

NEW MEXICO OIL CONSERVATION DIVISION

STATE LAND OFFICE BUILDING

STATE OF NEW MEXICO

Docket No. 3-93

Case No. 10656

IN THE MATTER OF:

Application of Mitchell Energy
Corporation for compulsory pooling
and an unorthodox gas well location,
Lea County, New Mexico

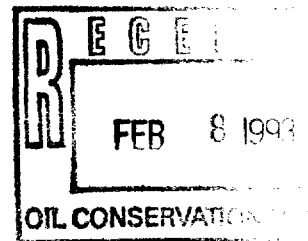
BEFORE:

EXAMINER MICHAEL E. STOGNER

January 21, 1993

REPORTED BY:

DEBORAH O'BINE
Certified Shorthand Reporter
for the State of New Mexico



CUMBRE COURT REPORTING

P.O. BOX 9262

SANTA FE, NEW MEXICO 87504-9262

(505) 984-2244

A P P E A R A N C E S

FOR THE NEW MEXICO OIL CONSERVATION DIVISION:

ROBERT G. STOVALL, ESQ.

General Counsel

State Land Office Building

Santa Fe, New Mexico 87504-2088

FOR MITCHELL ENERGY CORPORATION:

KELLAHIN & KELLAHIN

117 N. Guadalupe

Santa Fe, New Mexico 87501

BY: W. THOMAS KELLAHIN, ESQ.

FOR STRATA PRODUCTION COMPANY:

STRATTON & CAVIN, P.A.

P.O. Box 1216

Albuquerque, New Mexico 87103

BY: SEALY H. CAVIN, JR., ESQ.

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1 EXAMINER STOGNER: At this time I'll call
2 Case No. 10656.

3 MR. STOVALL: Application of Mitchell
4 Energy Corporation for compulsory pooling and an
5 unorthodox gas well location, Lea County, New Mexico.

6 EXAMINER STOGNER: Call for appearances?

7 MR. KELLAHIN: Mr. Examiner, I'm Tom
8 Kellahin of the Santa Fe law firm of Kellahin &
9 Kellahin, appearing on behalf of the Applicant,
10 Mitchell Energy Corporation. I have three witnesses
11 to be sworn.

12 EXAMINER STOGNER: Any additional
13 appearances?

14 MR. CAVIN: Mr. Examiner, my name is Sealy
15 Cavin. I'm an attorney with the Stratton & Cavin law
16 firm in Albuquerque. I'm representing Strata
17 Production Company, and I have two witnesses.

18 EXAMINER STOGNER: Any other appearances?

19 Will the witnesses please stand and be
20 sworn at this time?

21 (Thereupon, the witnesses were sworn.)

22 EXAMINER STOGNER: Mr. Kellahin?

23 MR. KELLAHIN: Thank you, Mr. Examiner.
24 During the break, Mr. Examiner, Mr. Stovall and Mr.
25 Cavin and I discussed potential issues for

1 consideration by the Division Examiner in this
2 compulsory pooling case, which also includes a request
3 for an orthodox gas well location.

4 In trying to identify the issues, Mr. Cavin
5 has raised a notice question, and subject to your
6 desires perhaps we ought to address the notice issue
7 first. Mr. Cavin has made mention of it in his
8 prehearing statement, and I would suggest that if he
9 desires to raise an issue about notice, that he ought
10 to go forward and describe for us what his concern is
11 with regards to notification. Let us deal with that
12 issue and, based upon the outcome of that issue,
13 determine whether we go forward or whether some other
14 solution is appropriate.

15 EXAMINER STOGNER: Mr. Cavin?

16 MR. CAVIN: Yes, Mr. Examiner. Our notice
17 issue goes to the question of whether, in connection
18 with compulsory pooling action, Mitchell has
19 adequately notified all interest owners in the west
20 half of Section 28. We have advised on several
21 occasions -- we have advised Mitchell there is a
22 Strata -- Mr. Mark Murphy, who will be called as a
23 witness, has advised Mitchell on several occasions
24 that there are various partners in a particular lease
25 that Mitchell seeks to force pool. We have indicated

1 to Mitchell that we would -- while we were trying to
2 strike an agreement, try to coordinate the deal
3 between the various partners. When the deal fell
4 apart, we told Mitchell in good faith that we couldn't
5 speak for the partners, if there was going to be a --
6 if it would be necessary to go forward with the forced
7 pooling, that they would need to notify the partners.

8 At that time we sent them a list of the
9 partners and their addresses and I believe suggested
10 they may want to contact these parties. We believe
11 these parties are entitled to notice, and we cannot
12 speak for their interest at this time, Mr. Examiner.

13 MR. KELLAHIN: In response, Mr. Examiner,
14 let me submit to you part of my tender of proof on
15 this issue. To aid you in understanding what Mr.
16 Cavin's concern is, let me show you what is going to
17 be Exhibit No. 6. It's simply an ownership plat.

18 Mitchell's proposal is to formulate a
19 320-acre gas spacing unit. There is not yet gas
20 spacing in Section 28. We are proposing to orient the
21 spacing unit so that there is a west half dedication.
22 The ownership within the section is such that Mitchell
23 has consolidated on a voluntary basis all ownership
24 with the exclusion of the south half of the southwest
25 west quarter. It's an unshaded tract, and it's

1 labeled "Strata."

2 Our tender of proof is that based upon a
3 title opinion rendered to Mitchell Energy by the
4 Hinkle law firm, that as of the date of the
5 application and as of the date the application for
6 compulsory pooling was served on Strata, which is
7 December 9, that Strata Production Company was the
8 owner of the operating rights for that particular
9 federal lease.

10 That during the course of the negotiations,
11 our landman will testify that Strata represented that
12 they had the ability to make deals on behalf of the
13 operating interest for that lease. And that while
14 there may be other partners of Strata, they were
15 undisclosed to us. It was not until negotiations
16 terminated unsuccessfully, that by letter dated
17 January 13, we were informed that Strata now was
18 telling us they had other interest owners that would
19 hold operating rights.

20 Application was filed on December 7.
21 Strata was served on the 9th. The case was originally
22 scheduled for the 7th of January, was continued to
23 this docket to give the parties additional time in
24 which to see if they could come to an agreement.

25 In addition, we will submit to you as part

1 of our proof a certificate from a certified abstract
2 company that does business in Lea County, New Mexico,
3 that has attested to the fact that they've made a
4 search of the public records of Lea County, New
5 Mexico, from a period beginning November 6 of '92,
6 ending January 19, 1992, and it shows that Strata
7 Production Company is still the owner of all those
8 operating rights.

9 Our point is the last-minute effort to
10 disburse their interests simply frustrates our efforts
11 to consolidate the interest and to formulate on a
12 compulsory pooling basis the drilling of the well. We
13 believe we've complied with the notice requirements.
14 We have dealt in good faith with Strata Production
15 Company. And it is not our obligation now to go out
16 and search and find these now disclosed parties that
17 Strata says we are now obligated to seek.

18 The certificate is here for your
19 consideration.

20 MR. STOVALL: Mr. Cavin, you are not
21 representing these other parties; is that correct?

22 MR. CAVIN: No, sir.

23 MR. STOVALL: Mr. Examiner, I don't think
24 that at this time it's necessary to rule on that
25 matter, quite frankly. Strata is here and appearing.

1 The other parties -- if a pooling order is entered,
2 the parties may object to that order as not being
3 applicable to them. And if Mitchell goes forward,
4 chooses to go forward at this time, it does so with
5 the risk, knowing that there may be other parties out
6 there at this time who possibly were entitled to
7 notice.

8 And without making that determination, I
9 would say that at this time Mitchell may go forward,
10 if it so desires, and that those other parties, if Mr.
11 Cavin doesn't speak for them, will have to assert
12 their interest. And Mitchell needs to be aware that
13 that may happen, and they may come back in here and
14 have to do it again. But so I would say that the
15 decision is up to Mitchell at this point.

16 Only those interests over whom the
17 Commission has jurisdiction will be pooled, and
18 whether it has jurisdiction over those interests is
19 not a decision that has to be addressed today because
20 there's --

21 MR. KELLAHIN: I beg to differ with Mr.
22 Stovall. I think it's critically important for us to
23 know before we go through this exercise if we are
24 pooling Strata and the 25 percent working interest
25 ownership in that lease or whether we're only pooling

1 Strata as to 18.5 percent. I think that makes a
2 material difference as to what we do. We think we
3 have a tender of proof that meets the requirements on
4 notification. And I disagree with Mr. Stovall. I
5 think we need some decision from the examiner as to
6 whether we've notified the proper properties.

