STATE OF NEW MEXICO

ENERGY, MINERALS AND NATURAL RESOURCES DEPARTMENT

OIL CONSERVATION COMMISSION

IN THE MATTER OF THE HEARING CALLED BY THE OIL CONSERVATION COMMISSION FOR THE PURPOSE OF CONSIDERING:	CASE NO. 12,935
APPLICATION OF THE NEW MEXICO OIL CONSERVATION DIVISION TO AMEND RULES 303.B (SURFACE COMMINGLING), RULE 309.B (ADMINISTRATIVE APPROVAL, LEASE COMMINGLING), AND RULE 309.C (ADMINISTRATIVE APPROVAL, OFF-LEASE STORAGE), AND TO MAKE CONFORMING AMENDMENTS TO RULE 303.A (SEGREGATION REQUIRED) AND TO RULE 309.A (CENTRAL TANK BATTERIES - AUTOMATIC CUSTODY TRANSFER EQUIPMENT)	

REPORTER'S TRANSCRIPT OF PROCEEDINGS

COMMISSION HEARING

BEFORE: LORI WROTENBERY, CHAIRMAN
JAMI BAILEY, COMMISSIONER
ROBERT LEE, COMMISSIONER

November 22nd, 2002

Santa Fe, New Mexico

This matter came on for hearing before the Oil Conservation Commission, LORI WROTENBERY, Chairman, on Friday, November 22nd, 2002, at the New Mexico Energy, Minerals and Natural Resources Department, 1220 South Saint Francis Drive, Room 102, Santa Fe, New Mexico, Steven T. Brenner, Certified Court Reporter No. 7 for the State of New Mexico.

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I N D E X

November 22nd, 2002
Commission Hearing
CASE NO. 12,935

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E X H I B I T S

OCD	Identified	Admitted
Exhibit 1	34	77
Exhibit 2	41	77
Exhibit 3	20	77
Exhibit 4	7	77

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A P P E A R A N C E S

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* * *

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By: WILLIAM F. CARR

* * *

WHEREUPON, the following proceedings were had at 9:12 a.m.:

CHAIRMAN WROTENBERY: At this point what we would like to do is go ahead and hear Case 12,935, the Application of the New Mexico Oil Conservation Division to amend Rules 303.B concerning surface commingling, Rule 309.B concerning administrative approval and lease commingling, and Rule 309.C concerning administrative approval, off-lease storage, and to make conforming amendments to Rule 303.A concerning segregation required and to Rule 309.A concerning central tank batteries - automatic custody transfer equipment. That's a long one.

And I'll call for appearances in that particular case.

MR. BROOKS: May it please the Commission, I'm David Brooks, Energy, Minerals and Natural Resources Department of the State of New Mexico, appearing for the Oil Conservation Division.

I have two witnesses.

CHAIRMAN WROTENBERY: Would the witnesses please stand and be sworn?

(Thereupon, the witnesses were sworn.)

MR. BROOKS: Anyone else?

CHAIRMAN WROTENBERY: I don't see anybody else.

MR. BROOKS: Nobody else volunteering to appear?

CHAIRMAN WROTENBERY: No.

MR. BROOKS: May it please the Commission, I am going to ask that in this case -- My two witnesses, Mr. Ezeanyim and Mr. Foppiano, were both intimately involved in the formation of this Rule, and while each is going to testify specifically as to certain portions of the Rule, the division of responsibility for the presentation was actually quite arbitrary in the sense that it doesn't represent any difference of expertise.

Consequently, I'm going to request that while I'm examining one witness, the other witness sit at the opposing counsel table over there so that any questions the Commissioners might have over any portion of the testimony can be fielded to either of the two gentlemen, since they both have knowledge of all aspects of this Rule, if that procedure is acceptable to the Commission.

CHAIRMAN WROTENBERY: That sounds fine. I think we could take their testimony at the same time.

MR. BROOKS: Very good. At this time I will call Mr. Ezeanyim.

Do you want to sit over there? And you have a set of copies of the exhibits, do you not?

And you have a set also. Okay.

Good morning, Mr. Ezeanyim.

MR. EZEANYIM: Good morning.

RICHARD EZEANYIM,

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

DIRECT EXAMINATION

BY MR. BROOKS:

Q. Would you state your name for the record, please?

A. My name is Richard Ezeanyim.

Q. And by whom are you employed?

A. I'm employed by Oil Conservation Division, Energy, Minerals and Natural Resources Department.

Q. In what location?

A. In Santa Fe.

Q. And what is your title?

A. Chief Engineer.

Q. Now, you have appeared as an expert witness before the Oil Conservation Commission previously and had your credentials accepted by the Commission?

A. Yes, they have been.

MR. BROOKS: Okay, we tender Mr. Ezeanyim as an expert petroleum engineer.

CHAIRMAN WROTENBERY: We accept Mr. Ezeanyim's qualifications.

MR. BROOKS: Very good. I will call everyone's attention to Exhibit Number 4. It was our intention to have this on a PowerPoint presentation, however because we

didn't anticipate a lot of outside people being here as an audience, and since all the Commissioners would have a copy, we decided to do it the easy way and simply -- There are additional copies, if anybody wants them, of all of the exhibits up here.

Q. (By Mr. Brooks) Exhibit Number 4 is the summary presentation, and looking at page Number 1 of Exhibit 4, Mr. Ezeanyim, would you explain to us why the New Mexico Oil Conservation Division became interested in revising and updating our surface commingling Rules?

A. Yes, I think in the year 2000, in July, 2000, the Division Director formed a group, a work group, to look at Rules 303 and 309, because the way the Rules currently exist is very confusing.

For example, the main reason that -- There are three main reasons why this Rule has to be revised. One is, the Rule talks about liquid hydrocarbons. Liquid hydrocarbons are what people in the industry deem to be oil, and it doesn't seem that gas is involved in that surface commingling.

Q. Okay, let me interrupt you just a second.

A. Yes.

Q. In fact, in practice the Division has treated the Rule as though it applied to gas as well as oil?

A. Yeah, we have done that, even though the Rule is

different.

Q. Very unclear from the language whether that's actually the case or not?

A. That's right, and that's one of the main reasons --

Q. Okay, continue.

A. -- so we have to incorporate it.

So we needed to revise the Rule to include gas -- oil, gas, anything that is being produced in the field out there.

The second reason for revising this Rule, again, is, if you look at Number 2, is the application process. The application process currently is very confusing. You have to -- There is no specific application that an operator can pick up and fill out to apply for any surface commingling.

So in that process all they have to do is to write a letter telling us what they need to do. And it's very, very confusing to the operators.

So we developed an application form which I'm going to go through later on in the presentation, how we came up with those application forms to try to streamline the process on how to apply for surface commingling.

The third reason is that we need to simplify the Rules and streamline it so that it becomes more beneficial

to both the OCD and to the operators.

For example, if you want to apply for, say, pool commingling, you go to Rule 303, maybe 303.B. If you want to apply for lease commingling, you go to Rule 309.B, and there's no application form, and it's very confusing.

And if you want to apply for both pool commingling and lease commingling, a combination of them, you have to turn between 303 and 309, and the whole thing is very confusing.

So now, we have constructed it everything in one Rule, instead of going through 303 and 309 to get what you want before you can operate. Very confusing, very time-consuming, and it's not efficient.

Q. Interrupt again. Is it not true that the Rules 303 and 309, while they deal with different subject matters, because of the related nature of the subject matters they have various confusing cross-references between each other?

A. That's exactly right, yes.

Q. Okay.

A. So those are the main reasons. There are other reasons, you know, why we do surface commingling, but I'm just stating why we want to revise the current Rules to make it more effective and more efficient for both us and for the operators.

Q. Yeah, and one of the reasons why we wanted to simplify and streamline the process, though, is because that will make it easier to do surface commingling, correct?

A. That will make it very easy to do surface commingling.

Q. And surface commingling, in appropriate cases, furthers the goal of prevention of waste by enabling us to -- by enabling the production of oil and gas at lower cost, correct?

A. That's right. Even the present Rule and the revised Rule also encourages that.

Q. Okay. Explain to us how the Division went about formulating the proposed Rule.

A. As I said at the beginning, I think in 2000, even before I came here, the group formed to try to look into revising this Rule because of this ambiguity.

And if you look at page 2 of Exhibit 4, you can see we have the original work group. It's comprised of both members of the staff at OCD and a lot of people from industry and some lawyers and everything, and BLM. It stretches across all walks of life.

You can see, if you look at the list of the work group, who have worked really tirelessly to be able to come out with a Rule that we think is very workable and easy to

understand. I give credit to all these people who worked on this.

You can see the Oil Conservation Division, people from law firms, Bill Carr, Marathon Oil, Dugan Production, Phillips Petroleum, Yates, Conoco, Burlington, Texaco Exploration, Bureau of Land Management and Amerada Hess.

So you can see that it comprises all kinds of operators together to be able to come up with a usable Rule.

Q. Okay. And did the work group reach a consensus on the proposals that were adopted?

A. Yes, the work group reached a consensus and made a recommendation that has been the subject of the discussions today.

If you go to page 3 of Exhibit 4, this is the recommendation of this work group. The work group wants the Commission to repeal current Rules 303.B -- 303.B is the pool commingling -- and then 309.B is the administrative application, lease commingling; and 309.C, the off-lease storage and measurements; and then adopt amendments to Rule 303 and 309.

Those are the new Rules that we are talking about today, new Rules 303 and 309.

Q. Okay. And when we had gotten almost to an impasse in getting a suitable draft, did not Mr. Foppiano

save us his with his graphic skills and explain how all this was to work together?

A. Yes, that's very good. And we were very happy to have Rick with us.

Q. Okay. Well, we'll call everyone's attention, then, to pages 4 and 5, which I believe represent Mr. Foppiano's work product.

A. If you look at page 4 and 5, I love picture representations. And this is the crux of the matter, and I'm going to go through it to help the Commissioners understand the thought process in developing this Rule.

If you look at page 4, you can see the light rectangle there is -- we're talking about basic regulatory concept. The concept is segregation. I mean, there is no commingling, commingling prohibited, both pool, lease, everything is prohibited. That's the basic concept.

However, under certain circumstances you need to have some exceptions, and that's where you see all the three arrows going off. The fourth one is in green -- I'm color-blind, I don't understand, either green or blue. It's downhole commingling --

CHAIRMAN WROTENBERY: Blue-green.

THE WITNESS: Okay. Downhole commingling is Rule 303.C. And Rule 303.C is not at issue today.

Q. (By Mr. Brooks) That has recently been

extensively revised?

A. Yeah, it's been extensively revised, and that's why it's in the green color.

So you can see the other two colors now are in yellow.

One is surface commingling. And surface commingling entails lease commingling, pool commingling, pool and lease commingling.

And then you have off-lease storage and off-lease measurements. Those are the exceptions to the current basic regulatory requirements.

Now, if we look at surface commingling and off-lease storage and off-lease measurement, if you are going to do any of those, surface commingling, that commingling takes precedence over off-lease storage and off-lease measurement.

In rare circumstances do you do off-lease storage and off-lease measurement.

However, if you need to do that without commingling you could still do that. And if you look at the off-lease storage and off-lease measurement, you can see the first one, no surface commingling between different leases. So in that case, you can do off-lease storage and off-lease measurement.

And I'm going to point out as I'm going through

what are the differences between our current Rule and the new Rule that we developed. This no surface commingling is the same for both.

All production will be from the same source of supply, from the same pool, the same for both.

No intercommunication between facilities, the same for both.

