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

IN THE MATTER OF THE HEARING)
CALLED BY THE OIL CONSERVATION)
DIVISION FOR THE PURPOSE OF)
CONSIDERING:) CASE NO. 10,961
)
APPLICATION OF)
MEWBOURNE OIL COMPANY)
)

ORIGINAL

REPORTER'S TRANSCRIPT OF PROCEEDINGS

EXAMINER HEARING

BEFORE: JIM MORROW , Hearing Examiner

April 28, 1994 MAY 19 1994
Santa Fe, New Mexico

This matter came on for hearing before the Oil Conservation Division on Thursday, April 28, 1994, at Morgan Hall, State Land Office Building, 310 Old Santa Fe Trail, Santa Fe, New Mexico, before Steven T. Brenner, Certified Court Reporter No. 7 for the State of New Mexico.

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I N D E X

April 28, 1994
Examiner Hearing
CASE NO. 10,961

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By: WILLIAM F. CARR

FOR KAISER-FRANCIS OIL COMPANY:

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Santa Fe, New Mexico 87504-2265
By: W. THOMAS KELLAHIN

* * *

1 WHEREUPON, the following proceedings were had at
2 8:17 a.m.:

3 EXAMINER MORROW: Call the hearing to order in
4 Docket Number 13-94 and call Case 10,961.

5 MR. CARROLL: Application of Mewbourne Oil
6 Company for compulsory pooling and unorthodox gas well
7 location, Eddy County, New Mexico.

8 EXAMINER MORROW: And we'll call for appearances.

9 MR. CARR: May it please the Examiner, my name is
10 William F. Carr with the Santa Fe law firm Campbell, Carr,
11 Berge and Sheridan.

12 I represent Mewbourne Oil Company in this case,
13 and I have two witnesses.

14 EXAMINER MORROW: Yes, sir. Do you have co-
15 counsel today with you?

16 MR. CARR: No, sir. Oh, may it please the
17 Examiner, today is father-daughter day. When my daughter
18 Peggy, who is with me today, discovered she could miss
19 school, she developed a burning desire to learn about the
20 Oil Commission. And so I have my daughter with me today to
21 see how it's done. And after this we're going to go do a
22 search through the records of the Oil Commission so she can
23 know what an exciting career I have.

24 EXAMINER MORROW: Welcome, Peggy, we're glad
25 you're here.

1 MR. CARR: At this time, Mr. Examiner, we would
2 call Paul Haden.

3 MR. KELLAHIN: There's other appearances, Mr.
4 Examiner.

5 EXAMINER MORROW: Excuse me, sir.

6 MR. KELLAHIN: I'm Tom Kellahin, Mr. Examiner, of
7 the Santa Fe law firm of Kellahin and Kellahin, appearing
8 on behalf of Kaiser-Francis Oil Company.

9 I do not have a witness.

10 EXAMINER MORROW: Okay. Ask the witnesses to
11 stand and be sworn, please.

12 (Thereupon, the witnesses were sworn.)

13 D. PAUL HADEN,

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

16 DIRECT EXAMINATION

17 BY MR. CARR:

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

19 A. My name is Paul Haden.

20 Q. And where do you reside?

21 A. Midland, Texas.

22 Q. By whom are you employed and in what capacity?

23 A. By Mewbourne Oil Company as a petroleum landman.

24 Q. Mr. Haden, have you previously testified before
25 this Division?

1 A. Yes, I have.

2 Q. At the time of that prior testimony were your
3 credentials as a petroleum landman accepted and made a
4 matter of record?

5 A. Yes, they were.

6 Q. Are you familiar with the Application filed in
7 this case on behalf of Mewbourne Oil Company?

8 Q. Yes, I am.

9 Q. Are you familiar with the subject area and the
10 lands that are involved with this Application?

11 A. Yes, sir, I am. *JAM*

12 ~~EXAMINER MORROW:~~ *Mr. Carr:* Mr. Morrow, are the witness's
13 qualifications acceptable?

14 EXAMINER MORROW: Yes, sir.

15 Q. (By Mr. Carr) Mr. Haden, could you briefly state
16 what Mewbourne seeks with this Application?

17 A. Mewbourne seeks an order pooling all mineral
18 interests from 500 feet below the top of the San Andres
19 formation to the base of the Morrow formation under the
20 following spacing units in the south half of Section 20 of
21 Township 18 South, Range 28 East in Eddy County, New
22 Mexico: the south half for 320-acre units, the southeast
23 quarter for 160-acre units, the east half of the southeast
24 quarter for 80-acre units, and the northeast of the
25 southeast quarter for 40-acre units.

1 This will be dedicated to Mewbourne Oil Company's
2 Chalk Bluff Draw Prospect, the Illinois Camp "20" State
3 Number 2 Well, to be drilled in an unorthodox location 1650
4 feet from the south line and 990 feet from the east line of
5 this Section 20. This is the Unit designation I.

6 Q. Mr. Haden, are there geologic and topographical
7 reasons that Mewbourne is proposing this well at an
8 unorthodox location?

9 A. Yes, there are, and our geologist will discuss
10 these aspects in detail.

11 Q. Have you prepared certain land exhibits for
12 presentation in this case?

13 A. Yes, I have.

14 Q. Could you refer to what has been marked as
15 Mewbourne Exhibit Number 1? That's inside the cover of the
16 land packet that we provided to you, Mr. Morrow.

17 Would you refer to that, identify it and then
18 review the information on this exhibit for the Examiner?

19 A. Yes, sir. The -- This is a land plat indicating
20 our proposed well location. Our well location is
21 designated by a red dot in the east half of the southeast
22 quarter of Section 20. The yellow-shaded area is our
23 proposed spacing unit for this well.

24 The outlying areas shaded in red are those areas
25 in which we have notified the offset operators and/or

1 owners of operating rights or unleased mineral owners
2 regarding our unorthodox location, pursuant to the rules of
3 the NMOCD.

