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REPLY TO SANTA FE OFFICE

February 14, 1991

VIA FEDERAL EXPRESS

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Bureau of Land Management
Roswell District Office
1717 West 2nd Street
Roswell, New Mexico 88201
Attention: Armando Lopez

Re: Lease Serial Nos. NM 68078, NM 77961 and NM 70402

Dear Mr. Lopez:

I am writing to you on behalf of Michael D. Leonhart, an individual owning an overriding royalty interest in the above-referenced federal leases. Mr. Leonhart is concerned that these federal leases are not being operated in a prudent manner and that as a result, Mr. Leonhart, other overriding royalty interest owners, and the federal government as the royalty owner, and the State of New Mexico are suffering severe revenue losses.

The leases involved are all located within Section 9 of Township 14 South, Range 29 East, Chavez County, New Mexico. This property has been the subject of extensive hearings before the New Mexico Oil Conservation Commission in the past and as a result of these hearings in November of 1989, the Oil Conservation Commission entered Order No. R-9035, attached. The effect of this order was to severely restrict the allowable rate of production from all wells within the North King Camp Devonian Pool until the various operators in that pool could reach voluntary agreement on operations and allocations of production. To date, the operating parties have not reached an agreement and as a result the allowables have continued at the low rates established in Order No. R-9035 with a resulting revenue loss to all royalty and overriding royalty owners.

It is our estimate that based upon \$20 per barrel oil, the lost royalty, which we understand is divided 50/50 between the federal government and the State of New Mexico has been approximately \$600,000.00, the overriding royalty lost during the year 1990 has been approximately \$300,000.00 and the loss in the state severance taxes has been more than \$300,000.00.

Mr. Leonhart is concerned that non-operating interest owners in Section 9 have suffered several million dollars in lost revenue because the operating parties have been unable or unwilling to reach agreement. This letter is a request that you investigate this matter and take what ever steps are available to you to protect the interest of the governmental agencies as well as the other non-operating interest owners in these lands. Mr. Leonhart is available to provide you whatever information he has available to him relating to this matter.

If we can be of assistance to you, please do not hesitate to contact me. Thank you for your attention to this matter.

Sincerely,



W. Perry Pearce

WPP/pmf:18
Attachment

cc: Don Stevens, Stevens Operating Corp.
Donald R. Curry
Robert L. Thornton
Santa Fe Exploration Company
Larry E. Sailer, Exxon Co., U.S.A.
Gill Lockwood
Joseph Chesser
William J. LaMay, Director of Oil Conservation Division
William F. Carr, Esquire
Thomas W. Kellahin, Esquire
Earnest L. Padilla, Esquire
Mike Leonhart

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:

DE NOVO

APPLICATION OF CURRY AND THORNTON
FOR AN UNORTHODOX OIL WELL LOCATION
AND A NON-STANDARD PRORATION UNIT,
CHAVES COUNTY, NEW MEXICO.

CASE NO. 9617

APPLICATION OF STEVENS OPERATING
CORPORATION TO AMEND DIVISION ORDER
NO. R-8917, DIRECTIONAL DRILLING AND
AN UNORTHODOX OIL WELL LOCATION,
CHAVES COUNTY, NEW MEXICO.

CASE NO. 9670

Order No. R-9035

ORDER OF THE COMMISSION

BY THE COMMISSION:

This cause came on for hearing at 9:00 a.m. on October 19, 1989, at Santa Fe, New Mexico, before the Oil Conservation Commission of New Mexico, hereinafter referred to as the "Commission."

NOW, on this 2nd day of November, 1989, the Commission, a quorum being present, having considered the testimony presented and the exhibits received at said hearing, and being fully advised in the premises,

FINDS THAT:

(1) Due public notice having been given as required by law, the Commission has jurisdiction of this cause and the subject matter thereof.

(2) The applicant, Curry and Thornton and Stevens Operating Corporation, own the leasehold on the W/2 of Section 9, Township 14 South, Range 29 East, NMPM, Chaves County, New Mexico and desire to dedicate their directionally-drilled Deemar Federal Well No. 1 to a non-standard unit consisting of

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Cases Nos. 9617 and 9670 (De Novo)
Order No. R-9035

the E/2 W/2 of said Section 9 at an unorthodox bottomhole location 1948 feet from the South line and 2562 feet from the West line (Unit K) of said Section 9 in the North King Camp-Devonian Pool.

(3) Santa Fe Exploration and Exxon USA appeared at the hearing and opposed the subject application on the basis that the unorthodox location would impair correlative rights; and, if granted, a penalty should be assessed based upon an estimate of recoverable pool reserves under each tract or the ratio penalty formula set forth in Division Order No. R-8917 and R-8917-A.

(4) The discovery well, the No. 1 Holmstrom, was drilled by Santa Fe Exploration at a standard location 1980 feet from the South and East lines of said Section 9.