However, one of the differences is Form C-107B, application form that I talked about, which I'm going to go into detail with the Commissioners on how we developed this. You need to fill out an application, Form C-107B. That's something different from the old -- I mean the current Rule.

Now, all working interests notified. There's a difference here too. The current Rule says all working interests have consented in writing that they are doing off-lease storage and measurement, but we are simplifying it down to just notify them, and then you can submit your application to OCD.

And of course you see the 20-day notice without protest requirement in both current and the new Rule.

Q. Well, let me interrupt here. In effect, I don't believe we've changed the notice requirements in the sense of what really is required as consent in writing. Either they consent in writing, or they be notified and not

protest it, and that's really --

A. Yes.

Q. -- the same as the way it currently is --

A. Yes.

Q. -- as far as the interest owners, working interest and royalty owners, correct?

A. That's correct.

Q. But as to the Bureau of Land Management or the State Land Office where they're involved, the present Rule requires that the operator have their written consent and file it with this application, correct?

A. That's correct, because we feel that BLM and SLO will take their own action before they --

Q. Yeah.

A. -- do any commingling.

Q. But now -- But under the new Rule, we will simply require that they show that they've notified those agencies, and we will allow those agencies to make their own rules in regard to how that is actually handled, right?

A. That's correct.

Q. Okay, go ahead.

CHAIRMAN WROTENBERY: Will the approval issued require BLM and State Land Office concurrence? Will there --

MR. BROOKS: That is a change that we have made

on today's draft over the one we filed, we actually filed. And that, of course -- under the draft that we previously filed, we provided that our approval would not be effective until the other agencies approve it.

After considering it again yesterday, we decided to recommend that that be deleted and we leave it simply as saying that they must be notified, and it's up to the operator to comply with their Rules. We're not intimating that we are trying to overrule either the BLM's or State Land Office rules, but neither do we feel it's necessary for us to enforce them. But of course, that's for the commission to decide.

THE WITNESS: That's correct.

Q. (By Mr. Brooks) You may continue.

A. Okay. Now, let's turn to page 5, the same pictorial representation continuing. There now, we -- if you look at page 4 we have a surface commingling, and now we're going to deal with surface commingling.

There are two situations in surface commingling, two very important situations. One is identical ownership and the second is diverse ownership. And before I talk about either of them, let me point to what we just said if BLM or SLO is involved, they have been notified in those two cases. We need to notify them and not get the consent before we issue any order.

Now after that is taken care of, let me start with identical ownership, how we treated it, and the simplifications that we did, the work group did, to make it a little more efficient from work we are currently doing.

If you look at identical ownership, first of all the State Land Office and the BLM, if they are applicable, have been notified. And under this Rule we define what is called an identical ownership, and we're going to go through that as we present this Rule to you.

So for us to make sure that the situation is truly identical, the ownership is truly identical, we require that a landman certify that the ownership is truly identical.

Q. Now, I'm going to go through this with Mr. Foppiano, but at this point, just because this concept is so critical to what we're doing with this whole Rule --

A. Yes.

Q. -- can you tell us just what do we mean when we say identical ownership?

A. What we mean by identical ownership is you have the same working interest, the same royalty interest, overriding royalty interests, and also in exactly the same percentages. That's identical ownership.

But they have to have the ownership in the same percentage to be truly identical. And we're going to go

through that as we proceed in presenting the body of the text to the Commissioners.

And what is important to make sure that so you can get a glimpse of what identical ownership -- when we use the word "identical ownership", what it means and what we're talking about.

So we need a certification from a landman saying that it's truly identical before we do what we're going to do.

Now, look at Application Form C-103. That's one of the most important things we did. There are no applications before. We want to use Form C-103. Form C-103 is the Sundry Notices and Reports on Wells. And as you see if you go to Form C-103, at the bottom there is a place for our approval.

And the work group thought that if the situation is truly identical, the only thing the operator has to do is to apply on Form C-103 with all the attachments I'm going to discuss about, and then we have about 48 hours to approve it, instead of the current 90 days or 60 days, who knows how long it's going to take?

And that is very important for the simplification of this Rule. Right now I have on my table a lot of them that are, you know, truly identical. But we can't just do what the current -- the present Rule we're presenting to

the Commission is -- what we're trying to do now. We have to wait until we issue it in 90, 60, 70 days or whenever we issue it.

But under the revised Rule that the work group worked on, we thought that once you apply on Form C-103 with all the attachments, then the Division can look at it and approve it as a sundry within 48 hours. That will really streamline the process. And if you look for that, you will see that you can attach on that Form C-103 your leases, your pools. You have to identify them, and you have to tell us your allocation methods, identify. And then the most important is your -- are those allocation methods.

We pre-approved three methods. One is metering, one is well test and the other one is subtraction method. If you look closely on those methods, if any of the wells are non-marginal, well test methods may not be considered on that. And we're going to talk about that later in the presentation.

So as you can see on this situation of identical ownership, if really the ownership is identical then the process will take place in 48 hours. So the Division here is -- It's now taking more than 90 days. We can take two days to issue that order.

So we deal with identical ownership.

Let's now turn our attention to diverse ownership. This is a little more complicated, and that's why we did a lot of work.

In diverse ownership we developed Form C-107B, as a --

Q. Now, that form as we propose to use it is Exhibit 3, correct?

A. Yeah, it's Exhibit 3, and I'm going to go through that when I finish with this --

Q. Okay.

A. -- and then give them an idea how we came up with the contents of that form.

Q. Okay, continue.

A. Okay, now you see application on Form C-107B to OCD, where you have to attach your plats, your schematics, diagrams, list of interest owners and etc.

Then you have to tell us that you've given notice to all interest owners and opportunity for hearing.

Then you have to give us the measurement methods -- and the measurement method that we really do approve here is metering method -- or any other method that the Division may approve.

And because of this measurement method, there is one addition to this diverse ownership.

If you look at the one that says OK to estimate

production of gas producing less than 15 MCF, because the metering method is very costly, if an operator is producing gas that is making 15 MCF a day and the metering method may cost more than the revenue generated, it might shut in the well. So in that case it will be okay to estimate production, if you are making less than 15 MCF a day.

This is an addition that we made to the current Rule, to make sure we take care of those wells that are making less than 15 MCF so that they're -- those wells are not shut in, because if I'm going to spend more money metering than what I get from producing less than 15 MCF, then my option is to shut it in. So we took care of that. It's one of the things that we did to streamline it.

Then on the measurement method we also provided some meter-proving frequencies for gas, for oil, and some adjustments, plus or minus two-percent adjustment. This might be onerous, but I mean because the ownership is diverse, we want to make sure we protect correlative rights, we want to make sure everybody's sharing in the production as it should be, and that's why we made this addition to the current Rule. They are not existing in the present Rule now. This is all we added to the new Rule that we are trying to develop.

So you can see the simplification here, and the whole thing is now embodied in a text that anybody can pick

up that Rule that we've developed, read through it and apply effectively to OCD. And we in OCD, we also work more efficiently in getting those orders written. So I'm very proud of the work we did to be able to present this Rule.

But this is in a nutshell. We still have to go through how we come up with most of these things.

Now --

Q. Did you want to go through the form itself?

A. Yes, the form --

Q. Exhibit Number 3.

A. -- because that's important to --

Q. First of all, why is it C-107B?

A. It's C-107B because as we thought -- Downhole commingling is C-107A, so the group thought that, well, surface commingling will be C-107B.

Q. Okay. Then if you will, go through and tell the Commissioners anything you feel that needs to be pointed about the proposed form.

A. Yes, it's important with this form we developed so that -- and as you can see, this form is not required for identical ownership, it's only required for diverse ownership. So as you can see, we identify all our four district offices there in case anybody wants to find where they are, and then the central office in Santa Fe.

We started with the operator name and then the

address of the operator, and then the type of application. What type of surface commingling is it? Pool commingling, lease commingling, pool and lease commingling combination?

And as you can see, only if not surface commingled. If it's not surface commingled you can do off-lease storage and off-lease measurement. But if you surface commingle, then those ones take precedence over those measurements.

And then you identify your lease types. Is it fee, is it state, is it federal?

Then we are going to go through the -- Is this an amendment to an existing order? Is there any order concerned with this commingling you're doing? Because it's important for us to know why. We're going to deal with it later.

Then have you notified the BLM and SLO? So those things we need to know.

Then you start with (A) Pool Commingling. You have to attach sheets if you can't get all of them on this form. You have to identify your pools and pool codes. And this is important, you have to identify the gravities or BTU of the non-commingled production and then calculate -- you have to include the calculated gravities/BTU of commingled production, and then indicate the value of

commingled production and value of non-commingled production. And then also the volumes.

This is the data we're going to use in making the approval of this surface commingling.

Let me go further, then. For pool commingling, we have to ask whether any well is producing at top allowable. In this case we're not going to allow well tests.

Has all interest owners been notified by certified mail of the proposed commingling? You have to let us know that.

Then the measurement type, because the diverse ownership -- the measurement type requires metering, or other if you could justify why you want the other instead of metering.

Now, look at number 5 question: Will commingling decrease the value of production? This is important. If you say yes, you need to justify why.

For example, let's say that the value of production will decrease. But the cost of not commingling is going to be very -- is going to be higher, you need to demonstrate that.

And that's why we put in those information there, because in certain circumstances the costs of not commingling will far outweigh the difference in that

production if you commingle.

Then (B) is the Lease Commingling. We go through the same thing that we did in Pool Commingling, measurement types and everything.

Then Pool and Lease Commingling you have to do A and E. And E, you attach schematics, a diagram of the facility including a good description and everything, so that we ensure you satisfy that this form is filled by you and send it to us.

Then attach -- and make other attachments that we need to have to approve this Application.

Q. Now, one of the reasons we are submitting -- Well, the main reason, really, we are submitting this form to the Commission at the time we're proposing this Rule is that we have some detailed provisions in the existing Rules as to what an application for surface commingling has to contain, correct?

A. That's correct.

Q. And we've proposed to remove those provisions from the Rule, but instead to reference the form?

A. Yeah, reference the form, that's right.

Q. Okay. So we're not actually asking the Commission to adopt the form as part of the Rule, other --

A. No --

Q. -- than by reference?

A. -- we are not asking --

Q. Okay.

A. -- but we want to make sure you understand what we're trying to do.

Q. We want the Commissioners to understand what's happening to the detailed requirements that are being repealed from the Rule?

A. That's correct.

Q. Okay. Before we go on to Mr. Foppiano, is there anything you would like to add?

A. Yes, I would like to add -- Go to page 7. I would like to talk more about the basic regulatory concept. I mentioned it in my diagram. Now, we are now starting the basic development of the Rule. I mean, the basic Rule says if you have a pool it has to be to be segregated, and if you have production you have to segregate -- when you transport, it has to be segregated. So the basic requirement is segregation.

However, if you -- under certain circumstances where -- on page 8, exceptions to the Rule, to the basic requirements, exceptions to the Rule. and there are a lot of reasons for exceptions to the Rule. We're going to go into detail with the next witness, is that, first of all, we are charged with preventing waste, interests of conservation, protect correlative rights, which are

incorporated into this Rule, and even some environmental issues.

For example, if you don't commingle and all these tank batteries are scattered all here and there and there's a lot of spill, that would be an environmental issue.

So there's a lot of things you look into, to be able to talk about surface commingling, and which will serve your environmental issues, will serve saving money and protect correlative rights and prevent waste. And under those circumstances we could grant exceptions to the Rule.

Q. Okay. Now, on page 7 it points out that the Rule provides two things, that pool segregation is required -- that is, the production from each pool, even if it comes from the same lease or sometimes from the same well if it's not downhole commingled --

A. That's correct.

Q. -- is required to be separated -- and production from different leases is required to be separated.

Now presently, Rule 303 deals with pool segregation, correct?