4 Q. Mr. Haden, this well is unorthodox because it is
5 moving toward the east?

6 A. That is correct.

7 Q. And it's only encroaching on tracts due east and
8 northeast of the well?

9 A. That's right.

10 Q. And who operates all of that acreage?

11 A. Mewbourne Oil Company operates the west half of
12 Section 21.

13 Q. So you're only encroaching on tracts operated by
14 you?

15 A. That is correct.

16 Q. What is the primary objective in the proposed
17 well?

18 A. Primary objective is the Morrow formation, the
19 estimated total depth being 10,700 feet beneath the
20 surface.

21 Q. At this point, would you provide Mr. Morrow with
22 a general summary of the ownership interest in the south
23 half of Section 20?

24 A. Yes, I can. The southwest quarter is owned by
25 Kaiser-Francis, a 75-percent interest in that 160 acres.

1 Texaco owns a 25-percent interest in that 160 acres.

2 In the east half of the southeast quarter, MOC,
3 et al., owns or represents 84 percent of the interest.
4 Louis Dreyfus Natural Gas Corporation owns 16 percent in
5 that 80-acre tract.

6 In the west half, southeast quarter, Mewbourne
7 Oil Company owns 50 percent of that interest. And the
8 Nichols estate owns the other 50-percent interest.

9 Q. What percent of the working interest in the
10 south-half unit has been voluntarily committed to the
11 proposed well?

12 A. Approximately 33 1/2 percent.

13 Q. Let's go to the AFE for the well, which is marked
14 Exhibit Number 2 -- it's attached behind the plat -- and I
15 would ask you to review this for Mr. Morrow.

16 A. Yes, sir, I will. This AFE is an estimated well
17 cost for this 10,600-foot proposed Morrow test well. The
18 total well cost is \$744,684. Dryhole cost estimated at
19 \$431,488.

20 Q. Has Mewbourne drilled other wells recently to the
21 Morrow in this area?

22 A. Yes, we have.

23 Q. In fact, you are currently drilling in the north
24 half of Section 20, are you not?

25 A. That is correct.

1 Q. And that's the result of a compulsory pooling
2 order that was entered following Mr. Morrow's April 20
3 hearing; is that right?

4 A. That is correct.

5 Q. Are the costs reflected on the AFE, which is
6 marked Exhibit 2, in line with the costs that you've
7 incurred in drilling other wells in the area?

8 A. Yes, sir, that's also correct.

9 Q. All right, Mr. Haden, let's go to the next
10 portion of the land exhibits, and I would ask you to
11 identify what has been marked as Exhibit 3A.

12 A. Exhibit 3A is our correspondence with all the
13 interest owners which we are force-pooling today.

14 Q. Do these letters confirm that in fact notice of
15 the hearing and of your proposal has been provided to each
16 of these owners?

17 A. Yes, that's correct.

18 Q. And there's also a list of the ownership included
19 in this portion of the exhibit?

20 A. Right.

21 Q. Let's go to the remainder of this exhibit, which
22 is 3B, and I would ask you to refer to this and summarize
23 for the Examiner the efforts you've made to obtain
24 voluntary joinder of all interest owners.

25 A. Exhibit 3B is a summary of the owners which we're

1 force-pooling, which currently include Kaiser-Francis Oil
2 Company; Louis Dreyfus Natural Gas Corporation; the estate
3 of Leonard Nichols, deceased; and Texaco Exploration and
4 Production, Inc., which gives the percentages in the
5 proposed spacing unit for this Morrow well.

6 As you can see in the summary --

7 EXAMINER MORROW: We never have found 3B yet.

8 MR. CARR: 3B, I believe, is on the other side of
9 that portion of the exhibit, and there are tabs at the
10 bottom, Mr. Morrow, that indicate by affected party.

11 EXAMINER MORROW: Oh, okay.

12 THE WITNESS: Let's start with Kaiser-Francis Oil
13 Company. We've made a well proposal by letter, an AFE was
14 sent to them February 7th of 1994, which we have been
15 negotiating with them ever since.

16 We have recently received a letter from them,
17 executed by them, stating that they would farm out their
18 interest under certain general terms. However, we have not
19 had the opportunity to execute a formal farmout agreement,
20 thus we will have to name Kaiser-Francis Oil Company,
21 still, in this proceeding.

22 As to Louis Dreyfus Natural Gas Corporation,
23 again we proposed the well February 7th, 1994, with an AFE
24 of our estimated well costs for the well. We have since
25 negotiated a trade with them wherein they would either farm

1 out or join us after the completion of the well in the
2 north half.

3 The estate of Leonard Nichols, deceased, we have
4 an assignment executed by Leonard Nichols' widow, in which
5 she has committed her interest to Mewbourne Oil Company.
6 The reason why we have to name this estate is that it has
7 not been probated yet. This is simply a title-curative
8 matter.

9 The last owner which we're seeking to force-pool
10 is Texaco Exploration and Production, Inc. We had proposed
11 the well, again, February 7th, 1994. We have been in
12 negotiations with them ever since. We have not been able
13 to reach a voluntary agreement, which is the object of this
14 hearing.

15 Q. (By Mr. Carr) Mr. Haden, as to the Kaiser-
16 Francis interest, as of today you have a letter which
17 appears to resolve the dispute with Kaiser-Francis; is that
18 correct?

19 A. That's correct.

20 Q. And once a formal farmout agreement is executed,
21 at that point in time Kaiser-Francis would be dismissed
22 from and no longer subject to pooling?

23 A. That is correct.

24 Q. As to the Nichols estate, this is the very
25 situation that you testified to at the hearing for the

1 pooling in the north half of this section?

2 A. Right, that's the same place.

3 Q. And you have reached a letter agreement with her
4 whereby if, in fact, the estate is probated, she could
5 voluntarily join in the well at that time?

6 A. Right, as evidenced under the correspondence
7 regarding the Nichols estate, you'll see our letter dated
8 March 25th, 1994, which involved the north half, which Mr.
9 Carr was talking about.

