut-in.

(19) The West Monument-Tubb Gas Pool is governed by the general rules of the Oil Conservation Division which provide for gas wells to be located on spacing units consisting of 160 surface contiguous acres, substantially in the form of a square, which is a quarter section and a legal subdivision of the U. S. Public Lands Survey with wells to be located no closer than 660 feet to any outer boundary of such unit and no closer than 10 feet to any quarter-quarter section or subdivision inner boundary. *Division Rule 104 C(3).*

(20) Division Rule 104 D(2) provides that "Any well that does not have the required amount of acreage dedicated to it for the pool or formation in which it is completed may not be produced until a standard spacing unit for the well has been formed and dedicated or until a non-standard spacing unit has been approved."

(21) The Bertha J. Barber Well No. 12 is at an unapproved unorthodox gas well location which is in violation of the Division Rules.

(22) By failing to properly account for and pay the other interest owners in the standard

spacing unit for the production from this well, Sapiient is in violation of the New Mexico Proceeds Payment Act.

FINDING: The Barber 12 Well is located at an unapproved unorthodox gas well location on a non-standard spacing unit in the West Monument-Tubb Pool which has not been properly formed under the rules of the Oil Conservation Division. The standard spacing unit for the well is the quarter section upon which it is located and the owners therein are entitled to their share of the production from this well. The well has illegally produced over 470 MMSCF of gas since September 1999, and is draining reserves from offsetting tracts. The well must be immediately shut in and remain shut in until the well is in compliance with Division rules and the past production from the well is reallocated to the owners of the reserves drained by the well.

LAND MATTERS

✓ (23) Chevron owns 100% of the working interest in the SE/4 of Section 6, Sapiient owns 100% of the working interest in the E/2 E/2 of Section 7. The working interest ownership of the W/2 E/2 of Section 7 is as follows:

| | |
|-----------------------------------|-----------|
| Conoco Inc. | 37.41862% |
| Phillips Petroleum Company | 25.0% |
| ARCO | 18.70931% |
| Chevron U.S.A. Production Company | 18.70931% |
| James Burr | 0.06511% |
| Larry Nermyr | 0.06511% |
| Ruth Sutton | 0.03255% |

Testimony of Rule, Conoco Exhibit A.

(24) Sapiient presented land testimony which showed that it had been unaware of the rules of the Division and the regulatory requirements for the Barber 12 Well at the time the well was purchased. Sapiient testified that prior to the acquisition of the Barber 12 Well it had “not previously owned or operated any properties in New Mexico,” that it was only after Chevron filed its application to recomplete its G. C. Mathews 12 well it “was made aware that its well was not in absolute compliance with State rules,” that it has paid 79 different royalty owners \$137,000 for production from the well, and that “Sapiient will suffer significant economic hardship if it is forced to comply with any unit, which would reduce its ownership in the well.” *Testimony of Perrin, Sapiient Exhibit No. 2.*

GEOLOGICAL EVIDENCE

(25) Sapient presented geological evidence which showed

A. the productive Tubb reservoir in the West Tubb-Monument Gas Pool extends in a north-south direction primarily located on the E/2 NE/4 of Section 7 (*Testimony of Von Rhee, Sapient Exhibits 13 and 14*);

B. a reservoir which is limited on the north by a short fault which separates the three Marathon oil wells in Section 5 from the Sapient Barber 12 Well in Section 7 (*Sapient Exhibit 13*), and

C. a reservoir which is further limited by a porosity cut off between the Barber 12 Well and the Chevron G. C. Mathews Well No. 6 located in Unit I of Section 6. (*Testimony of Von Rhee, Sapient Exhibit 14*).

(26) Although Sapient alleged there was a fault on the northeastern edge of this reservoir, it offered no evidence as to the orientation or length of the possible fault. *Testimony of Von Rhee, Sapient Exhibit 13*. However, while Conoco testified that, based on an indentation of the contours, a short fault may lie in a north-south position west of the Marathon wells, it concluded that it is unlikely that this fault isolates the Marathon wells from the Barber 12 Well. *Testimony of Wiley*.

(27) Contrary to Sapient's porosity isopach map, the data from the Barber 12 Well and the Chevron G. C. Mathew's Well No. 6 suggests similar porosity-feet in both wells. Furthermore, even if the Sapient isopach map is accepted as correct, there is significant reservoir thickness on both the Conoco-Chevron acreage in the NW/4 NE/4 of Section 7 and the Chevron acreage in the SE/4 of Section 6 which is being drained by the Sapient Barber 12 Well. Sapient Exhibit 14.

(28) The geological interpretations of Conoco and Chevron showed a reservoir with an east-west orientation which extended under the SW/4 of Section 5, the SE/4 of Section 6, the NE/4 of Section 7, and the NW/4 of Section 8. *Testimony of Wiley, Conoco Exhibits 1 and 2; Testimony of Denny, Chevron Exhibits 1 and 2*.