A. That's right.

Q. And Rule 309 deals with --

A. -- lease --

Q. -- lease segregation?

A. That's correct.

Q. Under the new Rule, both of these are incorporated into -- the general Rule that segregation is required for both pools and leases is incorporated into our proposed Rule 303.A?

A. A, yes, 303.A.(1) and A.(2).

Q. Okay. And then the authority to grant exceptions to either is delineated in 303.A.(3)?

A. That's correct. That could be found as page 1.

Q. Okay. Now, I think you made a good statement of the reasons why exceptions should be granted, and it's my understanding that we are going to have Mr. Foppiano discuss the definition of lease, if we're ready to go on with that -- to that, or is there something else we need to do first?

A. No, we can --

Q. Okay.

A. -- unless there is questions.

MR. BROOKS: Okay. Honorable Commissioners, at this point I'm ready to go on to the portion of the proceeding that Mr. Foppiano -- the portion of the discussion I'm going to go through with Mr. Foppiano.

Obviously I will be happy to tender Mr. Ezeanyim for examination by the Commission at this time, or we can go through the rest of the presentation and then tender

both witnesses, whichever the Commission please -- whichever suits the Commission.

CHAIRMAN WROTENBERY: Why don't we go ahead with Mr. Foppiano's testimony --

MR. BROOKS: Okay --

CHAIRMAN WROTENBERY: -- and get the whole picture, and then --

MR. BROOKS: -- very good, and --

CHAIRMAN WROTENBERY: -- we can --

MR. BROOKS: -- then if I can ask --

CHAIRMAN WROTENBERY: -- ask questions?

MR. BROOKS: -- Mr. Ezeanyim and Mr. Foppiano to change places here --

MR. FOPPIANO: Sure.

MR. BROOKS: -- so you will be closer to the honorable reporter.

CHAIRMAN WROTENBERY: Mr. Brooks, do you consider Mr. Foppiano a hostile witness?

MR. BROOKS: No. In this case -- without estopping myself to assert that in some future case, in this case I think Mr. Foppiano is a friendly witness.

(Laughter)

CHAIRMAN WROTENBERY: Okay.

MR. BROOKS: However, since this is an uncontested proceeding, I hope you won't be too hard on me

if I ask him some leading questions.

(Laughter)

RICHARD E. FOPPIANO,

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

DIRECT EXAMINATION

BY MR. BROOKS:

Q. Good morning, Mr. Foppiano.

A. Good morning.

Q. State your name for the record, please?

A. My name is Richard E. Foppiano.

Q. And by whom are you employed?

A. I'm employed by OXY in Houston, Texas.

Q. And in what capacity?

A. I am a senior advisor of regulatory affairs.

Q. No, you told us yesterday that you are a registered professional engineer.

A. I'm a registered professional engineer in Texas, yes, in petroleum engineering.

Q. Now, you are an expert in both regulatory affairs and petroleum engineering, correct?

A. Knowledgeable, I don't like to ever consider myself as an expert because I think I'm always learning.

MR. BROOKS: Well, everybody else considers you as such.

(Laughter)

Q. (By Mr. Brooks) Have you testified before the New Mexico Oil Conservation Division -- Commission, before and had your credentials accepted?

A. Yes, both.

MR. BROOKS: Okay, we will tender Mr. Foppiano as an expert witness on regulatory affairs and petroleum engineering.

CHAIRMAN WROTENBERY: Despite Mr. Foppiano's modesty, we'll accept his qualifications as an expert.

(Laughter)

MR. BROOKS: Very good. Having qualified you as an expert in petroleum engineering and regulatory affairs, the first thing I'm going to examine you about is a land question.

(Laughter)

Q. (By Mr. Brooks) Mr. Ezeanyim explained to us that there are two separate provisions in the current Rules with regard to commingling. One prohibits commingling production from separate pools, and the other prohibits commingling production from separate leases. Now, is the word "lease" defined anywhere in the New Mexico Oil Conservation Division's Regulations as they presently exist?

A. Not to my knowledge.

Q. Not, certainly, in any of the provisions that deal with surface commingling, correct?

A. That's correct.

Q. Now, the New Mexico Oil Conservation Division has a procedure of assigning names and numbers to what they call leases, correct?

A. It's my understanding, yes.

Q. Now, one would thus assume that if the term is used without definition, and even though it obviously doesn't mean exactly the same thing that a landman would mean by the term "lease", that when we use the term "lease" in the present Rules, that it refers to the leases as the names and numbers of leases that are assigned by the Division, correct?

A. That's one presumption that could be made --

Q. Yeah.

A. -- but there are others in this --

Q. There's nothing in the Rule that says that?

A. Exactly.

Q. And it's not at all clear, given the fact that it wouldn't make sense -- Well, a reading of the Rule would indicate that a lease is a geographical area?

A. Yes.

Q. Whereas to a land person a lease is a document, and there may be one lease or many leases that cover a

particular geographical area?

A. Correct.

Q. Okay. So one of the things we undertook to do was to come up with a definition of "lease" that used it in the way that we wanted to use it for purposes of this Rule, correct?

A. Correct. Yes, the work group felt that it was beneficial to define "lease" for the purposes of this Rule so everyone operated on the same understanding of what commingling was between leases and what commingling wasn't between leases.

Q. Now, I prepared a very complicated definition of "lease" which was included in our previous draft that was filed during the notice period, correct?

A. Yes.

Q. And earlier this week we decided that -- Mr. Ezeanyim was kind enough to find an error that I had to admit was very significant in my complicated definition, so we decided to scrap that and do a very simple definition, right?

A. Right, but I think it still addresses the same concept that was intended by the work group.

Q. Okay. How do we define "lease" in the present draft?

A. Well, the present draft defines "lease" as an

area of common ownership that is specific --

Q. Hold on one second, I'll call everyone's attention to page 2 of Exhibit 1. That's 303.B.(2).(a) of the draft Rule.

Okay, continue.

A. The lease, as defined in the proposed revision basically is a geographic area. It's common ownership -- actually identical ownership is what we've said there, and it's specific to a pool. So anywhere there is that identical ownership throughout that geographic area for one pool, that is considered to be one lease.

And where there are multiple pools or there is any diversity of ownership, then that's where it becomes separate leases. And what's important there is, that's where the Rule operates to require exceptions for lease commingling. And if it's on the same lease then it is obviously not an exception to the Rule for commingling separate leases.

Q. Now, I will call your attention to the words "zones or strata" which appear on the fourth line of that Rule.

Generally we've steered away from using those terms in OCD Rules because geologists always argue about those things, and we define pools, and we have a feeling that for regulatory purposes a pool is a pool, whatever

some -- daring interpretation some geologist may have.

But we had a particular reason for putting that terminology in this particular point in the Rule. Can you explain what that was?

A. Yes, it's just to cover the probably small number of cases where there is a change in ownership within a pool that was created by lease instruments, farmout agreements, whatever, and so that there would be a diversity of interest, even though the wells that were producing from that pool would be producing from the same pool and producing from the same lease, but because they were producing from different strata within that same pool and there was a difference in ownership between that strata, there will be a difference in ownership in that production, and that sets that up to be production from two leases which would require an exception to Rule 303.

Q. For example, is it not fairly common in farmout agreements to have a provision that the party who drills the well earns to the deepest depth penetrated by the well or some number of feet below that depth?

A. Yes, that's common.

Q. And if you have a formation like the Morrow in the southeast that has numerous productive strata within the formation, it may well be that the well penetrated the Morrow but didn't go all the way through it, correct?

A. Correct.

Q. And so you might have a situation where the farmee owns a portion of the Morrow as to a particular tract of land, but the farmor still owns the portion below that?

A. Correct.

Q. And if that were the case under this definition, then those two portions of that one pool would be a different lease --

A. If our lease --

Q. -- for purposes of this Rule?

A. Yes, the whole concept is, there again, where there is identical ownership in the same geographic area and --

Q. Right.

A. -- within the same pool, that is a single lease. But where there's any diversity, then that -- the Rule operates to create different leases, so that an exception is required.

Q. And following through that ownership requirement, it would also be true, would it not, that there are some instances in which two or more leases -- that is, two or more properties that have specific names and lease numbers in the OCD records, would actually be considered one lease, so it wouldn't be necessary to apply for an exception for

surface commingling; is that not true?

A. That's correct. The definition does allow for two contiguous -- what might be considered by land people to be separate leases.

Q. Or it might be the separate leases under the OCD's classification system as it currently exists?

A. Correct. But because that ownership is identical between those two contiguous areas and within that pool, then those two contiguous leases can be considered as one lease for purposes of this Rule.

Q. And of course it's necessary that all ownership, not just the working interest, be identical for that purpose?

A. All ownership, and as we'll see in a few minutes, the work group also actually created a definition for identical ownership so there was no confusion about what is identical ownership.

Q. But the effect -- Yeah, well, Mr. Ezeanyim talked about that, and we'll go over it again. But the effect is, for instance, with state leases -- the State owns a lot of land and they carve it up in various parcels for leasing purposes -- it's quite possible that there might be two state leases held by the same party, adjacent to each other, producing from the same pool, they're leased on behalf of the same beneficiary fund, and those would be one

lease under this definition?

A. Yes.

Q. Okay. I've probably tired everybody by so many questions about leases, about the lease definition, but -- and you have, once again, with your artistic talents, Mr. Foppiano, you have prepared a series of pictures to illustrate the definition of a lease. So I'm going to ask you to go through those and explain them to the honorable Commissioners.

A. Okay, I just wanted to lay out a couple of pictures that convey what the work group was intending with the definition of "lease". The first example, on page 11, is the basic example. It's shown in yellow. It's a geographic area, and it can be a single lease. The ownership is identical throughout this geographic area, or it could actually be, as we discussed before, multiple leases that are contiguous to each other, but the ownership is still identical with respect to this entire area. And so that would be considered a single lease, and production from wells in the same pool within this geographic area would not require an exception to Rule 303 if it was going to be commingled.

On page 12 is another example, same geographic area, but just further showing where we might have spacing units, pooled units, communitized units within that

geographic area. There again, production from those different units within that geographic area, as long as it's in the same pool, would allow -- would not require an exception to Rule 303 if it was going to be commingled before it left this lease.

And then on page 13 is another example of how the lease definition operates. Here we have Lease A and Lease B, and we can consider Lease A to be owned by different owners or different percentages from Lease B. So Lease A and Lease B are not identical ownership between the two.

And portions of Lease A and Lease B are contributed to a spacing unit that is then pooled or communitized. And the way the lease definition would operate is, it would actually create in this instance three leases. There would be production from wells in the same pool within the spacing unit or pooled unit, and then there would be production from wells outside of that spacing or pooled unit that are on Lease A, and then production from wells that are outside of that spacing unit and on Lease B. And to commingle any of those would require an exception of Rule 303, as long as they're -- I mean, if they're producing from the same pool.

And then another example on page 14 is just a secondary or enhanced recovery unit. That's a geographic area of common ownership throughout, so this just makes it

clear that production from wells in the same pool within that area can be commingled without the need for an exception to Rule 303.

Q. Now, some of those units are quite large, correct?

A. Correct.

Q. But the entire unit, since all the ownership of the production is common -- even though the ownership of the various tracts within the unit is not -- since the ownership of all the production is in common, it would be the same lease, correct?

A. Correct. And I'd also point that if the unit covers multiple pools, then because the Rule is written in such a way that it only applies to a single pool, the commingling of production from different pools, even within this unit, would require an exception to Rule 303.