10 This same letter, as you turn to the page dated
11 April 19th, involves this case, the same exact terms, which
12 state that we would dismiss her from pooling when the
13 estate is probated.

14 Q. Until, in fact, that estate is probated and they
15 participate in the well, you do need to include them in the
16 pooling order?

17 A. That is correct.

18 Q. In your opinion, have you made a good-faith
19 effort to locate and obtain the voluntary participation in
20 this well of all the interest owners in the south half of
21 Section 20?

22 A. Yes, we have.

23 Q. And you have also included in your land exhibit
24 waivers from various interest owners in the tract; is that
25 right?

1 A. That is also correct.

2 Q. Could you identify what has been marked as
3 Mewbourne Exhibit Number 4?

4 A. Exhibit Number 4 is the affidavit of notice,
5 wherein we -- It's evidence that we have properly notified
6 all the owners affected by this case.

7 Q. So Mewbourne has notified them, as have we, so
8 that they all have notices that, in fact, the hearing is
9 going forward today?

10 A. That's correct.

11 Q. Have you made an estimate of the overhead and
12 administrative costs while drilling this well and also
13 while producing it if, in fact, it's successful?

14 A. Yes, we have. Those costs are \$6167 per month
15 while drilling and \$626.50 per month while producing.

16 Q. Are these costs the costs that are reflected in
17 the operating agreement that's been signed by the parties
18 who are voluntarily in the well?

19 A. That's correct.

20 Q. Are these costs also the same figures that were
21 approved by this Division in Order Number R-10,103, which
22 pooled the north half of Section 20?

23 A. Yes, those rates were approved.

24 Q. Do you request that these figures be incorporated
25 into the order that results from today's hearing?

1 A. Yes, I do.

2 Q. Does Mewbourne seek to be designated operator of
3 the proposed well?

4 A. Yes, we do.

5 Q. And you will be calling a geological witness to
6 review the risk associated with the well and also the
7 conditions which bear on the unorthodox well location?

8 A. Yes, sir, we will.

9 Q. Were Exhibits 1 through 4 either prepared by you
10 or compiled under your direction?

11 A. Yes, they were.

12 MR. CARR: At this time, Mr. Morrow, we move the
13 admission of Mewbourne Oil Company Exhibits 1 through 4.

14 EXAMINER MORROW: We never did find 4.

15 MR. CARR: 4, I think, is behind the land packet.
16 It's not attached to it, Mr. Morrow, but right behind that
17 folder and ahead of the geological exhibit.

18 EXAMINER MORROW: Oh, okay, right here.

19 1 through 4 are accepted into the record.

20 MR. CARR: That concludes my direct examination
21 of Mr. Haden.

22 EXAMINER MORROW: Thank you, sir.

23 CROSS-EXAMINATION

24 BY MR. KELLAHIN:

25 Q. Mr. Haden, let me ask you a couple of questions

1 about your efforts to consolidate the tracts --

2 A. Yes, sir.

3 Q. -- into the spacing unit for this well.

4 It appears from your summary that your initial
5 efforts with regards to these four different parties --
6 Kaiser, Texaco, Dreyfus and the Nichols estate -- it looks
7 like fall of 1993, about September, you started your
8 discussions with Ms. Nichols and with Texaco to get those
9 tracts?

10 A. Right, with Mrs. Nichols, it was first around
11 September, from 1993. With Texaco, we had sent an offer to
12 purchase their interest or have them join us around
13 September also.

14 Q. At this point I think you've told us that you
15 have a third of the tract committed to you on a voluntary
16 basis?

17 A. Right.

18 Q. What is the source of that interest?

19 A. That interest is Mewbourne Oil Company, along
20 with the working interest owners who have agreed to
21 participate in the well, being Yates Petroleum Corporation
22 and also Marathon Oil Corporation.

23 Q. Are Marathon and Yates participating with you in
24 a joint operating agreement?

25 A. Yes, sir, they have.

1 Q. What interest does Marathon have in the spacing
2 unit? Do you recall?

3 A. It's the same interest as Louis Dreyfus Natural
4 Gas Corporation. It's roughly, I believe, four percent --

5 Q. About four percent of the unit?

6 A. Right.

7 Q. When you apportion it out to the spacing unit?

8 A. That's right.

9 Q. And the Yates interest, what is their working
10 interest, approximately?

11 A. It's slightly higher than four percent.

12 Q. Your remaining interest, is that committed to you
13 on a lease basis?

14 A. What do you mean by "a lease basis"?

15 Q. Apart from the Marathon and the Yates interest,
16 you then have your own portion of the working interest
17 committed to you?

18 A. Right.

19 Q. Was that by lease or by farmout?

20 A. That was by an assignment of interest by Margaret
21 Nichols.

22 Q. All right. So part of that interest that you're
23 consolidating from Nichols, you already hold by reason of
24 an assignment?

25 A. That's right.

1 Q. All right. Have you acquired any leases for the
2 spacing unit?

3 A. By virtue of assignment from Mrs. Nichols.

4 Q. What did you have to pay her per acre to --

5 A. We did not pay her any consideration.

6 Q. I've noticed in some of the correspondence, the
7 Texaco offer -- One of the options you provided to Texaco
8 was to acquire their interest based upon terms that
9 included \$150 per acre?

10 A. Right, that was offered at that time.

11 Q. Okay. And that's in September of 1993?

12 A. Right, that was in September of 1993.

13 Q. The Nichols offer at one time included your
14 proposal to acquire her interest for \$200 per acre; do you
15 recall that?

16 A. That was probably also in the fall of 1993.

17 Q. It was, sir.

18 What was the basis for the \$150 to Texaco and the
19 \$200 an acre to Ms. Nichols during that period of time?

20 A. Probably because Mrs. Nichols owned more acreage.
21 Her acreage was more valuable than the Texaco acreage.

22 Q. Your offer to Kaiser-Francis, one of the options
23 was to acquire their interest, and you proposed in March of
24 this year as an acquisition price \$125 an acre?