7 MR. CAVIN: Might I interject, Mr.
8 Examiner? We agree that there is a due process
9 question as to these interest owners that were
10 previously identified to Mitchell as far back as
11 October 26. Perhaps they were identified in generic
12 terms, but they were nonetheless advised that they
13 were silent partners.

14 It is not unusual, as you know, to have
15 other recorded interests, and we, Strata, did its best
16 to advise Mitchell of this situation. In fact, under
17 the definition of the federal regulations, these
18 parties do in fact have operating rights even though
19 they're not reflected in the public records.

20 We would be happy to submit that to the
21 Division.

22 EXAMINER STOGNER: I suppose you have a
23 land witness prepared today to testify on their work
24 to contact all unleased parties at this point; is that
25 correct, Mr. Kellahin?

1 MR. KELLAHIN: Yes, sir, and our testimony
2 is that party is Strata. And while they said they had
3 other interest owners, as late as January 12, they
4 represent that those interest owners are undisclosed
5 to us. And so that is the issue is whether, having
6 dealt with and exhausted the efforts with Strata, and
7 been unsuccessful to get a voluntary agreement because
8 they now disclose to us on the 15th of January -- 13th
9 of January, some 15 other individuals and entities,
10 must we now restart the process and go and try to find
11 those people?

12 MR. CAVIN: Mr. Examiner, if I might,
13 Strata -- and I don't think there's been any
14 indication otherwise -- has offered to provide these
15 names. Mitchell has not pursued that. And it wasn't
16 until -- and we also did not indicate that we had the
17 authority to speak for these individuals. We
18 indicated that we would try to work a deal. And
19 that's what we were doing in a good faith effort.
20 When the deal came apart, we said, look, this is
21 getting too complicated. You're going to have to go
22 to these parties directly. Frankly, some of them may
23 want to participate, some of them you may just have to
24 force pool, and others may accept the farm-out terms.
25 And it's incumbent on the applicant, it

1 seems to me, and certainly we would take that position
2 if we were force pooling, to contact anybody that we
3 were aware of. It's not just constructive notice of
4 the record. It's actual notice that you receive in
5 the process.

6 EXAMINER STOGNER: That's part of the
7 forced pooling provisions and part of the forced
8 pooling statutes in which a reasonable determination
9 or reasonable effort was made, and I think we can hear
10 that today and that determination can be made. And,
11 as always, any party who doesn't feel they're up to
12 the forced pooling provision, they can seek the
13 Division's assistance or the provisions either through
14 hearing or whatever means, but obviously we have them
15 here today, and we haven't made that determination yet
16 by listening to any of the testimony.

17 Mr. Kellahin?

18 MR. KELLAHIN: We're ready to go forward.

19 EXAMINER STOGNER: Are there any other
20 issues, Mr. Stovall, that you see -- that you
21 mentioned prior?

22 MR. STOVALL: No. I think if you're
23 prepared to go with the land case and then, I think --
24 the legal issue I see here, and I think Mr. Cavin is
25 raising -- and, Mr. Kellahin, get your response to

1 this -- it appears that you have complied with the
2 requirements with respect to notifying all those
3 having a record title interest?

4 MR. KELLAHIN: Yes, sir.

5 MR. STOVALL: Are you required to notify
6 those -- two questions is, have you been given actual
7 notice of interests which are not recorded; and,
8 secondly, are you required to notify those interests?
9 To what extent do they have due process rights to
10 receive notice; is that correct?

11 MR. KELLAHIN: And then as an additional
12 item, whether or not Mitchell could rely on what they
13 believe were representations by Strata that Strata was
14 representing all those undisclosed interests as we
15 dealt with this issue. And if you make that
16 determination, then we don't have any obligation to
17 notify these undisclosed people.

18 MR. STOVALL: Mr. Kellahin, again, the only
19 question I would ask you is what if one of these
20 undisclosed parties comes back in and seeks an order
21 from the Commission that their interests have not been
22 pooled by the order because they did not receive
23 notice?

24 MR. KELLAHIN: We would obviously have to
25 have a hearing and discuss that issue, but our defense

1 is that their interest is bound by the activities of
2 Strata.

3 MR. STOVALL: I think we need to go forward
4 with the land testimony to flesh out the facts.

5 MR. CAVIN: We can say without
6 equivocation, their interests are not bound by Strata,
7 and if there is a case for misrepresentation, I doubt
8 that this is the forum for that.

9 We would also also assert that Strata has
10 not represented that. We have made a good faith
11 effort. We continued until the 13th. Just so long as
12 everyone is aware of that as we press into this.
13 We're perfectly willing to hear this case today. I
14 can also assure you that there will-- I would be
15 surprised if none of these parties objects to not
16 having notice. And I just say that for the record
17 today.

18 MR. KELLAHIN: One final point. Mr.
19 Cavin's representation is inconsistent with the
20 proof. There is a December 20 letter from his client
21 that purports an arrangement and attaches to it the
22 federal assignment form by which, if we accept their
23 proposal, they are prepared to execute that assignment
24 form on behalf of the full 25 percent working
25 interests. You can't have it both ways, Mr. Examiner.

1 MR. CAVIN: It also states there are
2 undisclosed owners, that we have been in contact with
3 these owners and we have tried to -- it expresses that
4 in black and white. And it's consistent with the
5 whole pattern. There are undisclosed owners. We have
6 tried to work out a deal. Where we can't work out
7 this deal, we said, look, this thing is too
8 complicated. You're going to have to deal with these
9 people directly. We set that forth in the agreement
10 precisely. Our correspondence is consistent. All the
11 telephone conversations are consistent. And it was
12 just a lazy landman that didn't want to contact these
13 folks. We would have been happy to give the
14 information --

15 MR. STOVALL: Let's pass on those kind of
16 judgments, Mr. Cavin.

17 MR. KELLAHIN: That's unfair.

18 MR. STOVALL: I guess the question is, we
19 don't even know at this point whether the people have
20 the property interests which is -- we don't have a
21 record on that. So let's proceed with the land case,
22 and the records we have before us at this point show
23 no interest other than Strata, and so therefore we
24 don't even know who they are.

25 Mr. Cavin, I will advise that you cannot

1 represent these people because you are -- you have
2 represented to this Division this morning that you do
3 not represent these people.

4 MR. CAVIN: That's true.

5 MR. STOVALL: There's a little bit of a
6 problem there as far as your now taking up their flag.

7 MR. CAVIN: I am not attempting to
8 represent these parties at this hearing. I want to
9 make that perfectly clear. If there's any
10 misunderstanding on that, I would state that for the
11 record.

12 MR. KELLAHIN: My choice of presentation is
13 to present the geologic data first. That's the heart
14 of the case. We're interested in the geology by which
15 we fully develop the section, and I'm going to call
16 Mr. Gawloski first rather than deal with the land
17 testimony.

18 EXAMINER STOGNER: I'd rather hear the land
19 testimony at this time because, after all, there is a
20 separate issue here. Granted, geology and engineering
21 and the overhead charges, but we need to proceed with
22 the land testimony at this time and get these other
23 issues raised up because if there is a problem, why
24 hear the other things at this point?

25 MR. KELLAHIN: Well, that's my point.

1 We're raising this in terms of response to Mr. Sealy's
2 motion. My tender of proof on behalf of the landmen
3 is what I've summarized at this point. And if we're
4 going to address the notice issue, then I need to draw
5 him out of the regular sequence of presentation, and
6 we'll talk about the notice.

7 MR. STOVALL: It's unusual. Normally, the
8 land testimony comes first in most forced poolings.

9 MR. KELLAHIN: I understand.

10 MR. STOVALL: And probably the reason for
11 that is because the fundamental issue in the previous
12 case is, you know, is there an agreement and has there
13 been any good faith negotiations.

14 MR. KELLAHIN: I had understood the
15 fundamental issue in this case was the orientation of
16 the spacing units.

17 MR. STOVALL: That's the issue between the
18 parties.

19 MR. KELLAHIN: Yes, sir.

20 MR. STOVALL: The issue before the
21 Commission is you've got to have the basis for a
22 forced pooling order in the first place before you get
23 into the issues of how will that order be drafted.