Q. Yes, even if you're on the same lease, you've got to have OCD permission to commingle between pools?

A. Correct.

Q. Okay, go ahead.

A. And then the last picture, on page 15, is just an example of a federal exploratory unit, one that provides for participating areas, such that the ownership would be different within that participating area, as opposed to inside the federal exploratory unit, and the lease

definition would be that those participating areas are actually separate leases inside of that federal exploratory unit.

And so to commingle production within the PAs with production outside of the PAs, or even between the PAs, would all require an exception to Rule 303 as a lease commingling exception.

Q. Very good. Now, the definitions of diverse ownership and identical ownership appear as subdivisions (b) and (c), and I get all wound up when I try to keep track of what subdivision is called a subsection, what's called a paragraph, what's called a paragraph and so forth, so subdivisions (b) and (c) of B.(2). I went over those concepts with Mr. Ezeanyim, so I think I will skip over those at this point, unless there are questions, and go on to the -- From this point on, we will be going through these slides which have summaries, but we will also be going through the Rule section by section.

And in addition, I will call the Commission's attention to Exhibit Number 2 where I have attempted to summarize those portions of the Rule which appear to be changes from the existing Rules.

And it was the intention to have the description of the changes in black and the Division's rationale for those changes in red. However, because of timing we had to

print these on a black-and-white printer, so the rationale appears in a separate paragraph but not a different color.

Anyway, these three exhibits will be considered in conjunction in the rest of the presentation.

Once we get past the definitions -- Well, before we do that, we've already talked about the change with regard to notification of the BLM and the State Land Office, correct?

A. Correct.

Q. And so I won't go over that again. That appears -- The new provision, because it applies regardless of the ownership, whether it's identical or diverse, that new provision is a portion of 303.B, which begins on page 1 and continues -- 303.B.(1), the introduction, which begins on page 1 of Exhibit 1 and continues over onto page 2. And the specific provision with regard to the BLM and the State Land Office, which is different substantively from the existing Rule, appears as subdivision (b) of B.(1) on page 2 of the proposed draft Rule.

Now let us look at page 17 of Exhibit 4 and page 2 of Exhibit 1, where we talk about identical ownership.

A. Yes.

Q. Now, the procedure that is provided for surface commingling exceptions and identical ownership is significantly changed from the way it works under present

Rules, correct?

A. Yes, and if I could expand on that a little bit --

Q. Please do.

A. -- the work group, when we sat down and tried to identify how surface commingling should work, we started getting hung up fairly easily on lease-lease commingling, pool-pool commingling, pool-lease commingling, and as we worked our way through that what became evident -- and this became evident when we worked with it visually -- were that the requirements, regardless of whether we were pool-pool commingling, lease-lease commingling, whatever, really diverged when the ownership issues became different between the commingling situations.

So that's kind of where we had a breakthrough in looking at this surface commingling. The regulatory approach to surface commingling was that it really divides itself on the ownership issues, and not the lease-lease, pool-pool. Those are just basically commingling situations.

So what we ended up with was, we took the Rule and broke it down to commingling situations involving identical ownership and commingling situations involving diverse ownership. And the diverse-ownership commingling situations in large part reflect current OCD practice, is

my understanding, with respect to how -- the allocation methods and everything and the process. It's all pretty much the way it is done today, with some changes. But the intent was to really capture most of what that regulatory approach was already.

On identical ownership, since we felt like that's where more flexibility could be allowed in terms of allocation procedure and process, that's where we really streamlined the whole regulatory approach, was on the identical ownership.

So as we go through these next couple exhibits, you'll see the regulatory approach contained in the proposed Rule changes for identical ownership, and then you'll see it for diverse ownership. And we think that really, that breakdown helps guide industry people to look at their situation and decide under which set of rules and provisions do they fall under.

Q. Now, we have dealt with identical ownership in B.(3)?

A. Yes, B.(3) lists out the process and the regulatory requirements, including the allocation methods that are pre-approved when the commingling proposal involves only identical interests.

Q. And everything from where (3) starts on page 2 of the draft Rule, over to where (4) starts on page 4 of the

draft Rule deals with identical-ownership situation, right?

A. That is correct.

Q. Now, explain to us what allocation methods are authorized for identical ownership.

A. The three somewhat industry-standard allocation methods that are authorized specifically under identical ownership are use of well tests, use of meters, and what's called the subtraction method.

And those are -- We try to capture in the text in the Rule any limitations that might apply to, for example, well-test allocations. For example, you can't -- That's not applicable when top-allowable wells are involved or there's proration.

And also it describes how subtraction method works, and should work for the purposes of the Rule. So it's fairly detailed. And then it has the metering requirement in there, set out.

So the intent was to describe the methods to pre-approve them, and then describe what is exactly intended in that pre-approval.

Q. Now, without going into engineering detail that a lawyer wouldn't understand, the well-test method means simply that you test each well and determine how much it can produce, and then you allocate the total production among the various wells by assuming that each one

contributed in proportion to its productive capacity, correct?

A. Exactly.

Q. And you conduct those tests periodically so that you can determine if there have been changes in the capacity of particular wells to produce?

A. Yes, uh-huh.

Q. Now, explain to us what the metering method of allocation is and why that's different from separate measurement of each production stream.

A. Well, the metering allocation method involves the metering of oil and gas from each individual well before it is commingled, and so you have continuous metered numbers, and those are then used to allocate back a master metered volume that is read either at a LACT meter or a central sales point for gas wells.

Q. And what you're actually doing is, you're crediting the production to the various wells based on taking the stream that flows from the outflow meter and allocating that based on the readings of various inflow meters, which for some reason that I don't understand aren't the same. The total of the inflow meters and the amount on the outflow meters doesn't ever come out to be the same.

A. Yeah, there's good and valid reasons why it's not

the same, which I can go into if you want me to, but --

Q. Well, I think we don't need to --

A. Okay.

Q. -- I think we can accept that without detailed presentation.

Now, we have a provision (iv) on the bottom of page 3 that authorizes the Division to consider other methods. Why is that in there?

A. That's just a catch-all provision that presumes that as we go forward there might be new technology or new methods that are arrived at to -- and appropriate for the circumstances that a particular operator has, that they can be used for allocation.

And so that is a catch-all provision. It says if you want to use anything other than what is pre-approved in the Rules for your allocation, then tell us what it is and why it addresses -- how it addresses the basic requirements to accurately determine the production.

Q. Now, the methods that are specifically approved in the Rules, these are methods that are being routinely approved by the Division through the exception process currently; is that correct?

A. That is my understanding. Richard may agree or disagree.

MR. BROOKS: Well, then I will turn to Mr.

Ezeanyim. Is that a correct statement?

MR. EZEANYIM: Yes, that is a correct statement.

Q. (By Mr. Brooks) Okay. Well, there's nothing in the present Rule that says an operator has a right to use the well-test method or the subtraction method, but normally it's being approved as of the way things are being done now?

A. There is some discussion in Rule -- I think it's 309 -- about well-test allocation and when it cannot be used. So it is mentioned in the Rules, but --

Q. Well, yeah, and generally we're not authorizing it -- 309 deals with lease commingling, correct, primarily?

A. Yes.

Q. And we're not authorizing the use of well-test method in lease commingling, correct?

A. When there is identical ownership --

Q. Well, I mean, sorry --

A. -- yes.

Q. -- well, but lease commingling -- commingling between leases, by definition, is going to be where there's not identical ownership, right?

A. Correct.

Q. Or unless they're noncontiguous --

A. Unless they're noncontiguous, yes.

Q. -- there could be -- I'm sorry, I stand

corrected. There could be noncontiguous leases.

Okay, but where there's diverse ownership, the well-test method is not authorized unless the Division otherwise orders?

A. Yes, that's correct.

Q. Okay. And it's also not authorized where you have to determine the production from particular wells in order to determine whether or not they're producing in accordance with their allowables, correct?

A. Where there is proration or top-allowable production --

Q. Right.

A. -- or wells capable of producing top allowable, well-test method is not pre-approved --

Q. Right.

A. -- which is, from my understanding, consistent with the current approach if an operator files an application today requesting well-test allocation with diverse ownership or top-allowable wells involved, the Division, I believe, sets it for hearing and does not automatically approve it or --

Q. What is the reason why we would allow more -- why we would be less rigorous with regard to the allocation method and allow more different alternatives to the operator with the identical ownership, versus diverse

ownership?

A. I think the primary reason is the correlative-rights issues that are involved. When you have diverse ownership, there are good and valid reasons to inquire in detail as to how the commingling will be done, so that the interests of all parties are protected.

Whereas in the case of identical ownership there is not that concern, so there's just more or less -- There's just a lesser need for that stringent and detailed inquiry.

Q. Basically, where you're not dealing with diverse ownership of the various streams and where you're not dealing with seeing if wells meet their proration allowable, the allocation of the production stream is for statistical purposes; there's not really any other reason for it, correct?

A. Correct.

Q. And we believe that a less rigorous treatment is appropriate where the data is for statistical purposes only?

A. Correct, that's what the work group recommended.

Q. Okay, then I am going on to page 4 of Exhibit 1, page 2 of Exhibit 2, but still on page 1 of Exhibit 4. Make sure everybody's on the same page -- or on the same pages, I should say.

Subdivision (b) of B.(3) deals with the procedure for a surface commingling application with identical ownership. Could you describe the procedure provided and tell us wherein it's different from the procedure under the existing Rule?

A. My understanding, the procedure under the existing Rule is irrespective of whether it's identical or diverse ownership.

Q. Well, that's not entirely true, I believe, though, because under diverse ownership you have to give notice to everyone, whereas with notice it's not currently required under -- while there's identical ownership. I believe that to be the case.

MR. EZEANYIM: That's right.

THE WITNESS: I stand corrected.

Q. (By Mr. Brooks) I stand corrected if I'm misreading the Rules, but that's my understanding. But the application is the same, and the data required are the same.

A. Okay.

Q. Okay, so could you go ahead and tell us what the new Rule -- what the proposed Rule is?

A. The proposed Rule is a very slimmed-down version of the process that involves just filing a sundry notice. The operator files a sundry notice, and as Richard

mentioned, he identifies where the commingling is going to occur in terms of leases and pools, he identifies the allocation method that is going to be used to determine the production between those various leases and pools, and -- with the appropriate limitations there. And as long as it's a pre-approved method, there's no additional evidence required about the allocation method.

Then the identical ownership situation has to be certified to by a licensed attorney or qualified landman for the operator, and then any evidence that the State Land Office or BLM has been notified, if they are an interest owner in the proposed commingling.

Q. Now, there are a bunch of things required under the existing Rule to be included in the application that would not be required under this proposal, correct?

A. Yes, that's correct.

Q. Such as a schematic diagram of the facility, certifications as to the specific gravity of the production stream, et cetera, et cetera?

A. Yes, there's no need to submit detailed data for the different pools and leases about the production and the quality of the production and the volume of production, there's no need to economically justify the proposed commingling.

And so there's several requirements that are in

the existing Rules that have been eliminated for identical ownership.

Q. For instance, the present Rule provides that there has to be a demonstration that the value of the combined production stream will not be less than the value of the contributory streams, correct?

A. Yes, that's --

Q. And that's for the prevention of waste?

A. Correct.

Q. However, it wouldn't be very smart for an operator dealing with common ownership to combine streams and reduce their value when he doesn't own any larger interest in one than another, correct?

A. There could be some situations where there is a small reduction in the value of the stream, but that small reduction is far offset by the savings in consolidating facilities, so it's still economically justified to do it.