(5) Special pool rules for said pool were promulgated by Order No. R-8806 after the hearing held November 22, 1988 in Case No. 9529, which provided for 160-acre spacing and proration units consisting of a governmental quarter section with the well to be located not less than 660 feet from the unit boundary, nor less than 330 feet from an inner quarter-quarter section line, nor less than 1320 feet from the nearest well completed in said pool.

(6) Pursuant to Order R-8917-A, Stevens Operating Corporation ("Stevens") re-entered the Philtex Oil Company Honolulu Federal Well No. 1 in Unit K of said Section 9 and directionally drilled the Deemar Federal Well No. 1 to the approved bottomhole location and encountered only water. After notifying the Division, Stevens plugged back said well bore and deviated a second hole at a higher angle to the east, which they completed as a producer.

(7) Timely applications for hearing de novo before the Commission were filed by both Stevens Operating Corporation and Santa Fe Exploration and the hearing date was extended to October 19, 1989 with the concurrence of all parties.

(8) After reviewing the Eastman Christensen "Report of Subsurface Directional Survey" for the Stevens Operating Corporation Deemar Federal Well No. 1, which showed the bottom-most perforated interval of the wellbore to be at 1948 feet from the South line and 2562 feet from the West line of Section 9, or 78 feet from the East line of the proration unit, the Director assigned a daily oil allowable of 35 barrels per day in accordance with Decretory Paragraph (5) of Order No. R-8917-A.

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Cases Nos. 9617 and 9670 (De Novo)
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(9) Both sides presented testimony that was in substantial agreement as to the geometry, the geology field and the producing reservoir characteristics, of the reservoir differing in their interpretations of the rate of north dip and to a minor degree, the trace of the major trapping fault at the west boundary.

(10) In unorthodox location cases, the Commission has generally endorsed a penalty formula using ratios based upon the proportional distance a well crowds the proration unit boundary and nearest producing well as in Division Order R-8917-A, but in cases where there is substantial evidence and agreement as to productive acreage and recoverable reserves, the Commission is obligated under the Oil and Gas Act to set allowables which allow operators to recover the oil and gas underlying their respective tracts while preventing waste.

(11) The geological witness for Stevens presented testimony that the pool oil-water contact was estimated at subsea elevation of -6055 feet which was not refuted by subsequent witnesses.

(12) The same witness established the major fault trace based upon a Formation Micro Scanner survey run in the Deemar Federal No. 1.

(13) Santa Fe Exploration's geophysicist presented a seismic interpretation showing a rate of north dip steeper than that presented by the Stevens' witness who relied upon a geological interpretation of the Micro Scanner survey. That survey only shows the rate of dip within the No. 1 Deemar wellbore.

(14) Based upon the oil-water contact and the major fault trace established by Stevens' geologist, the rate of north dip established by the Santa Fe geophysicist, and other geologic and engineering criteria which was in substantial agreement, the relative percentages of oil productive rock volume calculated under each tract are as follows:

- (a) Within the total field there is approximately 10,714 acre-feet of Devonian oil pay or oil saturated rock volume.
- (b) Underlying the E/2 W/2 of Section 9, there is approximately 2,246 acre-feet of Devonian oil pay or 21% of the pool total.

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Cases Nos. 9617 and 9670 (De Novo)
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(c) Underlying the SE/4 of Section 9 there is approximately 5,688 acre-feet of Devonian oil pay or 53% of the pool total.

(d) Underlying the NE/4 of Section 9 there is approximately 2,780 acre-feet of Devonian oil pay or 26% of the pool total.

(15) The North King Camp-Devonian Pool has an active water drive and the relative percentages of oil pay or oil-saturated rock volume under each tract are the same approximate percentages as the recoverable oil reserves under each tract, provided wells are positioned to permit the recovery.

(16) Productive surface area is calculated to be approximately 177 acres and expert engineering testimony has established that one well located at the highest part of the North King Camp structure could effectively and efficiently drain all of the recoverable oil reserves under this 177 acre pool.

(17) The Stevens' Deemar Federal No. 1 well occupies the highest portion of the structure and could effectively drain the entire pool. Only well locations that are unorthodox, such as the Stevens' well, could drain the upper portion (attic) of this oil reservoir and prevent the waste of unrecoverable oil reserves.

(18) Producing the Stevens' well at top allowable rates would eliminate waste but would violate the correlative rights of interest owners in the SE/4 of Section 9 unless all interest owners in Section 9 agreed to operate the pool and share oil and gas production and costs in some equitable fashion.

(19) The Santa Fe Exploration No. 1 Holmstrom Federal, the only other producing well in the pool, is located 55 feet lower structurally than the No. 1 Deemar.

(20) Testimony did establish that Santa Fe Exploration is producing their No. 1 Holmstrom well at a rate of 200 barrels of oil per day plus 10 barrels of water so as to minimize the effects of coning water.