25 A. Yes, sir, but they obviously did not accept that,

1 which is the reason why we're here today.

2 Q. Why didn't you offer them acquisition prices in
3 the range that you had previously proposed to Texaco and to
4 Ms. Nichols?

5 A. Well, as you will note, that offer was made, I
6 believe, in March. The other offers were made in the fall
7 of 1993. Our valuation of this area has changed. The
8 Kaiser-Francis --

9 Q. It's become more -- Has it become more risky?

10 A. There is certainly, yes, risk associated with it.
11 However, the Kaiser-Francis acreage simply is not as
12 valuable to us as the other acreage.

13 Q. They have a greater interest and therefore have a
14 larger percentage of the spacing unit?

15 A. They have a greater interest.

16 Q. How could that greater interest not be more
17 important to you when you're trying to consolidate those
18 interests in the spacing unit?

19 A. It's all based on geological reasons.

20 Q. Your proposal to Mewbourne on December 14th of --
21 Mewbourne's proposal on December 14th of 1993 to Louis
22 Dreyfus shows a proposal to acquire their interest for \$200
23 an acre?

24 A. Again, that was in December of 1993, also. Their
25 interest is in the east half, southeast quarter. Their

1 acreage is more valuable to us than the Kaiser-Francis
2 acreage.

3 Q. I assume because of the potential to include that
4 acreage in smaller-size spacing units and other formations?

5 A. That could be a reason.

6 Q. Was it the reason?

7 A. I don't recall what the reason was.

8 Q. Did you determine the reason for the change in
9 price per acre?

10 A. Our management determined that.

11 Q. Is that a decision that you participated in?

12 A. That is not a decision which I participated in.

13 Q. Do you know why they made that decision the way
14 they did?

15 A. Again, it was probably because of the value of
16 the acreage.

17 Q. Do you have any other explanation for the change
18 in price?

19 A. I don't see what bearing that has. That -- We
20 had paid no one any consideration for the south half.

21 Q. As part of your exploration plans in this area,
22 are you continuing to explore for deep Morrow gas
23 production?

24 A. Yes, we plan to.

25 Q. And I noticed on the cross-section, there's other

1 Morrow wells on the geologic displays.

2 A. Other Morrow wells being where? To the -- the
3 ones that are -- have already been drilled or --

4 Q. Yes, sir.

5 A. Okay, yes, to the northwest, I assume, is what
6 you're talking about?

7 Q. Yes, sir. It looks like you have some
8 exploration plan in the area for not only Morrow but other
9 formations.

10 A. Right now it's simply Morrow.

11 Q. Okay. What are the range of prices you have to
12 pay per acre in order to consolidate leases or acquire
13 interest?

14 A. This all varies, but right now we are not paying
15 any consideration; we are acquiring farmouts from the
16 interest owners.

17 Q. That's been your strategy, and that's worked so
18 far?

19 A. Yes, that's correct.

20 MR. KELLAHIN: All right, sir. Thank you, Mr.
21 Examiner.

22 REDIRECT EXAMINATION

23 BY MR. CARR:

24 Q. Mr. Haden when did you first start trying to put
25 together a south-half unit?

1 well, that would probably do it.

2 A. You're talking about this exhibit here?

3 Q. Yes, sir.

4 A. Okay. Again, Kaiser-Francis Oil Company owns a
5 75-percent interest in the southwest quarter --

6 Q. Okay.

7 A. -- which, on a unit basis, is a 37-1/2 percent
8 interest.

9 Q. All right.

10 A. Texaco Exploration and Production, Inc., they own
11 a 25-percent in the southwest quarter, which is a 12-1/2-
12 percent interest in the unit.

13 Q. Okay.

14 A. The Louis Dreyfus Natural Gas Corporation, they
15 own approximately 16-percent interest --

16 Q. Okay.

17 A. -- in the east half of the southeast quarter and
18 a roughly 4-percent interest in the unit.

19 The estate of Leonard Nichols, deceased, owns a
20 50-percent interest in the west half of the southwest
21 quarter, which corresponds to a 12-1/2-percent unit
22 interest.

23 Q. All right. Now, go ahead and tell me what the
24 committed interests are.

25 A. The committed interests --

1 Q. Mewbourne, you said, was 12 1/2 percent. What
2 part of the 320 does that derive from?

3 A. Okay, Mewbourne Oil Company's 12- -- We acquired
4 a 12-1/2-percent unit interest by virtue of the widow of
5 Leonard Nichols -- her name is Margaret Nichols -- which is
6 -- That interest was in the west half of the southeast
7 quarter. She owned a 50-percent interest individually as a
8 community-property interest.

9 Q. Okay.

10 A. Also, we have acquired the interest of Arco, a
11 farmout agreement. They own a 50-percent interest in the
12 east half, southeast quarter.

13 Q. East half of southeast quarter?

14 A. Yes, sir.

15 Q. So that gives you another 12 1/2, right?

16 A. Right. Marathon Oil Company, they have committed
17 their interest voluntarily to Mewbourne, either joining or
18 farm out.

19 Yates Petroleum --

20 Q. Where did that come from?

21 A. East half of southeast quarter. Roughly the same
22 interests as Louis Dreyfus Natural Gas Corporation.

23 Q. So it was that 15-point --

24 A. Right, 15.97222 percent.

25 Q. Okay.

1 A. And then Yates Petroleum Corporation, they own a
2 18 -- roughly 18.06-percent interest in the east half of
3 the southeast quarter.

4 Q. And how much does that give you? That would be a
5 fourth of that, I guess, wouldn't it?

6 A. Right.

7 Q. All right. Now, the -- Did you say that Kaiser-
8 Francis's farmout has been -- the agreement has been
9 completed in the north half, in the north half?

10 A. The -- Kaiser-Francis is not an interest owner in
11 the north half of this section.

12 Q. Oh, they're not?

13 A. No, sir.

14 Q. I thought there was a farmout agreement pending
15 with someone up there.

16 A. No, the Kaiser-Francis agreement with Mewbourne
17 affects only this southwest quarter. They're 75 percent
18 interest in that.