Q. Correct. And if there weren't a greater savings some other way, they wouldn't do it?

A. Correct, there's a presumption that the operator will act in his own self-interest, and that's to the benefit of all parties in the identical-ownership situation.

Q. The work group concluded that the market system will work in this instance?

A. Yes.

Q. So there's not a need for detailed regulation.

COMMISSIONER BAILEY: Question.

MR. BROOKS: Yes.

COMMISSIONER BAILEY: You just made the statement that it was in the interest of all the working interests?

THE WITNESS: In the interest of all the owners.

COMMISSIONER BAILEY: All of the owners?

THE WITNESS: Yes.

COMMISSIONER BAILEY: However, do you believe that's true for the royalty owners?

THE WITNESS: Yes, I do, if the ownership is identical.

COMMISSIONER BAILEY: To see a reduction in the value of the production?

THE WITNESS: It could be -- There again, it would be probably a rare situation, but if the value of the production was reduced, say, over -- the net present value of which, we'll say $10,000 over a five-year life, but because of the consolidation of facilities the production of those wells was extended for more years, then the extension of that production may translate into a net present value, even at the reduced amount of say $20,000.

So it's in the best interests of all to actually go ahead and do that commingling. It's technically and

economically justified.

COMMISSIONER BAILEY: That's all the questions I have.

THE WITNESS: Thank you.

Q. (By Mr. Brooks) I believe Mr. Ezeanyim explained adequately the certification by a licensed attorney or petroleum landman, that ownership is identical, so I won't go over that again.

I want to go -- well -- Yeah, I want to go ahead now to the provisions with diverse ownership. This is covered --

CHAIRMAN WROTENBERY: Mr. Brooks, would this be a good time to take just a short break?

MR. BROOKS: Sure.

CHAIRMAN WROTENBERY: Okay, that would be helpful. Thank you.

MR. BROOKS: I'm in favor of that.

CHAIRMAN WROTENBERY: Okay.

(Thereupon, a recess was taken at 10:20 a.m.)

(The following proceedings had at 10:35 a.m.)

CHAIRMAN WROTENBERY: Okay, I think we're ready to get started again.

Q. (By Mr. Brooks) Very good. Mr. Foppiano, during the break we took a look at the present Rule in regard to the notice provisions, correct?

A. Correct.

Q. And while the present Rule's complexity is such that we may have to defer making a final answer on that subject -- And of course the document speaks for itself, as we attorneys always say. Unfortunately, it doesn't speak very clearly. But it would appear to be that the present Rule requires notice to all interest owners wherever there is commingling between two or more leases, but does not require notice where there's commingling between two or more pools on the same lease; is that a fair summary?

A. Yes.

Q. Okay. But we're not entirely sure that that is in accordance with the way the Rule is currently being administered. We believe that there may be some tendency to not require notice where there's identical ownership, but we're not entirely sure of that, right?

A. It has become abundantly clear to me that the Rule is very ambiguous about those issues.

Q. Okay. Well, I agree with that. Let us continue.

We're now going into diverse ownership, which is covered in -- I believe it is paragraph 303.B.(4), which begins at the bottom of page 4 of Exhibit 1 and continues to the top of page 8 of Exhibit 1. So it's a fairly lengthy discussion there that we have of this subject matter. Also it is covered on pages 2 and 3 of Exhibit 2,

summarizing the changes, and on page 19 of Exhibit 4. Okay.

In the case of diverse ownership, what method of allocation is provided?

A. Diverse ownership is, of course, where the proposal focuses the regulatory process on numerous items, the most important of which, obviously, is the allocation process. And it only authorizes one process of allocating between wells when there's diverse ownership, and that is metering.

Q. Okay. And is that because that's the most accurate method?

A. That is the most accurate method. I think everyone would agree that that's the best way to ensure that the correlative rights of all owners in the production are protected, is by metering the individual streams.

Q. Now, once again, although the present Rule, as in so many places, is not entirely clear, that is a continuation of current practice?

A. That's my understanding, yes.

Q. Next we have a provision in subparagraph (b) called Meter Proving Frequencies. It appears on page 5 of the draft Rule. That is a new provision, correct? There's no provision about that subject in the existing Rule?

A. Yes, that's -- There's no provision. It may be

contained in the manual, and the Rule references the manual, but what the intent was here by the work group was to clearly set out -- because metering is so important to accurately determine the production from the individual wells and diverse ownership situations, that we decided it was prudent to set out some restrictions or some requirements for improving the accuracy of the meters involved in the allocation.

And for oil, as you can see, there's a requirement for frequency of proving that oil production meter, based on the throughput through that meter. And there is a similar requirement for gas meters, to prove those based on the volume of throughput.

And then there is even a meter-proving standard, an accuracy standard that is set out in the Rule of two percent, such that if the meter-proving and calibration tests reveal an inaccuracy of more than two percent, then the volumes have to be corrected back since the last allocation or the last meter-proving that was done. And it goes without saying that every time the meter is proved, the meter factor will be adjusted to accuracy, 100-percent accuracy. But this just says where it's more than two percent, there will actually be a correction of volumes that have been filed previously.

Q. Now, these requirements are in accordance with

what the Bureau of Land Management requires for federal leases, correct?

A. That's my understanding, is that they are consistent with requirements of other jurisdictions, and consistent with industry practices of sales meter and accuracy standard for sales meters.

Q. Okay, and it's not customary for the attorney to testify, but this is a rule-making proceeding so we'll be a little informal. I would state that my experience in private practice reviewing gas contracts, that these provisions are essentially very similar to and is related to gas essentially in the same language that's customarily used in gas purchase and sale contracts.

You mentioned the manual, and I will digress in a minute to ask you about that. There are a number of references to the manual on surface commingling in the present Rule. We have deleted all those references, correct?

A. Yes, the work group felt that the manual was a very outdated document and was not widely known in industry. And as a result, they felt it was very good to go ahead and eliminate references to the manual and put the things that should be required -- just go ahead and put those in the Rule.

Q. Indeed, just observing the work group

discussions, I detected a rather high degree of hostility toward that manual.

A. Yeah, it's -- I would agree with that.

Q. And basically that's because it hasn't been revised and kept updated with industry changes; is that --

A. My understanding is that it is at least 30 years old and maybe longer.

Q. Okay, so we're just eliminating all references to the manual?

A. Yes.

Q. Now, Rule 303 -- or subparagraph 303.B.(4).(c) is a new provision. Now, that is a technical provision in essence, is it not, this low-production gas well?

A. Yes, it's -- Essentially, we put this requirement in here, or this statement in here, because under diverse ownership there's a strict requirement to meter. However, in Rule 403 of the Division's Rules, there is an opportunity to get an exception to directly metering wells, based on the fact that they're very low-volume wells.

And so what we tried to do was to capture that same concept that was described in Rule 403.B, we captured that here in this. So it was clear that even though the Rule requires metering, it does not require metering where there are these very low-volume gas wells, consistent with Rule 403.

Q. And the reason -- Well, if we didn't have this subparagraph (c) there would be an inconsistency between Rule 403 and Rule 303; is that correct?

A. Yes, that's my opinion.

Q. And is the reason for this provision that it just doesn't justify the cost to have the separate metering facilities for a well that has that lower production?

A. Yes. In fact, I have some personal experience with it in other areas where we get down to these very low volumes, and the cost of maintaining a meter can outweigh the volume derived from the well and actually -- an oil well with very low amounts of gas.

But if a meter is required, an orifice meter is required, and somebody has to be paid to go pull the chart and then the chart has to be integrated to determine the volumes and so forth and so on, that whole monthly cost can exceed the value of the production from the well and cause the well to be prematurely plugged.

So this provision allows for an estimation of production to occur, to maintain production on those very low-volume wells in that case.

COMMISSIONER LEE: Low volume well, what's the wellhead pressure?

THE WITNESS: It could be very, very low, and probably would be if there was an opportunity -- if it had

a high wellhead pressure but very low volume, I would presume there would be a reason to -- I mean an opportunity to install compression. But it may be that the line pressure is very low, and so it's very low volume and compression is not justified.

COMMISSIONER LEE: So metering is not accurate anyway, measurement of pressure?

THE WITNESS: In all honesty, Dr. Lee, I'm not sure if an orifice meter will accurately measure 15 MCF a day or not. That is a very low volume for an orifice meter to measure, and when we get into the low-volume ranges, as you well know, the accuracy gets very suspect anyway.

COMMISSIONER LEE: So are you an expert on this?

THE WITNESS: Oh, no. Knowledgeable, though.

Q. (By Mr. Brooks) Now the next subparagraph, 303.B.(4).(d), on page 6 of the draft Rule -- actually it goes page 6 through the top of page 8 of the draft Rule -- covers the procedures for lease commingling with diverse ownership. Could you describe those generally?

A. Yes, I'll just run down those pretty quickly. Obviously, where there's a diversity of ownership there has to be an application filed on C-107B, and that application, as Richard described, has numerous requirements to it. There is an inquiry into the value of the production, the amount of production, the quality of production, the pools

that will be commingled, what allocation method is going to be proposed, and an economic justification and a variety of things that's pretty consistent with the current requirements in that situation.

And then there's also notice to all interest owners, and here again this is clarifying all these notice issues and the fact that it applies regardless whether there's lease-lease commingling, lease-pool commingling or pool-pool commingling.

And then in subparagraph (iii) there, the notice that is required says that there's 20 days allowed for an opportunity to protest by those receiving notice, and that if there is no protest then the Commission can approve it administratively.

There also is a provision for a hearing in the case of a protest or if the OCD or the Division decides that a hearing is prudent, given the application has been submitted.

There's also a provision that allows that when there is the operator or applicant is unable to locate all of these different parties that have an interest in production, that a publication can suffice for those parties that direct notice can't be given to, and there's a description of how that publication will occur.

And there's a provision that discusses the effect

of a protest, which essentially says that even though somebody says they're going to protest, if they don't show up at the hearing and effectively protest, then the Division can consider the application as an unprotested application and process it accordingly.

And then there is another paragraph related to additions that provides an operator the opportunity to request as part of his application that the order authorize the addition of other leases and pools and -- under certain restrictions, without notice to the entire universe of interest owners and the whole commingling operation, only notice to those that are going -- in the lease or pool that will be added to the commingling facility.

Q. Okay. Now in general terms -- that is to say, notice to owners, an opportunity to protest, administrative approval if they don't protest, opportunity for a hearing if they do -- that's basically the same way the Rule currently works, correct?

A. Yes.

Q. But there are some changes, and I want to go through the specific changes -- You've gone through them all, but just to point out that they are changes.

In the first place, the present Rule uses the phrase "notice to owners of the leases", and that's somewhat ambiguous as to what owners are involved, and we

have specified specifically what is actually the current practice, what OCD requires -- that is, notice be to all royalty owners, overriding royalty owners as well as working interest owners, right?

A. We attempted to be very clear on who should be given notice.

Q. Now, the present Rule does not have any express provision for notice by publication where you have unlocatable owners. It probably can be inferred, but there's nothing in the Rule that says that that can be done?

A. That's my understanding, yes.

Q. Whereas the new Rule does provide for it specifically.

Now, the -- you mentioned this provision of the effect of the filing of a protest. We've put in a procedural provision which is covered in subparagraph (vi) on page 7, which so far as I know is unique to the OCD Rules, although if the operators have their way those provisions may become more common in the future, that says in effect that if someone files a protest but they don't appear at the hearing, or they appear at the hearing and don't offer any evidence, then the operator does not have to present any evidence other than the application itself; is that correct?