(29) Conoco's geological interpretation was computer generated so it should not favor either party and included more of the available data from surrounding wells than the interpretation presented by Sapient. Conoco's interpretation included a key structural control point from the Conoco Barber Federal Well No. 1 located in the NE/4 SW/4 of Section 7 which constrains the structure on the southern flank. *Testimony of Wiley, Conoco Exhibit No. 1*.

(30) Independently from Conoco, Chevron constructed a structure map of the Tubb

formation in the West Monument-Tubb Gas Pool which is similar in shape, orientation and size to the structure as mapped by Conoco. *Testimony of Denny, Conoco Exhibit No. 1, Chevron Exhibit No. 1.*

FINDING: The geological evidence presented by Conoco and Chevron is more reliable than the interpretation of Sapient for Sapient's interpretation of a north-south structural orientation for this reservoir is inconsistent with the east-west trend of the offsetting Monument-Tubb Pool to the east, is based on a limited well data set which contains no control points south or west of the Barber 12 Well (*Testimony of Von Rhee*) and skews the orientation of the reservoir to fit Sapient's north-south standup 160-acre unit.

ENGINEERING EVIDENCE

(31) In support of its request for either non-standard spacing units or for 80-acre spacing rules for this pool, Sapient presented volumetric calculations for the Barber 12 Well which showed that it should only drain 103 acres. *Testimony of Travis, Sapient Exhibit No. ___.*

(32) The engineering evidence presented by Conoco showed that the Barber 12 Well has maintained an established decline for more than a year after the fracture stimulation in December 1999 (*Testimony of Lowe, Conoco Exhibit No. 3*) and each company independently projected that gas production is declining at a consistent rate of 16% per year. *Testimony of Lowe, Conoco Exhibit No. 4; Testimony of Lobato, Chevron Exhibit 3.*

(33) Chevron presented a material balance calculation which assumed drainage was confined to 160-acres with an initial pressure of 2600 psi, and computed an ultimate gas recovery of 2.21 BCF for the Barber 12 Well. *Testimony of Lobato, Chevron Exhibit 4.*

(34) Conoco's material balance calculation considered the well as not confined to a 160-acre drainage area and honored the historic performance of the well. Conoco estimated an ultimate gas recovery for the well of 2.8 BCF. Conoco calculated a drainage radius for the Barber 12 Well of 1466 feet which is the equivalent to a drainage area of 154 acres which extends onto the Conoco acreage in the W/2 E/2 of Section 7 and the Chevron acreage in the SE/4 of Section 6. *Testimony of Lowe, Conoco Exhibit 5.*

(35) Both Conoco and Chevron used conservative assumptions in their volumetric calculations and did not consider pressure depletion prior to the recompletion of the Barber 12 Well. If pressure depletion had occurred prior to the recompletion of the Barber 12 Well, the drainage radius could have been as long as 1700 feet with a drainage area for the Barber 12 Well of 204 acres. *Testimony of Lowe.*

(36) Pressure depletion from the 470 MMSCF of gas produced from the Sapient Barber 12

Well extends beyond the current drainage radius. The impact on the ultimate recovery of oil reserves has already occurred and cannot be reversed. *Testimony of Lowe.*

FINDING: The Bertha J. Barber Well No. 12 will drain a large area in the Tubb formation and 160-acre spacing and proration units are appropriate for the West Monument-Tubb Pool.

FINDING: The Bertha J. Barber Well No. 12 has drained reserves from the SE/4 of Section 6 and the W/2 NE/4 of Section 7 and will continue to do so.

PROPOSED NON-STANDARD SPACING UNITS OR 80-ACRE SPACING

(37) Wells in the West Monument-Tubb Pool drain in excess of 80-acres and adopting special pool rules which provide for 80-acre spacing will result in the drilling of unnecessary wells thereby causing waste. *Testimony of Lowe, Conoco Exhibit 6; Testimony of Lobato, Chevron Exhibit 4.*

(38) Approval of Sapient's application for two non-standard spacing units in the E/2 of Section 7 would promote additional nonstandard spacing units and the drilling of additional wells which would accelerate production with no associated incremental production thereby causing economic waste. *Testimony of Lowe, Conoco Exhibit 6.*

FINDING: Adoption of Special Pool Rules for the West Monument-Tubb Pool which provide for 80-acre spacing or the creation of a non-standard spacing unit for the Barber 12 Well comprised of the E/2 E/2 of Section 7 will result in reserves being drained from offsetting tracts which can only be recovered by the owners of that production by the drilling of unnecessary wells.

(39) Conoco and Chevron requested that Sapient be required to form a standard unit for the Barber 12 Well and reallocate production from the date of first Tubb production from the well to the interest owners in the NE/4 of Section 7. *Testimony of Lowe, Denny and Lobato.*

(40) Conoco recommended that the production be reallocated out of future production by means of a balancing arrangement with Sapient. *Testimony of Lowe.*

(41) Formation of a standard 160-acre spacing and proration unit for the Barber 12 Well comprised of the NE/4 of Section 7 will result in the owners of this acreage sharing in the reserves drained therefrom.