19 Q. But I believe you or Mr. Carr, one, indicated you
20 had a letter from Kaiser-Francis which indicated --

21 A. Well, this letter -- I've seen a copy of it
22 today. It was sent to us, I believe, yesterday. That was
23 an agreement wherein they would farm out their interest to
24 us, they would retain an overriding royalty interest.

25 However, the formal farmout agreement obviously

1 has not been executed yet. We have to work those terms
2 out.

3 Q. I had a question on overhead cost the fixed
4 rates. The *Ernst and Young* survey that I had available to
5 me indicated lower numbers than what you've proposed.

6 A. Right, that's -- That's correct.

7 Q. At the last hearing we didn't get into that very
8 much, because you had indicated on still another previous
9 order you had been granted those same rights.

10 A. Right.

11 Q. I wanted to ask you to give me some explanation
12 as to why you feel that the higher costs are -- than what
13 the industry standard is, why it's justified in this case.

14 A. Well, our rates are agreed upon by the interest
15 owners who join in our wells, and that obviously is --
16 should be viewed as the rates that should be charged,
17 because that's what people agree on.

18 These *Ernst and Young* rates are not in reality
19 rates that should be charged. They're low, lower than the
20 risk, the overhead that actually occurs regarding drilling
21 and producing wells.

22 A lot of these interest owners who had responded
23 to the *Ernst and Young* survey, they -- Many of them were
24 companies and individuals who have low, low overheads.
25 They could be a mom-and-pop organization, for instance.

1 They simply do not have the overhead which we do.

2 All the working interest owners in our previous
3 wells have all agreed to our rates, and we have no problem
4 with it.

5 Q. Well, I'd sure agree with that on the people that
6 signed the agreement. But the ones that are being force-
7 pooled, it might be a little bit different --

8 Q. Right.

9 Q. -- opinion there.

10 In your negotiations, have any of the people
11 you've corresponded with talked to you about those overhead
12 rates, or have they disagreed for some other reason, those
13 that haven't signed up?

14 A. Those who haven't signed up did not want to
15 participate in the well. We --

16 Q. They didn't say nothing about the overhead?

17 A. No, sir, they didn't.

18 Generally, we do not send these uncommitted
19 owners an operating agreement until they say they would
20 like to see one.

21 Q. So they wouldn't know what was --

22 A. No, sir.

23 Q. -- what was proposed?

24 A. But however, those interest owners we have had
25 previous dealings with, and they're aware of what our rates

1 are.

2 Q. Are you involved as a non-operator in some
3 agreements where you're paying rates that are comparable to
4 these?

5 A. Yes, sir, we are. I'm trying to -- Okay, in
6 Township 22 South -- 22 East, I believe, it's -- we're in
7 some wells operated by Collins and Ware, Inc. These rates
8 correspond approximately with our rates. That's just --
9 And it's around the same depth range. I don't have the
10 exact legal descriptions for those lands, but I could make
11 them available to you.

12 EXAMINER MORROW: That's all right.

13 I believe that's all the questions I had. Rand,
14 did you have any?

15 MR. CARROLL: No, I don't think so.

16 EXAMINER MORROW: Thank you, sir.

17 THE WITNESS: Thank you.

18 MR. CARR: Mr. Morrow, at this time we would call
19 David Shatzer.

20 DAVID SHATZER,

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

23 DIRECT EXAMINATION

24 BY MR. CARR:

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

1 A. My name is David Shatzer.

2 Q. How do you spell your last name?

3 A. S-h-a-t-z-e-r.

4 Q. Where do you reside?

5 A. Midland, Texas.

6 Q. By whom are you employed and in what capacity?

7 A. I'm a petroleum geologist for Mewbourne Oil
8 Company in Midland, Texas.

9 Q. Mr. Shatzer, have you previously testified before
10 this Division?

11 A. Yes, I have.

12 Q. At the time of that prior testimony, were your
13 credentials as a petroleum geologist accepted and made a
14 matter of record?

15 A. Yes, they were.

16 Q. Are you familiar with the Application filed in
17 this case on behalf of Mewbourne?

18 A. Yes, I am.

19 Q. And have you made a geological study of the area
20 which is involved in this case?

21 A. Yes, I have.

22 MR. CARR: Are the witness's qualifications
23 acceptable?

24 EXAMINER MORROW: Yes, sir.

25 Q. (By Mr. Carr) Have you prepared certain exhibits

1 for presentation here today?

2 A. Yes.

3 Q. Could you go to what has been marked Mewbourne
4 Exhibit Number 5, identify this and review the information
5 on this exhibit for Mr. Morrow?

6 A. Exhibit 5 is a production study of the deeper
7 production in the proposed Illinois Camp area. The wells
8 that are shown on this map are only Morrow penetrations.
9 The shallow control is not shown. The map is on a 1-to-
10 2000 scale.

11 The Morrow formation is the dominant production
12 in this area, and it is colored in orange. Cumulative gas
13 rates are shown in the first column -- second column. The
14 date of first production, is the first column. Second row
15 is the cumulative gas. The third is cumulative oil and if
16 it's still producing. Then also it's followed by the daily
17 gas and oil rates.

18 And what we see on this production map is that
19 there are some good Morrow wells. There's one good Morrow
20 well in Section 7 that's 2.8 BCF, in the southeast quarter
21 of 7. And then there are some other fair Morrow wells.

22 There's two recent producers in Section 17, and
23 that -- Our proposed prospect is moving away to the south
24 from the known control. It's also moving to an area where
25 there's a lot less control, Sections 18, 19, 21, 29. Those

1 sections have no Morrow penetrations.

2 The only well in the south half of the mapped
3 area is the well in Section 28, and it was a poor Morrow
4 producer, only producing 42 million.

5 So that we're moving in a direction away from the
6 better Morrow producers, into an area of little production
7 to date.