A. That's correct.

Q. Okay. Now why do we do that?

A. Well, I think it's just to eliminate people who protest without a good reason, eliminate the effect of that kind of a protest on delaying an application by utilizing the hearing process where the hearing process really wasn't necessary. So I think it is just trying to make the process work efficiently, when there is a protest that is not really prosecuted in such a way as to communicate anything other than a slowdown, or attempt to slow down the process of approval.

Q. Now with regard to additions, this paragraph (vii) at the bottom of page 7 and continuing on page 8, you described that in general terms, but it's a fairly complicated concept, so I want to go through it in a little bit more detail.

First of all, how it originated, and this was a comment that was made by Dugan Production Company and apparently something they were very concerned about. What they were saying as I understood it was, We have a lot of situations where we have commingled facilities and we keep adding new wells to them, and it costs a lot of money to have to notify all the owners of the production commingled facility every time we add an additional well. Now -- So they said, Well, why can't we just notify the new people

that are being added on?

Is that a correct description of the concern that led to this Rule?

A. Yes, it is.

Q. Okay. But I expressed a concern that the interests of the existing owners in the production being commingled could be diluted and that as a matter of due process they had a right to have notice and an opportunity for a hearing before they were subjected to that dilution. And we attempted in this Rule to address both those concerns, right?

A. Yes.

Q. And as I take it, the present Rule does not apply to any existing orders, because they wouldn't have this provision in them?

A. I don't know if there are orders out there that don't provide for additional leases, but I don't think that it's in the current Rules.

Q. So generally speaking, if you want to add additional leases where you have a current commingling order, if you want to add additional leases to it, you're going to have to give notice both to the people that are currently being commingled and to the new people?

A. I would have to speculate as to that's how the Division currently processes those. Richard may know

better.

Q. Well, I'm not sure how they currently process them, but I'm talking about how the Rule reads, what would be under this proposed Rule? That would be the effect. This 303.B.(4).(d) -- B.(4) -- I'm sorry, this 303.B.(4) --

MR. EZEANYIM: (vii)

Q. (By Mr. Brooks) -- B.(4).(d).(vii) would not apply unless the order itself had a provision in it that specifically authorized additions --

A. That's correct.

Q. -- further leases. But if it has such a provision and the additional lease is being added to the facility under the terms that are delineated in the order, then they would not have to give notice to those people who are on the stream that's currently being commingled under that order, correct?

A. I would guess they would have to give notice, whatever is required in the order, when those leases are added, and whatever the order says.

Q. But they wouldn't have to give notice to the people that were involved in the adoption of that order, because they already had notice at the time they got the order, and they could have objected to having that provision for additions put in that order if they had wanted to at that time?

A. Here again, you're asking me about the orders, Mr. Brooks, and I'm not aware of the orders that authorize additional leases and pools to be added to commingling --

Q. But such orders are authorized under this -- I'm talking about if you get an order that's authorized under subparagraph (vii) and then subsequently come in and want to add to that order.

A. I apologize, I thought you were asking me about existing commingling orders.

Q. No, no.

A. If you're --

Q. No.

A. Okay, yes. Under this proposal, future commingling orders would authorize under certain conditions -- in other words, advance notice to all the interest owners that such additional authority is being requested, and then also that the commingling is within the defined parameters that are originally granted in that order, then those leases and pools could be added with notice only to the interest owners on the new lease or the added lease or pool.

Q. And if those people that -- when they first got that order that contained those provisions for additions, if those people felt that they didn't want to be subject to further additions, then they could object at that time and

present their reasons for not wanting to be -- to have that provision in the order?

A. Correct. And I think the thing that protects them most of all is the requirement in here that it must be within the defined parameters of the Rule. For example -- I mean, the defined parameters that are already set out in the order.

For example, if the commingling involves gas-well gas and -- produced from multiple wells that have diverse ownership and the operator has that commingling authority by virtue of an order issued under this Rule, and it has that additional -- that language that allows for the addition of pools and leases, and he wanted to subsequently propose to add oil wells to that commingling operation, that would be outside the defined parameters because that's a different situation, that's a different quality of production.

Or if he wanted to use a different allocation method for that production from the added lease, that would be outside of the defined parameters.

So as long as it is within what is described in the order in terms of allocation and the conditions under which the commingling will occur, then the order would allow that lease to be added with notice only to those parties owning an interest in production in the new lease.

Q. Very good. Now, before I go on to subsection C and D, I want to call your attention to one other technical provision that's in this Rule, and this is back on page 1 in subsection -- or in paragraph A.(3). The last sentence is a savings clause that preserves, in effect, all existing surface commingling orders?

A. Yes, it essentially grandfathers all existing surface commingling orders that have been issued before.

Q. And that was put in there to make clear that even though we're adopting a new Rule and the new Rule prohibits surface commingling without an exception, that we're not attempting to repeal the existing orders that are in force?

A. Yes, that's the intent.

Q. Okay. Now, on page 8 of the draft we next refer to subsection C, which is downhole commingling, and that subsection is to be unchanged, correct?

A. Correct.

Q. We won't deal with that in this proceeding.

Now we go to subsection D which deals with off-lease storage and measurement. Now, this can be a very confusing concept, so could you explain what off-lease storage and measurement -- what that's all about?

A. Well, the basic regulatory requirement is that the production must be measured in a facility on the lease from which it's produced before it leaves the lease.

Q. And that's true even if it's not commingled, right?

A. Correct. And this entire provision covers noncommingled production. Commingling has nothing to do with this production, whether you're off-lease storage or off-lease measurement.

But this just covers situations where an applicant or operator desires to measure that production and separate it and store it at a facility that is not on the lease on which it is produced, and my understanding is, this authority is quite rare.

MR. BROOKS: Yes, let me turn, if I may, with the Commission's indulgence, to Mr. Ezeanyim to comment on that.

Mr. Ezeanyim, in practice does the Division often receive requests for off-lease storage and maintenance that do not also involve surface commingling?

MR. EZEANYIM: We do not. Very rarely do we receive those. Most of the applications we receive, we have one form of surface commingling involved with it, and no matter when we get that, then that surface commingling takes precedence, like I said in my presentation, over off-lease storage, off-lease measurements.

Q. (By Mr. Brooks) Okay. But because this is provided in the present Rule and we're not intending to

make substantive changes, we kept this provision in here, correct? Where we can authorize off-lease storage and maintenance without surface commingling?

A. (By Mr. Foppiano) Correct.

Q. Now, basically it's unchanged from the existing Rule, right?

A. That's my understanding. There's not much change.

Q. But there are a few differences?

A. Yes.

Q. And one of the differences is that in this case we require notice only to the working interest owners, right?

A. Correct.

Q. Once again, the existing notice provision says owners of the lease, which is ambiguous, in my mind at least, whether it means working interest owners or whether it means additional owners. But we felt like the notice to the more numerous parties that are often involved in royalties and overriding royalties, were not -- the cost was not justified where there's not been any commingling, correct?

A. Correct.

Q. Okay.

A. In addition to that, the existing Rule requires

notice to the purchaser, and that's been eliminated.

Q. Right, it requires consent of the purchaser --

A. Correct.

Q. -- does it not? And that's also -- that provision is being eliminated. We couldn't figure out for sure why that provision was in there, right?

A. (Shakes head)

Q. Okay. Now we are repealing Rules 309.B and 309.C because those Rules cover the subject matter that is now addressed in the proposed amendments to Rule 303, correct?

A. Correct.

Q. But 309.A, what is presently Rule 309.A, deals with another subject matter that is not addressed in the proposed amendments, right?

A. Correct.

Q. And what is that subject matter?

A. That is the authorization to utilize lease automatic custody transfer equipment.

Q. And presently that Rule is entitled Common Tank Batteries, Automatic Custody Transfer Equipment, right?

A. Yes.

Q. And we propose to -- since we're deleting everything in 309 that doesn't deal with automatic custody and transfer equipment, we're proposing to change the title of 309 to simply automatic custody transfer equipment?

A. Yes.

Q. Now we also made a modification of the initial sentence, or initial paragraph, of Rule 309, correct?

A. Correct.

Q. And in doing so we made one substantive change, and that was that the existing Rule 309.A provided that common tank batteries could not service more than 16 proration units?

A. That's correct, yes.

Q. And we're taking that provision out so that there's not a limitation on how many proration units the Division can approve, right?

A. Yes, we did that to avoid any potential conflict with Rule 303, as proposed.

Q. Plus in the present state of the art and the industry, is there any real reason why you should limit a common tank battery to 16 proration units?

A. I'm unaware of any.

Q. Very good. Is there anything you would like to add, Mr. Foppiano, since we've been through the entire Rule?

A. Nothing other than my thanks to all the members of the work group that slugged through this process for over two years to arrive at what I think is a very good product, a very simplified and a very clear rule proposal,

and my hat's off to them. There were a lot of people that worked very hard to get where we are today, including yourself, Mr. Brooks.

MR. BROOKS: Well, thank you. We would like to add our appreciation to you, and of course to all of the industry members that contributed to this process.

Is there anything you would like to add, Mr. Ezeanyim?

MR. EZEANYIM: Nothing except to thank Rick and the work group members that helped make this a reality today.

MR. BROOKS: Very good. Now, I do not know what the Commission's pleasure in this would be. If we were in court I would tender in evidence Exhibits 1 and 2 and offer Exhibits -- 1 and 3 and offer Exhibits Numbers 2 and 4 as demonstrative aids, since they're really my work product, mine and Mr. Ezeanyim's, and they're not really evidentiary; they just explain what the other exhibits are about. But I will defer to the Commission's pleasure in how we state the offer and the acceptance of these exhibits.

CHAIRMAN WROTENBERY: I think under the circumstances it would probably be easiest just to admit all four exhibits --

MR. BROOKS: Very good, then I --

CHAIRMAN WROTENBERY: -- as evidence.

MR. BROOKS: -- will tender Exhibits 1 through 4.

CHAIRMAN WROTENBERY: And they're admitted.

MR. BROOKS: Mr. Carr didn't object.

MR. CARR: No objection.

CHAIRMAN WROTENBERY: Mr. Carr didn't even enter an appearance, so I don't know if he can object.

(Laughter)

MR. BROOKS: He has no standing.

MR. CARR: Think about it.

CHAIRMAN WROTENBERY: Actually --

MR. BROOKS: Very good, I will pass my witnesses.

CHAIRMAN WROTENBERY: Okay, Commissioner Bailey?

COMMISSIONER BAILEY: I have a statement to make.

In general, I believe everyone is aware of the fact that at the Land Office we have always supported streamlining processes, opening up communication, enhancing communication with operators, the industry, and enjoying inter-agency cooperation in all of our regulations concerning the oil and gas industry.

I am dismayed today to hear the opinion that that inter-agency cooperation that we've had is a divisive misapprehension of enforcing each other's rules. It's my opinion that that is far from what the effects have been.

At the staff level and at the upper management

levels we have always had good communication between the OCD and the Land Office. And in fact, even in unit approvals, our approval at the Land Office is contingent upon approval of the OCD and the BLM for all units that are approved.

I would suggest that that be the process between the two agencies for approval of commingling -- either surface, downhole, off-lease, whatever -- because I would hate to see a rule put into effect where an operator is thrown into the position of having approval from one agency and disapproval from another agency over this type of application, and it is very apparent that more of those opportunities are going to arise for conflicting approvals. That is why I support many of these provisions for streamlining and making this more of an efficient process.

But I cannot support any part of this Rule that destroys the communication and the cooperation between the agencies.

That's all I have to say on that.