24 MR. KELLAHIN: It's already admitted
25 between these two parties that they can't come to an

1 agreement despite their efforts to do so. And the
2 only remaining issue is whether Strata represented the
3 25 percent or whether they don't. And if they don't,
4 then we need to go back and find the rest of them.

5 EXAMINER STOGNER: I don't see any reason
6 why we have to veer from the norm. I think the land
7 testimony at this time is appropriate.

8 MR. KELLAHIN: If you'll excuse the fact
9 that the exhibits are numbered in the sequence such
10 that the geologic displays are first, we'll present
11 Mr. Steve Smith, who is the landman, first,
12 recognizing that the numbers are out of sequence.

13 EXAMINER STOGNER: It will be noted.

14 MR. KELLAHIN: With your permission.

15 EXAMINER STOGNER: You have my permission.

16 MR. KELLAHIN: Let me call Steve Smith.

17 If I might, before we start, I'd like to
18 apologize for my comment towards Mr. Smith.

19 EXAMINER STOGNER: The record will so
20 note.

21 Just for the record, Mr. Kellahin, your
22 Exhibits are 5 through 19; is that correct?

23 MR. KELLAHIN: Mr. Smith is going to talk
24 about Exhibit 6. Exhibit 5 had to do with the
25 topographic constraints on the surface. Mr. Smith

1 will talk about Exhibit 6, and then he will take us
2 through, I want to say 17. I have an engineer here to
3 authenticate the AFE. Mr. Smith will also talk about
4 the certification, which is Exhibit 19.

5 EXAMINER STOGNER: Exhibits 6 through 17
6 and Exhibit 19 will be the topics for this witness.

7 Mr. Kellahin?

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

9 STEPHEN J. SMITH,
10 the witness herein, after having been first duly sworn
11 upon his oath, was examined and testified as follows:

12 EXAMINATION

13 BY MR. KELLAHIN:

14 Q. Mr. Smith, for the record, would you please
15 state your name and occupation?

16 A. My name is Stephen J. Smith. I'm a senior
17 landman for Mitchell Energy Corporation.

18 Q. Where do you reside, sir?

19 A. Midland, Texas.

20 Q. Have you on prior occasion testified as an
21 expert petroleum landman before the Oil Conservation
22 Division?

23 A. Yes, I have.

24 Q. Summarize for us your experience as a
25 petroleum landman for your company.

1 A. I went to work for Mitchell Energy
2 Corporation in 1985. I spent six months, a little
3 over six months in their Denver office as a senior
4 landman and was transferred to Midland in April of
5 1986. I have functioned as a senior landman in that
6 office since then, working areas mostly in southeast
7 New Mexico, but I also do work in Texas as well.

8 Q. Describe for us in a general way the kinds
9 of documents, instruments, and negotiations that you
10 deal with on a regular daily basis in the course of
11 performing your duties as a petroleum landman.

12 A. Fee oil and gas leases, checks of fee title
13 to minerals, federal and state ownership checks. I
14 negotiate farm-ins and farmouts between oil and gas
15 partners, terms of operating agreements. It's the
16 full gamut that landmen are expected to do.

17 Q. Were you the principal landman on behalf of
18 your company that negotiated with the working interest
19 owners for the formulation of a spacing unit on a
20 voluntary basis for the west half of Section 28 that's
21 the subject of this hearing?

22 A. Yes, I was.

23 MR. KELLAHIN: We tender Mr. Smith as an
24 expert petroleum landman.

25 EXAMINER STOGNER: Are there any objections

1 to Mr. Smith's qualifications?

2 MR. CAVIN: No, Mr. Examiner.

3 EXAMINER STOGNER: Mr. Smith is so
4 qualified.

5 Q. (BY MR. KELLAHIN) Mr. Smith, let me have
6 you turn to what is marked as Mitchell Exhibit No. 6.
7 Identify that for me, please.

8 A. That is a blow-up of the Midland map
9 representing the leasehold ownership centering Section
10 28, Township 20 South, Range 33 East, Lea County, New
11 Mexico.

12 Q. Have you independently verified the
13 accuracy of the information shown within the
14 boundaries of Section 28 in terms of the configuration
15 of those leases?

16 A. Yes, I have.

17 Q. Looking entirely at Section 28 and starting
18 wherever you choose to start, show us how that tract
19 is divided in terms of the leasehold.

20 A. Well, Mitchell Energy Corporation and its
21 partners own 100 percent of the federal leases in the
22 north half northeast quarter, the southeast northeast
23 quarter, and the north half southeast quarter, that
24 being Federal Lease 62228.

25 As to the federal lease covering the

1 northwest quarter and the northeast southwest quarter,
2 Mitchell Energy Corporation and its partners have 100
3 percent of the operating rights below 3,500 feet.

4 And as to the northwest southwest quarter,
5 Mitchell and its partners have 100 percent of the
6 operating rights as to the federal lease to all
7 depths. There is an unleased federal tract, being the
8 southwest northeast quarter.

9 Q. And that's the approximately 40-acre tract
10 that is uncolored and totally surrounded by yellow
11 shading?

12 A. That's correct.

13 Q. Continue.

14 A. Based upon my check of the county records
15 and instruments provided to us from the federal
16 abstract company and the county abstract, Strata
17 Production Company is the record title owner and owner
18 of 100 percent of the operating rights to the south
19 half southwest quarter and the southwest southeast
20 quarter of Section 28. And there is also a federal
21 lease in the southeast southeast quarter, being 40
22 acres, and it's owned by Pitch Energy Corporation.

23 Q. Let me ask you, in examining the documents
24 that affect the opportunity to participate on a
25 voluntary basis in a well to be drilled to depths

1 below the top of the Wolfcamp targeting the Morrow in
2 the west half of 28, did you find any voluntary
3 agreements entered into by any of the working interest
4 owners that would have affected their interest in the
5 west half?

6 A. There is an operating agreement in place
7 between Mitchell Energy Corporation and the partners
8 covering all of Section 28 and the majority of this
9 township and range and parts of surrounding townships
10 and ranges that governs the interaction and
11 development of any wells drilled in the area between
12 the parties to that agreement.

13 Q. When you talk about the Joint Operating
14 Agreement affecting all of 28, does that include any
15 interest for the federal lease identified in the south
16 half of the southwest quarter?

17 A. No. It only covers the interests colored
18 in yellow, being the interests owned by Mitchell
19 Energy Corporation and its partners.

20 Q. Who are the parties to the Joint Operating
21 Agreement that you describe?

22 A. Mitchell Energy Corporation is named as
23 operator of this operating agreement, and we have a 50
24 percent interest in the leasehold. Santa Fe Energy
25 Operating has a 25 percent interest in the yellow

1 acreage, and Maralo, Inc., has a 25 percent in the
2 yellow acreage as well.

3 Q. Has the well that is the subject of this
4 hearing been proposed to the interest owners pursuant
5 to the Joint Operating Agreement?

6 A. Yes, it has.

7 Q. And what decision have those interest
8 owners made with regards to this well?

9 A. They have agreed to participate in this
10 well pursuant to the operating agreement.

11 Q. Have they approved the authority for
12 expenditures of the well?

13 A. Yes, they have.

14 Q. And they have agreed upon the well
15 location?

16 A. Yes, they have.

17 Q. And they have agreed upon the formation of
18 the west half as the spacing unit for the well?

19 A. Yes, they have.

20 Q. What efforts have you made to identify the
21 working interest owners that would be able to commit
22 their interest for the west half of 28 that are not
23 currently committed under the Joint Operating
24 Agreement?

25 A. We conducted a search of the county and

1 federal records in order to determine who had record
2 title.

3 Q. As part of the ordinary custom and course
4 of doing business with your company, do you retain
5 outside counsel to prepare title opinions with regards
6 to drill sites and spacing units?

7 A. Always.

8 Q. And did you do so in this case?

9 A. Yes, we did.

10 Q. Let me ask you to turn to Mitchell Exhibit
11 No. 7 and identify that document?

12 A. That is a title opinion dated December 29,
13 1992, rendered for Mitchell Energy Corporation by Mr.
14 William B. Burford of the Hinkle, Cox, Eaton, Coffield
15 & Hensley law firm.