(42) Failure to require Sapient to form a standard spacing and proration unit for the Barber 12 Well would permit Sapient to retain the oil it has illegally produced from the well which has been drained from offsetting acreage including the W/2 NE/2 of Section 7.

(43) The effects of the drainage which has occurred from the Barber 12 Well on the W/2 NE/4 of Section 7 cannot be reversed and the formation of a standard spacing unit for the Barber 12 Well and the reallocation of the production to the owners in this standard unit is necessary to protect the correlative rights of all owners in the NE/4 of Section 7.

(44) Sapiant testified it can reallocate the proceeds received for these reserves among the owners of these reserves. *Testimony of Perrin.*

FINDING: The reallocation of production from the Barber 12 Well to September 9, 1999, the date of first Tubb production, is necessary if all owners of that production are to receive their fair share of the recoverable reserves from the pool thereby protecting their correlative rights.

(45) Sapiant testified that it knew at the time of its objection to Chevron's proposed unorthodox well location in Section 6 that as long as Chevron could not recomplete at its proposed location it would enjoy a drainage advantage on its offsets. *Testimony of Perrin.*

(46) The delays Chevron experienced in obtaining Division approval of its unorthodox location in the SE/4 of Section 6 have prevented Chevron from recompleting its G. C. Mathews Well No. 12 while the Sapiant Barber 12 Well has been permitted to continue to drain the reservoir.

(47) Chevron has requested that the Sapiant Barber 12 Well be shut in until a standard spacing and proration unit comprised of the NE/4 of Section 7 be dedicated to the well and all Tubb production from the well be reallocated to the owners thereof. Chevron also requests that the Barber 12 Well remain shut in until it has been able to recomplete the offsetting G. C. Mathews Well No. 12 in the Tubb formation thereby enabling it to offset drainage with counter drainage. *Testimony of Denny.*

(48) The economic hardship that Sapiant claims it would suffer from this reallocation of reserves is the only result of Sapiant's illegally producing reserves which are owned by other operators in the pool.

(49) The application of Sapiant Energy Corporation in Case 12587 for an unorthodox well location for its Bertha J. Barber Well No. 12 at a point 330 feet from the North line and 660 feet from the East line of Section 7, Township 20 South, Range 37 East, N.M.P.M., should be granted.

(50) The application of Sapiant Energy Corporation in Case 12587 For approval of two non-standard gas spacing and proration units in the E/2 of section 7, Township 20 South, Range 37 East, NMPM, should be denied.

(51) The application of Sapiient Energy Corporation in Case 12605 for the adoption of Special Pool Rules and Regulations for the West Monument-Tubb Gas Pool to include 80-acre gas well spacing should be denied.

FINDING: The Barber 12 Well has been and continues to be produced in violation of Division Rules 104 B(2), 104 C(3) and 104 D(2). The operator of the Barber 12 Well should be immediately shut in the Barber 12 Well and keep it shut in until a standard 160-acre gas spacing and proration unit comprised of the NE/4 of Section 7 has been dedicated to the well and production from the date of first Tubb production has been reallocated to the interest owners in this spacing and proration unit.

IT IS THEREFORE ORDERED THAT:

(1) The application of Sapiient Energy Corporation in Case 12587 for an unorthodox gas well location in the West Monument-Tubb Gas Pool for its Bertha J. Barber Well No. 12 located 330 feet from the North line and 660 feet from the east line of Section 7, Township 20 South, Range 37 East, NMPM, Lea County, New Mexico is hereby **approved**.

PROVIDED THAT Sapiient Energy Corporation is ordered to shut in the Bertha J. Barber Well No. 12 and that the well shall not be returned to production until a standard gas spacing and proration unit has been dedicated to the well in accordance with Division Rules 104 C(2) and 104 D(2) and all production from this well from September 9, 1999 has been reallocated to the interest owner in this spacing unit or an agreement reached with all interest owners in this standard spacing unit for the reallocation of this production to the owners thereof.

(2) At the request of Sapiient Energy Corporation, its application in Case 12587 for the approval of a non-standard gas spacing and proration unit comprised of the E/2 NE/4 and of Section 7 and the W/2 NW/4 of Section 8, Township 20 South, Range 37 East, NMPM, Lea County, New Mexico is hereby **dismissed**.

(3) The application of Sapiient Energy Corporation in Case 12587 for approval of a non-standard 160-acre gas spacing and proration unit comprised of the E/2 E/2 of Section 7, and the W/2 E/2 of Section 7, Township 20 South, Range 37 East, NMPM, and the application is Case 12605 for the adoption of special pool rules for the West Monument-Tubb Gas Pool including provisions for 80-acre gas spacing and proration units are hereby **denied**.

(4) Jurisdiction of these causes is retained for the entry of such further orders as the Division may deem necessary.

CASE NOS. 12015 AND 12017
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DONE at Santa Fe, New Mexico, on the day and year hereinafter designated.

**STATE OF NEW MEXICO
OIL CONSERVATION DIVISION**

**LORI WROTENBERY
Director**

S E A L