CHAIRMAN WROTENBERY: Thank you. Let me just ask a couple of follow-up questions, and I don't know who best can answer these. But first of all, I was a little bit surprised to see that there wasn't a representative from the Land Office on the work group. Can somebody explain how that happened, because --

MR. BROOKS: Well, I don't --

CHAIRMAN WROTENBERY: -- historically we have had Land --

MR. BROOKS: I don't really know who --

CHAIRMAN WROTENBERY: -- Office representation, I believe --

MR. BROOKS: I'm sorry.

CHAIRMAN WROTENBERY: -- in these kinds of discussions, but --

MR. BROOKS: Neither Mr. Ezeanyim nor I was employed by the Division when the work group was assembled --

CHAIRMAN WROTENBERY: Uh-huh.

MR. BROOKS: -- so... Mr. Ezeanyim?

MR. EZEANYIM: Yeah, and when we came on board I had a list that was supplied to me that -- the work group started on this. So I began on that work group and even acquired more from the industry, people who want to -- But I didn't know initially why SLO wasn't included in the original work group.

CHAIRMAN WROTENBERY: Okay. Did we send copies of the proposal to the Land Office?

MR. EZEANYIM: No, we sent it to all -- the only people we sent it -- The proposal of this Rule?

CHAIRMAN WROTENBERY: Uh-huh.

MR. EZEANYIM: No, we didn't.

CHAIRMAN WROTENBERY: Have we had any feedback from the Land Office that --

MR. EZEANYIM: No, we didn't have any feedback.

CHAIRMAN WROTENBERY: Okay. I believe the way the Rule was published, we would have required notice of these applications to the Land Office. Did it say anything about the OCD approval being --

MR. EZEANYIM: Yes.

CHAIRMAN WROTENBERY: -- contingent upon the Land Office and BLM approval?

MR. BROOKS: It did in one place, and -- In fact, when I was drafting I intended that to be the case, although I think I did not get it in, in both places where it should have been provided.

But our intention at the time we drafted that draft was that our approval should be contingent -- that we would not necessarily postpone our approval process, as the present Rule contemplates, until they had approved, but that our approval would be contingent on theirs and that our approval would not be effective unless and until their approval was also given.

I think the contrary view that was expressed this morning that is in the present draft was a result of changes made yesterday.

MR. EZEANYIM: That's right.

CHAIRMAN WROTENBERY: And could you repeat again the justification for that change that was made yesterday?

MR. FOPPIANO: I think it was really just a recognition that whatever approvals the operator needed to get for the commingling operation, be it BLM, SLO, OCD, that he would have to get those. And regardless of whether the OCD approved it, if the State Land Office had an interest in it and the State Land Office didn't approve it, then his commingling operation wasn't approved.

So it was really -- It wasn't an attempt to affect any difference of the approvals that are given, or -- It was an attempt to come up with a more streamlined process that affected the same thing, which is, all three agencies, if they had an interest, approved the commingling operation.

But I'm sensitive to what Commissioner Bailey is referring to. I think it was really just a -- you know, there was a perception that if the OCD's approval was contingent upon State Land Office and BLM approval, then before the operator would be able to commence the commingling operation, he would then have to get something from the BLM/State Land Office in writing and then communicate that to the OCD, which would then, you know, suffice for that consent before there was an actual --

maybe an order issued or an approval of a C-103 or something like that.

So it was really just an attempt to streamline the process and not circumvent any reviews or whatever, but...

And the same was true with the BLM. The BLM was initially involved in the work-group process, and I think they dropped out later on because they -- What they wanted in the Rule, as I understand it from the work-group members, they basically wanted their Rule codified into the Rule 303.

And since we couldn't get there and we didn't want to codify federal requirements in every situation, basically came up with a rule that satisfied the OCD's requirements for process and oversight. And then if you needed BLM approval for your commingling operation, it was presumed that you would have to give the notice, they would have to issue that approval regardless of what the OCD did.

So I think it was a last-minute idea to -- what we thought was a streamlining, particularly in the situation of identical ownership, that maybe we stepped a little too far out there and pushed the envelope.

MR. BROOKS: Yeah, I --

MR. EZEANYIM: It's --

MR. BROOKS: Go ahead, Mr. Ezeanyim.

MR. EZEANYIM: Excuse me. It's not that we did that, and I don't think it's -- In any case it's not our intention, Commissioner Bailey, to exclude the SLO or anybody.

First of all, I talked to somebody in BLM. Of course I didn't talk to anybody in SLO, because I think we have been working together. Everything we do, we think we are doing with SLO. But BLM, I talked to somebody in BLM. He said yes, if we approve something the operator is not going to do anything until they approve it.

So that's why we didn't want to make our approval contingent -- That's why we made our approval contingent on BLM or if, for that matter, SLO approval, any way you approve surface commingling or these kind of things, so that even if we approve it, the operator would not do anything until they get those approvals from BLM, or from SLO for that matter.

We are not trying to excommunicate SLO from our process, we are trying to make sure that if you have, for example, the process -- unless you want to dedicate it to us, we could do that. But I think you have a process as a royalty interest owner, how you approve most of these things before even they commingle or do any -- for that matter, any work on the -- as a royalty owner.

So it wasn't our intention in developing this

Rule to exclude or not work with SLO or, for that matter, BLM.

BLM, I think -- even though the worker -- I think he left, and they couldn't come to the meeting, but they told me when I talked to them, This is what we're doing, we are trying to make our approval contingent on you, the BLM, approving this. Well, they say, yeah, we have to do that. We have to do it because we also have to approve if the well is on some BLM land, federal land, they have to approve it too.

So that's why we did that.

CHAIRMAN WROTENBERY: Thank you, Mr. Ezeanyim.

Mr. Brooks, Mr. Foppiano had indicated that there was some concern that if we included language in the OCD commingling orders that indicated that the approval was contingent upon BLM and SLO approval, that that would require some additional coordination by the operator with OCD to submit --

MR. BROOKS: Yeah.

CHAIRMAN WROTENBERY: -- some kind of verification that that approval had been obtained. Is that really the way those contingency provisions operate? Because we --

MR. BROOKS: That was not the way I understood it when I wrote it. Now, there may have been some such

concern.

It would seem to me, though, that we could put in, very easily put in a conditional provision that would not involve any additional administrative burden. It would simply say that our approval, even though given, is not effective unless and until -- I think that would be an easy change to make in the present draft.

CHAIRMAN WROTENBERY: Sounds like maybe that would address everybody's concerns.

MR. BROOKS: It's coming back to me how this arose now, because we were going over the draft yesterday in order to try to eliminate errors. And one of the errors that existed was that the published draft had such a provision with regard to the identical ownership procedure, but it did not have a corresponding provision with regard to the diverse ownership procedure.

CHAIRMAN WROTENBERY: Okay.

MR. BROOKS: And instead of putting that provision in the diverse ownership procedure, we took it out of the identical ownership procedure.

CHAIRMAN WROTENBERY: Okay.

MR. BROOKS: Okay?

CHAIRMAN WROTENBERY: Okay. I think what we can do, then, is put back in some clause that conditions the --

MR. BROOKS: Yeah, I think there may have been

some concern that it would require an additional administrative burden, but I don't really see any particular reason why it should require an additional administrative burden.

CHAIRMAN WROTENBERY: Okay.

MR. FOPPIANO: I'll just offer that there was in the existing Rule some inconsistency on the BLM and SLO notice requirement.

MR. BROOKS: Well, that's what I was just saying. I thought there was an error in the way the previous draft was drafted, that we put it in one place and not in the other, and I think we were all agreed that it either should be in both places or it should be out both places?

MR. FOPPIANO: Yeah, I was talking about the existing Rule.

MR. BROOKS: Yeah -- Oh, okay, you were talking about the existing Rule --

MR. FOPPIANO: Yeah.

MR. BROOKS: -- not the filed draft?

MR. FOPPIANO: Exactly.

MR. BROOKS: Okay.

CHAIRMAN WROTENBERY: Okay. Commissioner Bailey, do you believe that your staff needs some additional time to review this proposed amendment?

COMMISSIONER BAILEY: I would like to see a

revised draft that includes the language that Mr. Brooks -- and then I could give it to my staff to look at.

CHAIRMAN WROTENBERY: Okay.

COMMISSIONER BAILEY: -- because there are other areas within this draft order that I think merit consideration by OCD and by us.

CHAIRMAN WROTENBERY: Okay. Okay, well, we can do that.

MR. BROOKS: Certainly.

CHAIRMAN WROTENBERY: Any other questions?

COMMISSIONER BAILEY: No, that's all I had. Thank you.

CHAIRMAN WROTENBERY: Did you have any questions?

COMMISSIONER LEE: I'm thinking about it.

CHAIRMAN WROTENBERY: Oh, Steve, go ahead.

MR. ROSS: If you're ready for me. I have some technical questions.

MR. BROOKS: Okay.

MR. ROSS: On page 7 --

MR. BROOKS: You're talking about the draft Rule --

MR. ROSS: The draft rule, yeah. And I think it's B.(4).(d).(vii) in the draft --

MR. BROOKS: That's B.(4).(d).(vii), okay.

MR. ROSS: (vi), Effect of Protest.

MR. BROOKS: Okay, (vi).

MR. ROSS: This is the provision that was discussed a little earlier that provides that if someone filing a protest in one of these applications doesn't appear at the hearing, that the application can be granted by the Hearing Officer without any kind of an additional evidentiary presentation.

MR. BROOKS: Correct.

MR. ROSS: And I don't know who to look at because I don't know who's going to answer this question.

MR. BROOKS: Well, since it's a legal question I imagine it's more likely to be me, but go ahead.

MR. ROSS: I have a little concern about this type of provision, were it to apply to a Commission hearing, because on appeal you'd need more than -- in most cases, than would be supplied along with the Application.

MR. BROOKS: I hadn't thought about that, but yeah, I can see that if it is applied in the context -- if this protester comes in and then the Hearing Officer grants the application and then the protester *de novo*'s to the Commission, if this were invoked at the Commission level it arguably would be a violation of the statute which gives them a right to a *de novo* hearing before the Commission.

So I can certainly see that argument, and there probably needs to be some qualification put in there for

that reason.

MR. ROSS: Well, and I think the provision that excuses the applicant from presenting evidence at a Commission Hearing might be subject to attack on appeal as lacking substantial evidence or having some sort of a problem with the legal residual rule or something like that.

MR. BROOKS: Yeah, I can see that could also be an argument. I think it would probably be best that this just simply not apply in the event of a *de novo* application to the Commission.

MR. ROSS: Okay.

CHAIRMAN WROTENBERY: I had a question on that particular provision too. As I read this language, it's a little bit different than the procedure that we use on occasion where we issue a notice indicating that we'll take a case under advisement if --

MR. BROOKS: In the absence of objection --

CHAIRMAN WROTENBERY: -- nobody shows up to object.

MR. BROOKS: -- correct.

CHAIRMAN WROTENBERY: Right.

MR. BROOKS: It is different from that.

CHAIRMAN WROTENBERY: Because in that case, I think we take it under advisement based on the application

submitted --

MR. BROOKS: Correct.

CHAIRMAN WROTENBERY: -- if nobody appears in opposition.

MR. BROOKS: Right.

CHAIRMAN WROTENBERY: This would indicate that even if somebody appeared in opposition, if they didn't have their own witnesses and their --

MR. BROOKS: If they didn't offer any evidence --

CHAIRMAN WROTENBERY: -- own evidence, then they wouldn't even have the opportunity to cross-examine the applicant's witnesses. And I'm wondering if -- Because I do believe that happens frequently, that --

MR. BROOKS: It happens --

CHAIRMAN WROTENBERY: -- an opposing party or a concerned party will appear and at least cross-examine the applicant's witness --

MR. BROOKS: Yes, I would say --

CHAIRMAN WROTENBERY: -- or witnesses.