16 Q. The opinion is voluminous, and you have
17 only attached the first six pages?

18 A. That's correct. And it purports to cover
19 all interests in the west half except for depths above
20 3,500 feet as to Tract 1 identified on that title
21 opinion. And we requested that they exclude those
22 depths because we had no ownership in them.

23 Q. Based upon your own information, what had
24 you determined to be the working interest owners for
25 that portion of Section 28 that's identified as being

1 included in the south half of the southwest quarter?

2 A. Could you restate your question, please.

3 Q. Yes, sir. Based upon your information,
4 whom did you believe or what entity did you believe
5 controlled the operating rights for the south half of
6 the southwest quarter?

7 A. Based upon the best information obtainable
8 on the records indicated that Strata Production
9 Company owned those rights.

10 Q. Then as of December 29th when Mr. Burford
11 rendered his opinion, did he come to any different
12 conclusion than you have?

13 A. No, he did not.

14 Q. Have you subsequently taken additional
15 action to verify whether there was placed of record in
16 Lea County, New Mexico, any assignments, transfers, or
17 conveyances from Strata Production Company that would
18 disclose the identity and the address of subsequent
19 interest owners for that tract?

20 A. Once we were put on notice by Strata
21 Production Company of their desire to scatter this
22 lease to the wind, we obtained a limited certificate
23 from Elliott & Waldron Abstract Company, who prepared
24 the base abstract examined by Mr. Burford to
25 complement that abstract, to come forward from the

1 closing date which is stated in this title opinion as
2 to the fee tract, November 6, 1992, at 9:00 a.m.,
3 coming forward from that date through January 19,
4 '92.

5 And the search was conducted specifically
6 to determine whether or not Strata had assigned out
7 any interest to any parties. And the conclusion
8 rendered in this limited certificate is, of course,
9 they have not.

10 Q. And that is through the ending of what
11 particular date?

12 A. December 19, 199- -- well -- there appears
13 to be a typographical error.

14 Q. Yes, it's obviously a typo.

15 A. It should be -- its date, 1993, January 19,
16 1993, at 7 a.m.

17 Q. You mentioned awhile ago, Mr. Smith, that
18 Strata disclosed to you the identity of these
19 previously undisclosed interest owners?

20 A. Yes.

21 Q. When did they do that?

22 A. By letter dated January 13, 1993, received
23 by Mitchell on January 14, 1993.

24 Q. Prior to that time, Mr. Smith, had Strata
25 or anyone representing Strata disclosed to you the

1 identity and the address of those partners?

2 A. No, they had not.

3 Q. What was your understanding and belief with
4 regards to the appropriate party with whom to enter
5 negotiations for the commitment of that operating
6 interest in the south half of the southwest quarter?

7 A. Based upon the information we obtained from
8 the records, Strata appeared to be the 100 percent
9 owner. We contacted them and entered into
10 negotiations.

11 It was stated early on by Strata, by Mr.
12 Murphy, that they did have silent partners, but at no
13 time did he indicate that we would have to have their
14 joinder in order to enter into any agreement; that
15 throughout all of our negotiations, until the very
16 end, he represented himself as having the capacity to
17 enter into agreements binding all the parties should
18 we have reached agreement as to terms.

19 Q. Let me interrupt you for a moment and go
20 now to Mitchell Exhibit 9, which is the next Exhibit
21 in sequence?

22 A. Okay.

23 Q. Identify and describe for me what Exhibit 9
24 means to you.

25 A. Exhibit 9 is a letter, an internal

1 memorandum, to me from Mrs. Harriet Minton. Mrs.
2 Minton is the assistant manager of Joint Venture
3 Accounting for our corporation. And among other
4 things, her responsibilities include overseeing the
5 accounting procedures involved in joint operated
6 properties, which includes overseeing the overhead
7 rates charged under operating agreements.

8 And the letter represents, at my request,
9 she looked at the operating agreement that's in place
10 that I previously described between Mitchell and its
11 partners. It covers a large part of this area, under
12 which there are currently two producing wells, both in
13 the Morrow, and looked at the overhead rates that were
14 stated in that operating agreement, and provided me
15 with a summary of the escalations of the overhead
16 rates from the effective date, September 1, 1989, to
17 the present to show what current overhead rates are
18 currently being charged under that operating
19 agreement.

20 Q. Having received that information, do you
21 have a recommendation to the examiner as to the
22 overhead rates you're seeking to have applied in this
23 compulsory pooling case?

24 A. Yes, I do. Based upon the fact that the
25 parties that have agreed to participate in this well

1 under this operating will be charged the rates stated
2 at the bottom of the two drilling and producing rate
3 summaries, we would recommend that Strata be also
4 charged the same overhead rates being for a drilling
5 well, \$6,470, and for a producing well, \$647.

6 Q. If the Examiner adopts your recommendation,
7 that level of rate will be consistent then with the
8 rate being charged those interest owners voluntarily
9 committing their interest under the existing Joint
10 Operating Agreement?

11 A. That is correct.

12 Q. Let's turn now specifically, Mr. Smith, to
13 your efforts to obtain Strata Production Company's
14 voluntary participation.

15 A. Okay.

16 Q. And without going into great detail about
17 all the correspondence and telephone calls, let me ask
18 you when you first provided written opportunity to
19 Strata specifically proposing this well and this
20 spacing unit, submitting to them an AFE and asking
21 them, as one of their choices, to voluntarily
22 participate in the well. Did you do that?

23 A. Yes, we did.

24 Q. When?

25 A. By letter dated November 20, 1992.

1 Q. And how is that marked?

2 A. It's Exhibit 10.

3 Q. Did you provide to Strata any other options
4 or alternatives in addition to participating --

5 A. Yes, sir.

6 Q. -- by paying their share of the cost of the
7 well?

8 A. Yes, we did. We offered them as an
9 alternative an industry standard, what we consider an
10 industry standard farmout.

11 Q. Did you provide them, in addition to a
12 farmout, any other options to handle their interest in
13 the spacing unit?

14 A. Not at that time.

15 Q. What, if any, response did you receive to
16 the November 10 letter?

17 A. I received a written response from Strata.
18 That written response is a letter dated December 9,
19 1992, marked Exhibit 11.

20 Therein Strata offered to Mitchell Energy
21 Corporation terms to either buy their oil and gas
22 lease that are stated in there, or, in the
23 alternative, they offered to farm out to Mitchell
24 Energy Corporation under substantially the same terms
25 proposed by Mitchell Energy Corporation by letter

1 dated November 20. However, the main difference in
2 their letter or in their proposal to farm out was that
3 they would retain an increased overriding royalty
4 interest above and beyond that proposed by Mitchell.

5 Q. You're describing the Strata letter of
6 December 9, Exhibit No. 11?

7 A. That's correct.

8 Q. What did you do in response then to this
9 letter? How did you reply to Mr. Murphy?

10 A. Well, first, as we always do, I had to seek
11 Mitchell management's approval to do anything. We
12 contacted the people in our Woodlands office to tell
13 them what the terms were and seek their approval for a
14 trade. We did that.

15 They approved, accepting Strata's farmout
16 as written, and verbally asked me to make sure that it
17 was clearly understood, as it clearly states here,
18 that if anyone under the terms of this farmout
19 proposal wanted to back in under the terms of that
20 farmout, that they would have to convert 100 percent
21 of their override. That means that they couldn't keep
22 a portion of their override and convert the other
23 portion for a working interest. And it clearly stated
24 that. It was just simply to make sure all parties
25 understood that.

1 Q. What had you thought you had done then in
2 response to Mr. Murphy's letter of December 9? Had
3 you fully examined the options that he had presented
4 to your company with regards to forming a voluntary
5 unit?

6 A. Yes, we had.

7 Q. And were any of those options acceptable to
8 you, or did you make a counterproposal to him?

9 A. No. We decided to take their second option
10 listed in their letter, and I made a phone call to Mr.
11 Murphy and informed him that Mitchell Energy
12 Corporation would take the terms of his farmout as
13 proposed.

14 Again, I restated, wanted to make sure it
15 was clear that everybody understood that all parties
16 had to convert 100 percent of their override for
17 working interest.