8 Q. Mr. Shatzer, there's an X in the south half of
9 Section 20. What does that indicate?

10 A. The X indicates the location of a standard Morrow
11 well location, as opposed to the unorthodox location in the
12 two circles, 990, 1650 from the east and south, that we
13 will explain both geologically and surface topography
14 constraints causes it to be proposed there.

15 Q. Let's move to your structure map, Mewbourne
16 Exhibit Number 6. Would you identify and review that,
17 please?

18 A. Exhibit 6 is a Morrow structure map contoured on
19 top of the lower Morrow. The contour interval is 50 feet.
20 The contours gently dip to the east southeast.

21 And that again, going to the southeast or downdip
22 can sometimes increase the geological risk because one of
23 the primary reservoirs, which I will explain, is the lower
24 Morrow orange sand, and it does produce in Section 7 and
25 Section 17.

1 But moving downdip sometimes can, in this
2 particular sequence of the Morrow, can cause the sand --
3 the sand can become a wet reservoir and nonproductive
4 downdip on some occasions, so that the risk is increasing
5 by going downdip in the proposed location.

6 Q. This exhibit also contains a trace for your
7 cross-section, S-S'; is that right?

8 A. That is correct.

9 Q. Let's go to that cross-section, Exhibit Number 6
10 [sic]. I would ask you to review the information on this
11 exhibit for the Examiner.

12 A. Exhibit Number 7 is the Morrow stratigraphic
13 cross-section. This is the Morrow stratigraphic cross-
14 section, S-S'. It's hung on a top of lower Morrow
15 stratigraphic datum, and this is also the point at which
16 the structure map was contoured. And the lower Morrow sand
17 is colored in orange, and the middle Morrow sand, also
18 productive in this area, is colored green.

19 The primary Morrow reservoirs, orange sand in the
20 lower Morrow and green sand in the middle Morrow, are
21 lenticular sandbody channels that generally trend to the
22 northwest-southeast.

23 And in Section 17 these Morrow sands are
24 productive, but they're somewhat broken. The lower Morrow,
25 for instance, is the only thing productive in section -- in

1 the 17 Number 2, in the southeast quarter, and that sand is
2 quite broken.

3 The proposed location is located in between the
4 Section 17 wells, and then the last well on the cross-
5 section is Section 28, Sinclair State, and this again was a
6 very tight, uneconomic producer of only 42 million cubic
7 feet of gas.

8 So that we're -- the ideal sand we're looking for
9 is really not even portrayed on this cross-section. There
10 are some sands in Section 7 that are blocky clean channel
11 sands that are more like what we're looking for.

12 Q. This exhibit shows, in fact, the erratic nature
13 of the Morrow sands in this area, does it not?

14 A. Yes, it does.

15 Q. And again, it would show that as you move toward
16 the south and southeast, you're increasing the risk of
17 drilling a successful Morrow well?

18 A. Yes, that is correct.

19 Q. All right. Let's go to the isopach map, Exhibit
20 Number 8. Would you review the information on this exhibit
21 for the Examiner?

22 A. Exhibit Number 8 is the lower Morrow orange sand,
23 gross sand isopach. What is contoured is the gross clean
24 sand, with the bottom figure shown next to each of the
25 wells, and the productive wells from the lower Morrow

1 orange sand are colored orange.

2 Again, the general trend of these channels is
3 northwest-southeast, and the wells need to be located in
4 the thickest portion of this sand to be commercial
5 producers. If wells are located at locations too near the
6 edge, many times they are too tight to be commercially
7 productive, such as was the case in the orange sand in
8 Section 28.

9 And that this map also will show in Section 20 at
10 our proposed location, our unorthodox location is moving
11 closer to the thickest portion of the channel, whereas the
12 standard location shown by the X is on the edges, and that
13 a location in the southwest quarter would be pretty much
14 out of the channel interpretation entirely.

15 Q. Mr. Shatzer, this exhibit shows that if you move
16 to the east from the proposed location, in fact, the sands
17 are thinning and you increase your risk; is that right?

18 A. If you move --

19 Q. If you move to the west, I'm sorry.

20 A. Move to the west. Yes, if you move to the west
21 the sands are thinning, and it greatly increases your risk.

22 Q. This also shows that it would be imprudent to
23 develop a south-half unit with a well located -- or an
24 attempt to locate a well on the southwest quarter?

25 A. Yes, that is correct.

1 Q. So for geologic reasons you really cannot move
2 from the standard location to the west or the southwest?

3 A. That is correct.

4 Q. Now, you've moved to the east. Were there
5 topographic conditions that required you to move from that
6 standard location?

7 A. Yes, there were also surface topographic reasons
8 that caused us to locate the well in a location further to
9 the east and south from the standard location of 1980 from
10 the south and east.

11 Q. Let's go to Mewbourne Exhibit Number 9. Would
12 you identify and review this for Mr. Morrow, please?

13 A. Exhibit Number 9 is a surveyor's plat of the
14 southeast quarter of Section 20. So this is on a 1-to-500
15 scale, quite a bit blown up from the geological maps that
16 I'm showing you, so that the entire picture here is merely
17 the southeast quarter of Section 20.

18 And the previous map showed why we didn't want to
19 drill in the southwest quarter, so here we're now confining
20 our view to the southeast quarter.

21 And that the locations that are -- We tried to
22 survey and stake locations. 1980 from the south and east
23 is shown with an arrow, and then also 1650 from the south
24 and 1980 from the east is also shown with an arrow. And
25 these were standard locations that were located too near to

1 the electric lines, are shown in the dashed with the "E",
2 all through this mapped area.

3 And then also the pipelines move from about the
4 center of the section in a southeasterly direction down to
5 the southeast corner. Those are a series of pipelines
6 cutting across the section. And in either case, the
7 standard locations were too close to these electric lines
8 and pipelines.