MR. BROOKS: -- it happens occasionally.

CHAIRMAN WROTENBERY: Okay.

MR. BROOKS: It happens probably most frequently in compulsory-pooling cases --

CHAIRMAN WROTENBERY: Okay.

MR. BROOKS: -- in my experience.

CHAIRMAN WROTENBERY: Is there a reason to preclude that opportunity in the surface commingling cases?

MR. BROOKS: I guess the concern is, of the people who advocated this provision, that that forces the applicant to put on their case, whereas if that were not -- if that provision -- under this provision, if the protester did not offer any evidence, the applicant could simply rest on their application and wouldn't have to offer any witnesses. I guess that's the justification that would be offered in support of it.

Now, whether this due-process problem -- and with that, there may be. I can't say absolutely there's not.

MR. FOPPIANO: If the language there, "present evidence", was eliminated and it just addressed if the protesting party didn't show up at a hearing --

MR. BROOKS: Well, I think that -- clearly, that would not be a due-process problem with that provision. Now, I can see that -- Part of due process is the right of cross-examination, so I can see that if we would permit the Application, which essentially is hearsay, to stand as evidence that the person came at the hearing and said, I want to cross-examine the witnesses who are supporting this application, I can see that a due-process argument would -- a certainly non-frivolous due-process argument could be made in that case.

CHAIRMAN WROTENBERY: Okay, thank you.

Go ahead, Steve.

MR. ROSS: Okay, and my next technical question pertains to the very next paragraph, the additions.

MR. BROOKS: Yes.

MR. ROSS: Is there going to be evidence presented along with the application that supports the additions at the time of the original application? Is that the idea?

MR. BROOKS: I think there would have to be, because the provision for additions is a part of what -- it must be sought in the application and provided in the order, and normally when you seek something in an application and ask the Division to include it in an order, there's a presumption that you have to present some evidence supporting what you want.

MR. ROSS: So you have a plan that might include subsequent expansions of your gathering system or whatever it is --

MR. BROOKS: Correct.

MR. ROSS: -- that you can see at this point you've just presented.

Now, what if somebody protests that initial application and a hearing is held and then an order is subsequently entered? This seems to say that once the

operator comes in and says, I'd like to do this now --

MR. BROOKS: Yeah.

MR. ROSS: -- I'd like to add these sections, that the folks who protested and brought it to hearing wouldn't be entitled to notice.

MR. BROOKS: I would assume that would be true the way I think it's contemplated to work, because the protester gets their opportunity to protest that provision for additions at the time that the initial order is entered.

And of course if that initial order is entered over their protest, then they have the right to take it to the Commission at that time and to appeal if the Commission affirms it.

And if they have lost, and the provision for additions is put in over their objection and either they don't appeal or they don't prevail on appeal, then they would not be entitled to another bite at the apple, so to speak, when the addition is actually requested.

MR. ROSS: Okay, so I read that right?

MR. BROOKS: Yes, you did, sir.

MR. ROSS: Another -- and I apologize for bringing all these things up now, I've been so busy I didn't have a chance to look at this before.

MR. BROOKS: Oh, no problem.

MR. ROSS: Exhibit -- I think it's Exhibit B is the new form?

MR. BROOKS: Exhibit 3.

MR. ROSS: Oh, Exhibit 3. Isn't this going to require a modification to Rule 1107?

MR. BROOKS: Probably.

MR. EZEANYIM: 1107?

MR. BROOKS: Yeah, the forms portion of the --

MR. ROSS: Forms portion of this.

MR. BROOKS: Yes, I believe that -- it probably will. I believe that it will.

MR. ROSS: Okay. We're going to do that subsequently. I don't think we can do it in this proceeding, because we haven't --

MR. BROOKS: We didn't notice it, yes. That's my mistake. But now that you mention it, I think you're probably right.

CHAIRMAN WROTENBERY: What would be the nature of the revision?

MR. ROSS: Well, the 1100 series of Rules describe the forms.

CHAIRMAN WROTENBERY: Uh-huh.

MR. ROSS: They kind of mirror the provisions in other parts of the Rule that require you to submit an application or something, and then 1107 describes the

application, and in some cases --

CHAIRMAN WROTENBERY: Is this a new -- I was thinking of this as a revision of an existing form, but is this a new form?

MR. EZEANYIM: It's a new form.

CHAIRMAN WROTENBERY: Brand-new form?

MR. EZEANYIM: It's a brand-new form, yes.

CHAIRMAN WROTENBERY: Okay.

MR. ROSS: So we may need to take care of that too --

CHAIRMAN WROTENBERY: Okay.

MR. ROSS: -- just for consistency.

Okay, I know I had one more question.

CHAIRMAN WROTENBERY: I'll ask one while you're thinking about that.

The new definition of "lease" -- Thank you for doing these diagrams. That helps us understand what it is that you're describing here and how it would play out in practice.

I do have a question for you about the effect, if any, of this new approach to the term "lease" on the production reporting requirements. Operators are required to report production by well. Would this definition of "lease" and the way it's used in the new surface commingling Rule have any adverse effect on an operator's

ability to report production by well?

MR. FOPPIANO: No. In fact, in my opinion, the same situation exists today where you have multiple wells on a single entity, and it is being measured as a group production.

A good example of that would be a secondary enhanced recovery unit, and yet an operator is still required to determine the production on a well-by-well basis for reporting purposes. And I guess my opinion is, I don't see that that affects that requirement at all. He still is going to have to report his production on a well-by-well basis, regardless of whether he has a Rule 303 exception or not.

MR. BROOKS: The present Rule does not require separate metering for each well, correct?

MR. FOPPIANO: I believe there's a Rule that requires separate metering for gas wells.

CHAIRMAN WROTENBERY: Will the changes here require any changes in ONGARD?

MR. BROOKS: Do you -- Can you answer that question, Richard?

MR. EZEANYIM: No, I don't think so. The changes we made would not affect the ONGARD entries, I think.

CHAIRMAN WROTENBERY: Okay. Did you find your other question?

MR. ROSS: Yeah, I remembered what I was going to ask, and this is really to try and help the record out a little bit. And I think the question is for you, Mr. Foppiano. Why do we regulate off-lease storage and off-lease measurement devices? What's the rationale there? I can understand the --

MR. FOPPIANO: That is a very good question. I think there is probably -- Well, first off, let me back up and say, I think the requirement and the oversight associated with the requirement is probably outdated. I think there is -- It reflects a concern of a very long time ago that the facilities be on the same lease where the production is, so the royalty owner can go out and check his gauges, royalty production, or something to that effect.

However, I know in other jurisdictions the off-lease storage and measurement is a very common thing to address with no notice required, because you're not doing anything differently, you're just doing it in a different location. And certainly there may be right-of-way issues that are associated with it, but those right-of-way issues are another issue that is handled to bring that production into the facility.

So it's -- I guess if I was writing it from scratch, I can't see what the strong regulatory concern is

about off-lease storage and measurement. But the fact that it is so rarely granted -- I guess we lost energy about trying to really re-work it and streamline it very much because it just doesn't have much practical impact anyway.

MR. BROOKS: Okay, thanks.

CHAIRMAN WROTENBERY: I believe those are all of the questions from the Commission at this point, Mr. Brooks.

MR. BROOKS: Very good. We have nothing further from the Division.

CHAIRMAN WROTENBERY: Thank you, Mr. Brooks. Thank you, Mr. Foppiano and Mr. Ezeanyim.

MR. FOPPIANO: Thank you.

CHAIRMAN WROTENBERY: Mr. Carr, I know you didn't enter an appearance, but you've been actively involved in this process. Is there anything you'd like to say?

MR. CARR: No, I'm glad that it's over.

MR. FOPPIANO: But somebody has to support this, so NMOGA supports it.

(Laughter)

MR. BROOKS: Well, there --

MR. CARR: I can tell you that it has been circulated, both by the Committee and through the NMOGA Regulatory Practices Committee. I think it is safe to say that at this time it enjoys the support of the industry,

and it certainly does by all of those who've worked at the local level.

CHAIRMAN WROTENBERY: Thank you, Mr. Carr.

MR. BROOKS: There's an anecdote I could relate in regard to off-lease storage, but I don't think I should waste the Commission's time.

CHAIRMAN WROTENBERY: We'll be interested in hearing it sometime.

Next steps on this particular matter.

Mr. Brooks, if you could revise the draft rule as we've discussed a moment ago --

MR. BROOKS: That I think can be very easily done.

CHAIRMAN WROTENBERY: Yeah, add the provisions requiring us to make our approvals contingent upon State Land Office and BLM --

MR. BROOKS: Right.

CHAIRMAN WROTENBERY: -- approval, and then distribute the revised language as quickly as possible to anybody who's interested, including the Land Office.

Commissioner Bailey, I guess we'll leave the record open in case the Land Office --

COMMISSIONER BAILEY: Thank you.

CHAIRMAN WROTENBERY: -- staff wishes to submit any additional comments --

COMMISSIONER BAILEY: Thank you very much, yes.

CHAIRMAN WROTENBERY: -- on the proposal.

It would probably be helpful to Mr. Ross if we could have those comments sometime in advance of the next meeting. Perhaps if the Land Office could submit any additional comments in two weeks' time? Our next meeting is in three weeks' time, I believe --

COMMISSIONER BAILEY: So December 6th --

CHAIRMAN WROTENBERY: -- on December 13th, so by December 6th, would that work?

COMMISSIONER BAILEY: That would work fine.

CHAIRMAN WROTENBERY: Okay. And I suppose any other comments anybody else wanted to submit could come in as well by December 6th, although I don't know --

MR. BROOKS: So far --

CHAIRMAN WROTENBERY: -- that we --

MR. BROOKS: -- I believe we have --

CHAIRMAN WROTENBERY: -- would expect any at this point.

MR. BROOKS: -- I believe we've received no comments.

MR. EZEANYIM: No comments so far.

CHAIRMAN WROTENBERY: That's what I thought, so...

And then we will plan to try to take final action

on this rule-making proposal on December 13th.

Okay. Thank you, everybody. Appreciate it.

MR. FOPPIANO: Is the plan to take any additional testimony at the 13th?

CHAIRMAN WROTENBERY: No, not at this point.

MR. FOPPIANO: Okay. I didn't know if you wanted the work group to comment on anything like --

CHAIRMAN WROTENBERY: Well, if the work group has any additional comments --

MR. FOPPIANO: Okay.

CHAIRMAN WROTENBERY: -- if they could submit those in writing by December 6th --

MR. FOPPIANO: Okay.

CHAIRMAN WROTENBERY: -- that would be helpful.

MR. FOPPIANO: I didn't know if you wanted any response or -- to anything, like the State Land Office comments, if there was -- if you needed any -- if it raised some questions like, did the work group consider these issues --

CHAIRMAN WROTENBERY: Well, we'll leave -- Okay, we'll leave that open as a possibility that we can have some additional comments on the 13th, then, but we would request that any additional written comments be submitted by the 6th.

MR. FOPPIANO: Okay.

CHAIRMAN WROTENBERY: Okay, thank you very much.

MR. FOPPIANO: Thank you.

MR. BROOKS: We're excused then?

CHAIRMAN WROTENBERY: You're excused, thank you

(Thereupon, these proceedings were concluded at 11:36 a.m.)

* * *

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 Commission 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 November 27th, 2002.

STEVEN T. BRENNER
CCR No. 7

My commission expires: October 16th, 2006