18 Q. Were you able to take that information and
19 discussion and reduce it to a written document that
20 all parties were willing to execute?

21 A. No, we weren't. When I called Mr. Murphy
22 to tell him that, he reminded me, and as it states in
23 his letter and as it states in all of my letters, that
24 the terms stated in his letter were subject to
25 approval by his partner. He informed me that, while

1 he felt he had the authority to write the letter, he
2 did have to seek his partners' approval. He felt he
3 stood a better chance of obtaining their approval if
4 Mitchell Energy Corporation would buy their lease.

5 And we got into a discussion about, you
6 know, that's all good and well, but we've got a deal
7 here. And the terms proposed in your December 9
8 letter for buyout were unacceptable. That's why we
9 didn't take that option. We discussed perhaps
10 Mitchell making them the very best cash offer to buy
11 out Strata.

12 Q. At this point did Mr. Murphy notify you
13 that you were going to have to deal directly with
14 these undisclosed interest owners that shared his
15 interest?

16 A. No, he did not.

17 Q. What then happened?

18 A. Well, he told me to, you know, go back to
19 your management and see what you can do and call me
20 back. And I did that.

21 Again, we went back to our management in
22 Woodlands and told them what had been discussed, and
23 that Strata, rather than farming out, even though they
24 had offered one, would still rather sell, and they had
25 asked us to make them our best cash offer to buy their

1 lease. They, in turn, gave me authority to make
2 Strata an offer to buy their lease.

3 Q. How did we get from the December 9 letter,
4 which is Exhibit 11, to the December 30 letter, which
5 is Exhibit 12?

6 A. There were various phone calls after
7 receiving the December 9 letter and after Mr. Murphy's
8 and my telephone conversation where he asked us to
9 make him an offer. I called him back at some later
10 date between those December 9th and 30th dates and
11 told him that I had in fact received authority to buy
12 their lease and offered to do that, paying Strata \$150
13 per net acre, being a total of \$18,000, and Strata, in
14 turn, could also retain an override equal to the
15 difference by which 20 percent exceeded lease burdens,
16 thereby assigning Mitchell an 80 percent net revenue
17 lease.

18 Q. Let me talk to you for a moment about the
19 cash offer.

20 A. Right.

21 Q. Based upon your experience in this area,
22 what does \$150 an acre represent to you as being a
23 fair and competitive price by which to acquire this
24 kind of interest?

25 A. It is higher than what we've paid in the

1 area, but in the interest of compromise, we decided it
2 would perhaps be better to buy Strata out and have 100
3 percent of the proration unit, take over control, and
4 march on down the road.

5 Q. What were you accustomed to paying to
6 acquire all rights at all depths from the surface to
7 the base of any production?

8 A. I acquired most of the leasehold in
9 Township 22 South, 33 East, that Mitchell has in
10 various acquisitions and paid probably on average
11 around \$85 per net acre on assignments covering all
12 depths, and on average received net revenues of around
13 82 percent in those assignments, 82-1/2.

14 Q. Let me ask you about the vertical interval
15 that you're dealing with, Mr. Smith. The pooling case
16 asked to pool all 320 gas spacing from the top of the
17 Wolfcamp on down.

18 A. That's correct.

19 Q. What formations were you dealing with Mr.
20 Murphy on?

21 A. All depths, all depths.

22 Q. The Exhibit 12 --

23 A. Yes.

24 Q. What is that, sir?

25 A. That is a letter dated December 30, 1992.

1 That was received by Mitchell two ways, once via fax,
2 and once via certified mail.

3 I believe in a later letter that's marked
4 -- it's a later exhibit, where we attempted to
5 sumimize [sic] the correspondence and the
6 conversations, I failed to mention that we received a
7 faxed copy of this on January 4. That was the first
8 time we saw this letter.

9 In my summation, I said we received it on
10 December 30. We did not. We got it on January 4.
11 And it was sent to me after Mr. Murphy had called me
12 to tell me basically what the contents of it would be.

13 Q. Without giving me all the details, tell me
14 how to summarize the agreement as Mr. Murphy presents
15 it to you.

16 A. Well, basically, it correctly described the
17 acreage to be conveyed, the lease to be conveyed, the
18 dollar per acre consideration, and the override and
19 sum to be -- well, it didn't correctly describe the
20 override. It went on beyond what was discussed when
21 Mr. Murphy and I -- when I made the dollar offer to
22 Mr. Murphy to buy Strata's interest.

23 It included terms such as a requirement for
24 us to pool Strata's retained override underneath the
25 entire section of 28. And, in turn, they would reduce

1 proportionately the override retained on their lease.

2 The effect was, they were seeking to have
3 an override under the entire section as opposed to
4 retaining an override underneath the lease which they
5 owned.

6 Q. Give me an idea how the mechanics worked.

7 A. Mechanically, again, in return for reducing
8 the override retained on their lease, we would have to
9 turn around and assign to them overriding royalty
10 interest against our leasehold, which they previously
11 had no interest in.

12 Q. Did you have authority to accept that
13 provision?

14 A. No, I did not.

15 Q. Did you discuss it with your management?

16 A. Not until receipt of this letter, which we
17 received on January 4.

18 Q. Did you review then this proposal with your
19 management, and what action, if any, did they take?

20 A. We were told -- I was told that it was
21 unacceptable; that was not something we would
22 consider, and that I was to write a letter back to Mr.
23 Murphy, stating the terms that we believed were agreed
24 to in our telephone conversation.

25 Q. As of the December 20, '92, letter from Mr.

1 Murphy to you, did you understand that you were
2 dealing with Mr. Murphy for the total interest on
3 behalf of this company, or were you dealing with
4 others?

5 A. Well, up until this point, again, he had
6 informed me that there were partners, and he clearly
7 stated it would require partner approval for the
8 farmout, but I would point out, in the December 30
9 letter, again, this is Exhibit 12, that an exhibit to
10 this letter agreement that purported to control the
11 terms of the sale in Strata's lease to Mitchell,
12 there's an Exhibit A attached wherein Strata
13 represented itself as being capable of assigned
14 Mitchell Energy Corporation 100 percent record title
15 to this lease.

16 Q. How do you reach that conclusion by looking
17 at this proposed assignment form?

18 A. It's a standard form, federal form
19 assignment of record title, and if you look down about
20 the middle of the page where it describes the acreage
21 to be conveyed, there's a column labeled Percentage of
22 Interest, and there are three subcolumns labeled
23 Owned, Conveyed, and Retained.

24 In the Owned column, it clearly shows that
25 Strata claims to own 100 percent record title. Under

1 the Conveyed column, it clearly shows that Strata
2 purports to be able to convey 100 percent record title
3 to this lease, and that they intend to retain no
4 record title interest.

5 Q. Having come to the decision that that
6 provision is not acceptable to Mitchell, what then did
7 you do?

8 A. After -- of course, I took this letter,
9 once we got it, as I told Mr. Murphy I would -- like I
10 said, he called me that day and faxed it to me to tell
11 me the contents of it. In that phone conversation, I
12 told him that that's not the trade; that was not what
13 was presented to Mitchell management, but go ahead and
14 send it on. I had no authority to pass on whether or
15 not it was acceptable to Mitchell.

16 I did send it in to Mitchell, our
17 management in Houston. It was turned down flat. I
18 was told to write a letter back, stating what our
19 understanding, the terms were, and I did that.

20 Q. And how did you do that?

21 A. By letter dated January 5, 1993.

22 Q. That's Exhibit 13?

23 A. That's correct.

24 Q. What then happened?

25 A. I, as it clearly shows, I sent it to Strata

1 via fax and by certified return receipt mail. I faxed
2 it early in the morning. Mr. Murphy got it, called me
3 up, and asked me what -- you know, what do you mean;
4 this is not what we agreed to.

5 And I reminded him or advised him that, you
6 know, this is what we agreed to on the phone. These
7 were the terms that were discussed, and this letter is
8 intended to represent the terms agreed to and
9 discussed in our telephone conversation.

10 Q. At this point, then, there is a difference
11 of opinion as to what the agreement was, and the end
12 result is you can't get it reduced to a written
13 agreement?

14 A. That's the bottom line.

15 Q. Identify for us Exhibit 14. What is this?

16 A. This is a letter again sent to us by Strata
17 dated January 6. It was sent via fax and by hard copy
18 by return receipt mail. It was a letter basically
19 where Mr. Murphy advised that he had talked to his
20 partners and advised them that we had refused to
21 execute their letter agreement.