9 The proposed unorthodox location 1650 from the
10 south and 990 from the east is shown with an arrow over to
11 the east portion of this quarter section. And there we
12 found a location that was in the thicker portion of the
13 sand on the previous isopach map, Exhibit 8, and that it
14 also satisfied the requirement of being sufficiently
15 distanced from the electric lines and the pipeline.

16 Q. By moving to the unorthodox location, you have
17 proposed the well at a substantially better geologic
18 location, have you not?

19 A. Yes, we have.

20 Q. To move to the west from the standard location,
21 you would do just the reverse: You'd put yourself
22 virtually out of the structure?

23 A. Yes, that is correct.

24 Q. Are you prepared to make a recommendation to the
25 Examiner as to the risk penalty that should be assessed

1 against any nonparticipating interest owner in the well?

2 A. Yes.

3 Q. And what is that penalty?

4 A. 200 percent plus well cost.

5 Q. And that's based on the geologic interpretation
6 that you've presented to Mr. Morrow in this hearing?

7 A. Yes.

8 Q. Do you believe there is a chance that a well at
9 the proposed location could in fact not be a commercial
10 success?

11 A. Yes, that's a distinct possibility.

12 Q. In your opinion, will the granting of this
13 application and the drilling of a well at the proposed
14 location be in the best interest of conservation, the
15 prevention of waste and the protection of correlative
16 rights?

17 A. Yes.

18 Q. Were Exhibits 5 through 9 prepared by you or
19 compiled at your direction?

20 A. Yes.

21 MR. CARR: At this time, Mr. Morrow, we move the
22 admission of Mewbourne Exhibits 5 through 9.

23 EXAMINER MORROW: Five through 9 are admitted
24 into the record.

25 MR. CARR: And that concludes my direct

1 examination of Mr. Shatzer.

2 CROSS-EXAMINATION

3 BY MR. KELLAHIN:

4 Q. Mr. Shatzer, Exhibit 6, the structure map, that
5 doesn't play a significance in your decision, does it?

6 A. No significance other than risk increases as you
7 go downdip in terms of proving risk.

8 But as far as the difference between a standard
9 -- The structure is not significant, other than when
10 gas/water contacts in given reservoirs come into play.

11 Q. You don't see a gas/water contact at this point
12 in the development of this Morrow?

13 A. No.

14 Q. All right. So the objective is to get in the
15 Morrow channel, if you will, at the greatest point of sand
16 thickness to give you the greatest chance of improving the
17 odds of getting a commercial gas well?

18 A. Yes.

19 Q. All right. Other than the Morrow, when we look
20 in this area is there any potential in any other formation?

21 A. Yes, there have been numerous shows in the
22 terminal Penn section, and there are always possibilities
23 in this area. I don't -- There's one Bone Spring producer
24 on --

25 Q. I'm looking at Exhibit 5, and I just see one Bone

1 Spring and a Queen well in 8.

2 A. Right, and that's a -- it's a poor Bone Spring
3 well.

4 Q. So Exhibit 5 represents all the established
5 production from any zone in this area?

6 A. Yes.

7 Q. All right. Is part of your risk or your strategy
8 inclusive of any other formation, other than the Morrow?

9 A. As far as our strategy to locate the well, the
10 Morrow is the primary objective and the driving force. But
11 in terms of our interest in the area, we definitely have
12 had shows in other formations, and they do weigh in our
13 decisions.

14 Q. Is it sufficient enough that you have taken that
15 information on other zones and prepared geologic displays?

16 A. No, I really haven't -- They're not significant
17 enough to date that I have prepared displays.

18 Q. When we look at Section 20, there's a well
19 location symbol in the northwest quarter of 20.

20 A. Yes.

21 Q. What does that represent?

22 A. That represents the Illinois Camp "20" State
23 Number 1.

24 Q. What's the status of that well?

25 A. It's drilling presently.

1 Q. What was the basis for locating -- What's its
2 target formation?

3 A. The Morrow.

4 Q. What's the basis for locating that well in the
5 northwest quarter?

6 A. For the mapped thickness -- It shows on Exhibit
7 Number 8 that it has over 20 feet of gross sand, and so
8 therefore it's in the interpreted thick of the lower Morrow
9 channel system.

10 Q. All right. That well is targeted for the same
11 lower Morrow sand channel that you've shown on the cross-
12 section with the orange color?

13 A. Yes.

14 Q. And it represents that portion of the Morrow
15 that's isopach'd on Exhibit 8?

16 A. Yes. Well, the -- Its primary objective is both
17 the lower Morrow and the middle Morrow green sands. But
18 the -- It's both Morrow formations, any and all Morrow
19 sands.

20 Q. Does the well location in the southeast of 20,
21 the subject well, does that include any potential for the
22 middle Morrow?

23 A. Certainly there is some potential for the middle
24 Morrow, but we feel that the lower Morrow orange sand is
25 the primary objective.

1 Q. When you look at the cross-section, tell me
2 what's happening here.

3 A. What's -- I'm not sure I understand the question.

4 Q. Yeah, just -- Find the display and let me ask you
5 some questions.

6 A. Oh, all right. Okay, I have it out.

7 Q. When we look at 17, the well in the northwest
8 quarter of 17 --

9 A. Yes.

10 Q. -- your interpretation on the log shows a
11 potential in middle Morrow, the green, showed potential in
12 the lower Morrow, the orange sand?

13 A. Yes.

14 Q. In that well both zones were perforated?

15 A. Yes.

16 Q. In what sequence? Was it done together or
17 separately?

18 A. The lower Morrow orange was perf'd first, but the
19 perms in the middle Morrow green were added within a matter
20 of less than a week. So they were nearly done together.

21 Q. All right. So when we look at the Exhibit 5 and
22 look at the productivity of that well, that index up there
23 that shows 67 MMCF of gas --

24 A. Right.

25 Q. -- that is the cumulative gas from both zones?

1 A. Yes.

2 Q. Is that well still productive?

3 A. Yes.

4 Q. When we go to the next well in the cross-section,
5 the one in the southeast of 17 --

6 A. Yes.

7 Q. -- they have not yet perforated the middle green
8 sand?

9 A. That is correct.

10 Q. Do you see any behind-the-pipe potential in that
11 well, in that zone?

12 A. Yes, that should be productive.

13 Q. Okay. And then as we move past your well
14 location and look at the last well in the cross-section in
15 28, just the reverse: They're producing out of the green
16 or the middle Morrow sand?