(21) In the absence of unitized operations, in order to prevent waste and protect the correlative rights of all interest owners in a pool, allowables must be established which reflect the relative percentages established in Finding (14), encourage voluntary unitization and discourage the

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 Cases Nos. 9617 and 9670 (De Novo)
 Order No. R-9035

drilling of additional wells which are not needed and would constitute waste.

(22) Penalized allowables for the Stevens well that are tied to the producing rates of the No. 1 Holmstrom would be indefinite and violate Stevens' correlative rights. Allowables which would encourage drilling additional wells would cause waste.

(23) In order to protect correlative rights, total pool allowable should be the current pool production rate which includes the penalized rate of 35 barrels of oil per day for the Stevens' well, and the producing rate of 200 barrels of oil per day from the Santa Fe well. Said pool allowable of 235 barrels of oil per day should be allocated according to the percentages established in Finding (14) which are:

- (a) The E/2 W/2 of Section 9 should have an allowable of 49 ($.21 \times 235$) barrels of oil per day.
- (b) The SE/4 of Section 9 should have an allowable of 125 ($.53 \times 235$) barrels of oil per day.
- (c) the NE/4 of Section 9 should have an allowable of 61 ($.26 \times 235$) barrels of oil per day if it is drilled.

(24) The allowables established in Finding (23) should become effective December 1, 1989 and should remain in effect unless voluntary agreement is reached by all interest parties in the field at which time the pool allowable should be increased to 1,030 barrels of oil per day which is the top allowable rate for the two producing wells currently in the pool and which new pool allowable could be produced in any proportion between the two existing wells.

(25) The tract allowables established in Finding (23) should protect correlative rights by honoring the percentages established in Finding (14) and prevent waste by discouraging the drilling of additional wells which are not necessary to effectively and efficiently drain the subject pool.

(26) Should all interest owners in this pool reach voluntary agreement subsequent to the entry of this order, operators of the pool wells should file with the Director of the Division application for approval of the unit agreement and, upon approval, this order should thereafter be of no further effect and the new pool allowable should take effect on the first day of the month following approval of said unit agreement by the Director.

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Cases Nos. 9617 and 9670 (De Novo)
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IT IS THEREFORE ORDERED THAT:

(1) Effective December 1, 1989, the pool allowable for the North King Camp-Devonian field shall be 235 barrels of oil per day which shall be shared by the below listed proration units in the amounts shown:

- (a) The E/2 W/2 of Section 9, Township 14 South, Range 29 East, shall have a top allowable of 49 barrels of oil per day.
- (b) The SE/4 of Section 9, Township 14 South, Range 29 East, shall have a top allowable of 125 barrels of oil per day.
- (c) The NE/4 of Section 9, Township 14 South, Range 29 East, shall have a top allowable of 61 barrels of oil per day if a well is drilled and completed in the Devonian.

(2) Said allowable shall remain in effect unless all interest owners in the pool reach voluntary agreement to provide for unitized operation of its pool.

(3) Should all interest owners reach voluntary agreement subsequent to entry of this order, this order shall thereafter be of no further effect.

(4) The operators of the pool wells shall file with the Director of the Division an application for approval of the unit agreement and this order shall then terminate on the first day of the month following approval of said unit. A new pool allowable of 1,030 barrels of oil per day shall then take effect; said new pool allowable can be produced in any proportion between existing pool wells.

(5) Jurisdiction of this case is retained for the entry of such further orders as the Commission may deem necessary.

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Cases Nos. 9617 and 9670 (De Novo)
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DONE at Santa Fe, New Mexico, on the day and year
hereinabove designated.

STATE OF NEW MEXICO
OIL CONSERVATION COMMISSION

WILLIAM R. HUMPHRIES, Member

William W. Weiss

WILLIAM W. WEISS, Member

William J. Lemay

WILLIAM J. LEMAY, Chairman
and Secretary

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

IN THE MATTER OF THE HEARING
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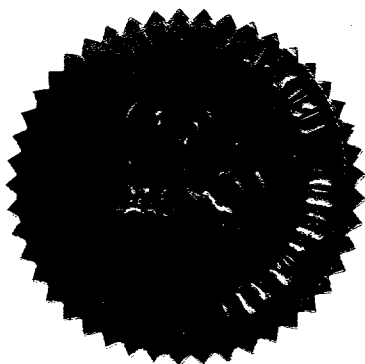
DONE at Santa Fe, New Mexico, on the day and year
hereinabove designated.

STATE OF NEW MEXICO
OIL CONSERVATION COMMISSION

WILLIAM R. HUMPHRIES, Member

William W. Weiss
WILLIAM W. WEISS, Member

William J. Lemay
WILLIAM J. LEMAY, Chairman
and Secretary



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