22 He states that "it appears we are unable to
23 resolve the sale, farmout or participate by Strata"
24 prior to the January 7 original hearing date. And it
25 states, as I told him, that we, Mitchell, would

1 request, in an effort to accommodate them and to
2 continue to work this deal out, we would request to
3 extend or seek a continuance to the next docket date.
4 We did that.

5 It also states that they now thought they
6 perhaps -- well, they might now consider wish to join
7 the well. To be honest with you, this is the first
8 time -- it purports to say that we had discussed
9 Strata's participation. I would go on record saying
10 that this is the first point in time where Strata ever
11 indicated any interest in participating in our well,
12 and asked that we send them an AFE or send them a
13 joint --

14 Q. A JOA?

15 A. JOA, and asked to be put on notice of any
16 people that were opposing our unorthodox location.

17 Q. At any point during the negotiations with
18 Strata, did you provide them or cause to be provided
19 any geologic data?

20 A. I did not.

21 Q. Do you know whether or not your company
22 provided geologic data to them?

23 A. It's my understanding that we have, that
24 Mitchell Energy Corporation has provided Strata with
25 geological data to show them our picture of why we're

1 doing what we're doing.

2 Q. After the January 6 letter, Exhibit 14,
3 what then happened, Mr. Smith?

4 A. Well, I wrote a letter back. Again, Mr.
5 Murphy in his previous letter acted as if we were --
6 had moved the location unbeknownst to him, and I
7 reminded him in our January 6 letter -- this is
8 Exhibit 15, Mr. Examiner -- that the location remained
9 as originally proposed. And I reminded him that the
10 location, while it was unorthodox, was unorthodox only
11 because of archeological and topographical reasons.
12 And that we were unaware of any opposition from the
13 parties who were notified of our unorthodox location,
14 and expected none.

15 Q. Did you respond to his request for a
16 proposed Joint Operating Agreement?

17 A. I did include -- again, I prepared for
18 Strata an operating agreement which was virtually
19 identical to the operating agreement that would have
20 governed the operations between the agreeing parties
21 to drill this well.

22 Q. You tailored your proposed operating
23 agreement with Mr. Murphy and Strata Production based
24 upon what document?

25 A. Again, it's the operating agreement that is

1 in place between Mitchell partners that would have
2 governed or will govern their participation in this
3 well.

4 Q. Did you have any discussions with Strata
5 Production Company with regards to what formations or
6 vertical intervals were being asked to finally be
7 committed to this well?

8 A. Well, we proposed all depths in all
9 formations. That was our intent.

10 Q. Exhibit 15, you've summarized various
11 activities. At the end of there anywhere, did you
12 leave open the opportunity for the exercise of any
13 other solutions?

14 A. Well, basically, yes. I basically offered
15 to Strata the three options that Mitchell was willing
16 to consider to resolve the problem, and I listed them
17 in our order of prevention: one, they participate in
18 the well as we proposed; two, that they agree to farm
19 out to Mitchell under the terms they proposed to us.
20 We were more than happy to accept those terms; or,
21 three -- or, excuse me, two, that they sell certain
22 terms that we believed to be agreed to; or, three,
23 farm out as agreed in their letter to us.

24 Q. Identify for us what is Exhibit No. 16.

25 A. Exhibit 16 is a letter from Strata

1 Production Company to Mitchell Energy Corporation
2 dated January 12.

3 Q. I'm not going to ask you to go through the
4 letter, Mr. Smith. Am I correct in concluding that
5 you and Mr. Murphy disagree with some of the specific
6 items with regards to this letter?

7 A. I would say that there is minor agreement
8 as to minor details, and I would say that there are
9 colorizations of conversations that are perhaps
10 inaccurate in both but --

11 Q. I don't want to get into that, Mr. Smith.

12 A. The gist of the deal is that it both
13 clearly summized [sic] the meat of the terms or the
14 efforts to reach agreement. And there's not really
15 any substantial difference in either summation of the
16 facts.

17 Q. Let me ask you to turn to the last page of
18 that letter, Exhibit 16, and the last paragraph,
19 second to the last sentence says, "Since you have had
20 notice that these undisclosed owners exist, we would
21 ask that you grant another two weeks' continuance and
22 notify these parties of your application."

23 Did you do that?

24 A. No, we didn't.

25 Q. At what point did you receive, if at all,

1 from Strata Production Company, a list of the names
2 and addresses of these undisclosed interest owners?

3 A. The first actual notice of the entities
4 that had been heretofore characterized as partners
5 with Strata was received via fax on January 13, 1993,
6 and we received a certified copy on January 14.

7 Q. And that is Exhibit No. 17?

8 A. That's correct.

9 Q. Let me ask you to help me deal with another
10 item. If you'll look at Exhibit 19, which is my
11 certificate of notice for hearing --

12 A. That's correct.

13 Q. -- and go back, sir, to the plat which is
14 Exhibit 6, the unorthodox location is 1,650 from the
15 north line of the spacing unit?

16 A. That's correct.

17 Q. And so it is moving in a northerly
18 direction as it becomes unorthodox?

19 A. That's correct.

20 Q. Did you determine the offsetting operators
21 for whom notice of that location was to be provided?

22 A. Yes, we did.

23 Q. Can you identify for me, using Exhibit 19
24 and Exhibit 6, and confirm whether or not the parties
25 that were entitled to notice of the location have in

1 fact received notification?

2 A. Yes, I would. Again, the movement or the
3 direction in which we encroached went northward, and
4 therefore we were required to notify the parties in
5 Section 21 and I believe the southwest quarter of 20
6 of that encroachment. And those parties were
7 Southwest Royalties, who had a 50 percent interest in
8 the southeast quarter of Section 20; Enerlock
9 Resources, who had the other 50 percent interest in
10 the southeast quarter of Section 20.

11 We notified Santa Fe Energy Operating
12 Partners and Maralo because we knew that at the time,
13 they were in negotiations to purchase Southwest
14 Royalties and Enerlock's interests; so we included
15 them.

16 As to the -- we also notified Phillips
17 Petroleum Company, who has a partial interest in the
18 west half southwest quarter and the northeast quarter
19 of Section 21.

20 We also notified Oryx, who also has a
21 partial interest in that same lease, and we notified
22 Grace Petroleum Corporation, who owns the leasehold
23 covering the southeast quarter and the northeast
24 southwest quarter of Section 28.

25 Q. And then the first notification was to

1 Strata Production Company because they were the party
2 to be pooled in the spacing unit?

3 A. That's correct.

4 MR. KELLAHIN: That concludes my
5 examination of Mr. Smith. We move the introduction of
6 Exhibits 6 through 17 and Exhibit 19.

7 EXAMINER STOGNER: Any objections?

8 MR. CAVIN: No, sir.

9 EXAMINER STOGNER: Exhibits 6 through 17
10 and Exhibit No. 19 will be admitted into evidence at
11 this time.

12 Mr. Cavin, your witness.

13 MR. CAVIN: Thank you.

14 MR. STOVALL: Let me do one thing first to
15 make sure we clear the record. I notice that on the
16 list of interest owners is an S.H. Cavin. Any
17 relation?

18 MR. CAVIN: Yes. That's my father.

19 MR. STOVALL: And you are not representing
20 your father here today?

21 MR. CAVIN: No. He's smarter than that.

22 MR. STOVALL: I won't go any further with
23 that one.

24 EXAMINATION

25 BY MR. CAVIN:

1 Q. Mr. Smith, I'd like to ask you a few
2 questions on what I think -- you may be able to help
3 me. I can't see the exhibit number on this?

4 A. Six.

5 MR. KELLAHIN: Six. It's on the back.

6 Q. (BY MR. CAVIN) Exhibit No. 6. Can you
7 tell me what the status of ownership is on the
8 southwest of the northwest quarter?