17 A. Yes. Well, they're -- It's an inactive well now.
18 It only produced 42 million, a matter of a few months.

19 Q. They shut it in in March of 1989?

20 A. (Nods)

21 Q. Is there any potential in the other zone in that
22 well?

23 A. I don't think so. It doesn't look productive.

24 Q. Do you have an isopach of the middle Morrow?

25 A. Not with me. I mean, I -- It is something that

1 we've mapped before, but I felt like the south half of the
2 20 -- the "20" Number 2 location, that the orange was the
3 primary zone.

4 Q. Well, you have established production in the
5 middle green -- or the middle Morrow on the cross-section,
6 you've got some behind-the-pipe potential in that zone in
7 the closest well in 17. Can you tell me what that sand
8 distribution looks like in relation to the isopach of the
9 lower Morrow?

10 A. It's fairly difficult. The middle Morrow green
11 is not -- the channel, the regularity that the lower Morrow
12 orange is found as channels is much stronger than the
13 middle Morrow.

14 The middle Morrow is both found as bars that
15 trend northeast-southwest and as channel systems that are
16 oriented similar to the orange, northwest-southeast. So
17 its orientation is not quite as consistent as the orange.

18 Q. How do you as a geologist handle that problem
19 when you're looking at trying to find the best location in
20 a section and the configuration of the spacing unit? What
21 do you do?

22 A. It's very difficult.

23 Q. Well, how did you do it here?

24 A. I don't think -- First of all, I didn't do it
25 here. I didn't submit a map here because I don't think the

1 map is as strong as the lower Morrow.

2 Nor do I think the objective of the lower Morrow
3 is -- The lower Morrow is the stronger objective, as you
4 move farther away from the control than the middle Morrow,
5 for exactly those reasons, that it's less consistent in the
6 channel geometry.

7 Q. I'm just trying to understand your method of
8 analysis. I want to see how you've correlated, if at all,
9 the opportunity in the middle Morrow, which we see on the
10 cross-section, and how it has affected your choice or
11 decisions on where to locate your well. Has it affected
12 your choice of location?

13 A. On the location for the "20" Number 2 --

14 Q. Yes, sir.

15 A. -- it had little influence by the middle Morrow
16 green. It was mostly influenced by the lower Morrow
17 orange.

18 Q. All right. When we look at the isopach for the
19 lower Morrow, what is the purpose of your well location?
20 What's your objective geologically with that location?

21 A. The objective?

22 Q. Yes, sir.

23 A. To find clean lower Morrow channel sands.

24 Q. Of the greatest thickness?

25 A. Yes.

1 Q. All right. When you look at the isopach -- this
2 is a gross isopach -- is there any usefulness to you to
3 prepare any kind of net isopach?

4 A. Yes. I don't -- Well, no, I don't usually do net
5 isopachs on the lower Morrow, because the lower Morrow,
6 when it is over 15 feet thick in a continuous channel
7 sequence, it is not often tight. That is not the case with
8 the middle Morrow.

9 But in the lower Morrow, gross thickness mapping
10 is the preferred way, because porosity is usually
11 associated with thicknesses over 10 to 15 feet.

12 Q. Okay. When we look at the gross isopach, Exhibit
13 8, the well is located at a point that shows a thickness of
14 slightly greater than 15 feet?

15 A. Yes.

16 Q. If we get less than 15 feet, is that
17 unsatisfactory in your geologic analysis in which to drill
18 the well, or will you accept less than 15 feet?

19 A. Any thinning of the sands from this point
20 increases the risk.

21 Q. Yes, sir. At what point does it become so thin
22 or so risky that you don't drill the well for that spacing
23 unit?

24 A. I would say ten feet.

25 MR. KELLAHIN: Thank you, Mr. Examiner.

REDIRECT EXAMINATION

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BY MR. CARR:

Q. Mr. Shatzer, you've been involved with the drilling of other Morrow wells in this area, have you not?

A. Yes, I have.

Q. You don't know what you have in terms of any of these Morrow sands until you actually drill the well; is that a fair statement?

A. Yes, that is correct.

Q. And until you've actually drilled the well and know your development activity, there's a certain amount of risk?

A. There's a great amount of risk.

Q. And you are carrying that risk in developing these properties for those interest owners who haven't voluntarily joined in the well?

A. Yes.

MR. CARR: That's all I have.

EXAMINATION

BY EXAMINER MORROW:

Q. Mr. Shatzer, does your company plan to get the well in the north half to TD and evaluated before you drill the one in the south half?

A. To -- ?

Q. Do you plan to finish the well you're currently

1 drilling in Section 20 before you begin this one?

2 A. Yes.

3 Q. I wanted to ask you about the control you had in
4 Section 20 on your isopach map, but there doesn't appear to
5 be any wells to the east or the west there to justify the
6 thinning of the sand there in the west half -- or to the
7 extent that it's drawn there. Could you explain that for
8 me, please?

9 A. That's absolutely correct. There's a great
10 amount of risk in terms of there's no well control in much
11 of the south half of this area.

12 I've worked the Morrow for nearly 18 years,
13 however, in this area extensively, and so we have to rely
14 on analogy with other channel systems, such as the one
15 that's found in the northeast portion of this map, as far
16 as geometry of the channel and the channel thickness, how
17 wide would it be? We rely on those types of things where
18 we don't have well control in this area of risk.

19 Q. Okay. Well, I know you have to do the best you
20 can when you don't have control, but it seems like you've
21 kind of pinched in there where the one to the northeast is
22 more or less completely northeast-southwest -- or
23 northwest-southeast. The trend there of the thickness
24 appears to be different than it is at the target location.

25