9 A. That is an unleased federal tract.

10 MR. KELLAHIN: I'm sorry. I think you
11 misspoke. Say it again.

12 Q. (BY MR. CAVIN) I'm sorry, the southwest of
13 the northeast quarter of Section 28?

14 A. That's correct. That is an unleased
15 federal tract.

16 Q. Has there been any attempt to lease this
17 tract and put it up for nomination?

18 A. We wrote a letter to Miss Martha Rivera in
19 September of 1992 in an effort to nominate it, and we
20 had every belief that it would be as appeared in this
21 most recent federal sale; however, by letter from Miss
22 Rivera, it did not reach the sale because they failed
23 to verify that the lease had actually terminated.
24 They felt that they would probably have it up on the
25 next sale.

1 Q. Okay. When would the next sale be?

2 A. I believe it will be April 21.

3 Q. Okay. Can you tell me what the status --
4 and if you've already testified to this, I apologize
5 -- the status of the ownership or status of the lease
6 in the northwest quarter of the southwest quarter of
7 Section 28?

8 A. It is a federal lease that, again, as I
9 stated, is owned by Mitchell Energy Corporation and
10 its partners, and it will be scheduled to expire on
11 10-1-93.

12 Q. Have there been any comments throughout
13 your negotiations with Mr. Murphy that would indicate
14 that he had the unfettered authority to act for his
15 partners in this matter?

16 A. I would say there were no comments made by
17 him that said he didn't have. And I would point again
18 to that letter agreement that he sent for our
19 execution where it was obvious that he had attached an
20 exhibit that had a federal assignment that Strata
21 purported to have authority to act on all parts.

22 Q. That's consistent with your understanding
23 thought that he had the unfettered authority to deal
24 for these parties?

25 A. He had the authority to sign an agreement

1 binding all parties to whatever agreement we reached.

2 Q. So in his earlier correspondence where he
3 said it would be subject to partner approval, you felt
4 like that was just a misstatement?

5 A. No. That to me, it's a standard -- I put
6 it in my letters. That's an industry standard thing.

7 Q. Would it be typical for you to require any
8 documentation where someone says they have the
9 authority to deal for other parties?

10 A. I -- as part of the title examination, it's
11 generally required that we determine the status of
12 whoever it is and from the search of the county
13 records determine whether they have record title to
14 the property, and we did that.

15 Q. As part of your due diligence you would
16 normally do, if a party told you they have undisclosed
17 partners, would it be typical to ascertain the
18 authority of those parties?

19 A. As long as I'm under the -- it's not
20 uncommon out here for companies like Strata to have
21 lots of silent partners. I mean, Mitchell Energy
22 Corporation is made up by lots of silent shareholders,
23 and we do not have to seek their joinder to enter into
24 any agreements.

25 Q. Would it be unusual for Mitchell to have

1 unfettered authority to deal for these partners?

2 A. We never seek the shareholders' authority
3 to enter into operating agreements or sell or farm
4 out.

5 Q. I guess I mean partners, not shareholders.
6 I'm not speaking of shareholders of Mitchell. I'm
7 saying your partners. You say you have partners quite
8 --

9 A. Well, when we have entered into an
10 operating agreement and we have obtained agreement
11 from our partners to drill a well, and that operating
12 agreement would govern what would happen if we
13 acquired an interest within the contract area, we can
14 act on our own behalf. And if the partners didn't
15 like what we did, we have to suffer the consequences
16 with those interactions.

17 Q. As far as the disposition of an interest or
18 the farming out of an interest, is it unusual for
19 Mitchell to have the unfettered authority to deal for
20 its partners?

21 A. I wouldn't ever purport to farm out --
22 let's just, as an example, turn this around. If I
23 were attempting or had entered into negotiations with
24 Strata to farm out Mitchell's leasehold for a well
25 proposed by Strata in the west half, no, I would not

1 purport to be able to bind either Maralo's or Santa Fe
2 Energy's interest.

3 Q. You mentioned the overhead rate. How does
4 that -- are you familiar with the Ernst and Whinney's
5 --

6 A. Absolutely.

7 Q. -- proposed overhead rate?

8 A. Sure.

9 Q. Does your overhead rate -- how does that
10 compare to the proposed overhead rates there?

11 A. The average in Ernst & Whinney I believe
12 right now is around -- it's lower than what we
13 proposed. I don't know exactly what it is. But the
14 schedule that we put forth, again, is what's currently
15 being charged in the area.

16 We operate two Morrow wells in this
17 township, and if you expand out into surrounding
18 townships, we have seven or eight or nine. And we
19 simply were asking Strata to pay the same overhead
20 rate everyone else is in the area.

21 Q. Would you have any problem using the Ernst
22 & Whinney overhead rate for the Strata and its
23 partners?

24 A. I would believe that the rates proposed by
25 Mitchell are reasonable, and that's what we would want

1 to stay with.

2 Q. So you wouldn't be agreeable to the Ernst &
3 Whinney's overhead rates?

4 A. I don't believe I, as a senior landman,
5 have the authority to make that decision on Mitchell
6 Energy Corporation's behalf. I would have to seek
7 management approval to make that statement.

8 Q. Would it surprise you that just
9 catty-corner to that Section 28 lease in Section 32
10 Meridian recently acquired interest at a price of
11 \$1,000 an acre?

12 A. Would it surprise me? I'm not aware of it.

13 Q. Based on the price that Mitchell's been
14 paying in this area that are much lower than \$150?

15 A. Well, I will say that I'm a landman, and
16 terms of a trade are always governed by what two
17 people think things are worth. And if for whatever
18 reason Meridian thought something was worth \$1,000,
19 that's between them and whoever they struck their
20 trade with.

21 Q. It might be possible that \$150 isn't an
22 inflated price, though?

23 A. We have no qualms about paying \$150 an
24 acre. We, in writing, offered to pay that and would
25 gladly accept that today.

1 Q. Okay. Based on the correspondence and
2 communications with Mr. Murphy, did you ever believe
3 if you weren't able to strike agreement that you might
4 have to deal with these partners directly?

5 A. Not until receipt of the January 14 or 13
6 letter.

7 Q. Did you ever ask Mr. Murphy for information
8 on the partners?

9 A. He always described them as silent
10 partners, and I've dealt with any number of companies
11 in the past who had silent partners. And when I'm led
12 to believe that the individual with whom I am dealing
13 has the capacity to bind those silent partners, I
14 don't need to know who they are.

15 Q. Okay. So you didn't ask for that
16 information?

17 A. Based upon the representations by Mr.
18 Murphy that he had the capacity to bind those
19 interests, no, I didn't.

20 Q. Did you ever consider getting something in
21 writing from Mr. Murphy that he had the authority to
22 represent these parties?

23 MR. STOVALL: Let me interrupt this at this
24 point and say, let's go back to Exhibit 12. I'd like
25 to -- you referred to the attachment to Exhibit 12,

1 and pardon me for doing this. I think we can
2 short-circuit this line of questioning.

3 THE WITNESS: The attachment to Exhibit
4 12?

5 MR. STOVALL: Did you read this letter, Mr.
6 Smith, at the time?

7 THE WITNESS: You're talking Exhibit 12?

8 MR. STOVALL: I'm talking Exhibit 12, the
9 December 30th letter.

10 THE WITNESS: Yes, I did.

11 EXAMINER STOGNER: Third page.

12 MR. STOVALL: Let's dispose of it by just
13 going to paragraphs No. 5, No. 7, and No. 8.

14 MR. KELLAHIN: I'm sorry, I'm not with
15 you. Which exhibit?

16 THE WITNESS: Twelve.

17 MR. KELLAHIN: And which paragraphs?

18 MR. STOVALL: Paragraphs 5, 7, and 8.

19 MR. KELLAHIN: Of the body of the --

20 MR. STOVALL: Of the body of the letter
21 itself.

22 THE WITNESS: I did read it.

23 MR. STOVALL: With that information in the
24 record, Mr. Cavin, do you wish to pursue this line of
25 questioning?

1 MR. CAVIN: Absolutely, and I'd be happy to
2 explain, too, because I was responsible for drafting
3 this. This was sent to Mitchell --

4 MR. STOVALL: Mr. Cavin, please don't
5 testify. Use a witness.

6 MR. CAVIN: All right.

7 Q. At any time prior to December 30th, did you
8 request anything in writing from Mr. Murphy regarding
9 his authority to act for the partners?

10 A. No, I didn't.

11 Q. Was it your understanding Mr. Murphy could
12 cut just any deal, or were there just certain deals?

13 A. No. He told me that it would take his
14 partners' approval. As I stated in my letters, it
15 takes management approval. I understood that he was
16 acting as a go-between, as I was.

17 Q. Referencing your Exhibit 12, did you
18 interpret that paragraph 7 to be unlimited or tied to
19 this agreement?

20 A. Direct me again.

21 Q. I'm sorry, your Exhibit 12, it's on page 3,
22 it's paragraph 7.

23 A. Undisclosed Owners. Restate your question,
24 please.

25 Q. Did you interpret this to be applicable to

1 just any agreement or specific to this agreement?

2 A. Well, I would state that if it's possible
3 for Strata to make this statement in this agreement,
4 then it would imply that Strata has the capacity to
5 bind those partners in any agreement should the
6 partners have agreed to it.

7 Q. Do you see any difference between a sale
8 and a joint operating venture as far as the partners
9 would be concerned and Strata binding them to those?

10 A. Well, as long as Strata retained 100
11 percent record title interest, no.

12 Q. Did you ever -- in your conversations with
13 Mr. Murphy, did you ever allude to reasons for a west
14 half proration unit?

15 A. I alluded to one of.

16 Q. What would that reason be?

17 A. One of the reasons is that I did state to
18 him was that we have an expiring lease, and we would
19 certainly like to save it, but I did clearly state to
20 him that it was one of many reasons.

21 And I would clarify by stating that that
22 was a landman to landman kind of reasoning. I won't
23 purport to be a geologist; that that's just one of
24 many reasons. There were other reasons; i.e., an
25 unleased federal tract in the southwest northeast that

1 any reasonable and prudent operator would not include
2 within a proration unit.

3 Q. Was there any discussion if you set up a
4 west half proration unit that, in that fashion, you
5 could drill two wells in the north half? Was that
6 ever discussed with Mr. Murphy?

7 A. That was the main geologic reasoning and
8 really the main reasoning to do it the way we're doing
9 it is that we believe -- and I don't want to get into
10 geology because I'm not a geologist -- but that is the
11 main reason for doing what we're doing.

12 Q. Do you keep a phone log, Mr. Smith?

13 A. Not in detail.

14 MR. CAVIN: I have no further questions,
15 Mr. Examiner.

16 EXAMINER STOGNER: Mr. Stovall?

17 MR. STOVALL: I don't think I have any.
18 Well, let me --

19 EXAMINATION

20 BY MR. STOVALL:

21 Q. Is there any indication that you have, Mr.
22 Smith, do you know the nature of the interest or the
23 interest of the partnership as its referred to?

24 A. No. We were relying on the fact that
25 Strata is of record, the record title owner to 100

1 percent interest, and they are a New Mexico
2 corporation capable of conducting business in New
3 Mexico, and his representation to us that he spoke for
4 these silent partners and was capable of binding them
5 in an agreement.

6 Q. Based upon your experience as a
7 professional landman, you've been involved in
8 situations before where there are -- I think you've
9 stated that --

10 A. Investors?

11 Q. Investors in the well?

12 A. Sure.

13 Q. Is it necessarily the case that they always
14 own a working interest in leases, that those investors
15 own working interest in leases?

16 A. When you say -- I'm not sure I understand
17 your direction.

18 Q. As an operator and the owner of oil and gas
19 leases, and you invested and put up money to
20 participate in your operations, do those investors
21 always, unequivocally have an interest in the real
22 property, or do they have an interest in the
23 production or --

24 A. Mr. Examiner, I would say that I've never
25 worked for a company that operated that way and would

1 not be able to comment. I've only worked for a major
2 corporation in my capacity as a senior landman, and we
3 don't have investors. We have shareholders.

4 MR. STOVALL: Okay. I don't think I have
5 anything further.

6 MR. KELLAHIN: I have one follow-up
7 question, Mr. Examiner.

8 EXAMINER STOGNER: Mr. Kellahin.

9 FURTHER EXAMINATION

10 BY MR. KELLAHIN:

11 Q. From a landman's perspective, Mr. Smith,
12 tell me, what, if any, difficulties are created with
13 regards to the unleased federal tract in the southeast
14 of the northeast, if, for example, the spacing unit is
15 the east half or the north half, and you have to now
16 include that tract as an unleased tract in the spacing
17 unit. What are your reservations, concerns, or
18 observations?

19 A. Well, the federal government or the BLM
20 would allow you to drill a well and approve a
21 communitization agreement covering the proration unit
22 containing an unleased federal tract as long as it
23 wasn't the drill site lease and as long as it did not
24 constitute a majority of the proration unit.

25 In doing that, they would allow you to

1 drill your well, and at such times as that lease then
2 came up for sale, on the next sale that it did come up
3 on, a condition would be placed upon the issuance of
4 that lease to the winner that the winner would be
5 required to sign a communitization agreement covering
6 the well in that -- or covering that tract as it
7 applied to that well.

8 Q. Is that a viable option for Mitchell to
9 exercise in order to form a spacing unit?

10 A. It's not what would be considered
11 reasonable and prudent because you would then be
12 putting for sale an interest in a known quantity up
13 for auction. You would be leaving a hole in your
14 proration unit for anyone to step in and buy it and
15 bid the price up to whatever it might go to. It's
16 just not something a reasonable and prudent operator
17 would do.

18 MR. KELLAHIN: That's all the questions I
19 have.

20 MR. CAVIN: I have a follow-up, Mr.
21 Examiner.

22 EXAMINER STOGNER: Mr. Cavin.

23 FURTHER EXAMINATION

24 BY MR. CAVIN:

25 Q. Mr. Smith, you have experience with federal

1 leases, I believe you stated?

2 A. Yes.

3 Q. Do you have any reason to doubt, based on
4 your conversations with the BLM, that this lease will
5 be put up at the next sale?

6 A. We have a letter in our files from Martha
7 that it did not make -- we inquired as to why it did
8 not make this most recent sale, and the reason was
9 that they had failed to verify, through whatever
10 procedure they do so, that the lease had actually
11 expired; that they felt and assured us that, as long
12 as the lease has expired, it should make the next
13 federal sale.

14 Q. Which again you say that was --

15 A. I believe it's April 21st of this year.

16 Q. Are there any considerations that would
17 require you to drill this well before that date?

18 A. We have signed AFE's with our partners
19 covering the proposed well that under the operating
20 agreement will expire after a certain period of time.

21 Q. Your partners being --

22 A. Santa Fe Energy and Maralo. And we would
23 proceed -- prefer to get on with our business.

24 MR. CAVIN: Oh, sure. I have no further
25 questions.

1 EXAMINER STOGNER: Any other questions of
2 Mr. Smith?

3 MR. KELLAHIN: No, sir.

4 EXAMINER STOGNER: He may be excused.

5 Mr. Kellahin.

6 MR. KELLAHIN: I'm prepared to continue
7 with my witnesses, if you desire. If you want to deal
8 with the notice issue, I guess we can do that, too.
9 However you would like to proceed.

10 EXAMINER STOGNER: You may continue, Mr.
11 Kellahin.

12 MR. CAVIN: Could I take a 60-second break?

13 EXAMINER STOGNER: We'll take five minutes.

14 (Thereupon, a recess was taken.)

15 EXAMINER STOGNER: Mr. Kellahin?

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

17 We'd call at this time Mr. Ted Galowski.

18 TED GAWLOSKI

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

21 EXAMINATION

22 BY MR. KELLAHIN:

23 Q. Mr. Gawloski, would you please state your
24 name and occupation.

25 A. I'm Ted Gawloski. I'm a staff geologist

1 for Mitchell Energy Corporation in Midland, Texas.

2 Q. Mr. Gawloski, on prior occasions, have you
3 testified as an expert petroleum geologist before the
4 Oil Conservation Division?

5 A. Yes, I have.

6 Q. Describe for us what it is that you have
7 done for your company with regards to the area in Lea
8 County, New Mexico, that your company is exploring for
9 Morrow gas production. What is it that you do in that
10 process?

11 A. I'm essentially the geologist who works the
12 exploration end of defining the first location in an
13 area for the Morrow, using all available geologic data
14 that we have to determine the best possible locations
15 to develop Morrow gas in the area.

16 Q. Section 28 that's the subject of this case
17 is your own personal project?

18 A. Yes, it is.

19 Q. And you are the exploration geologist that
20 is attempting to find Morrow production in this
21 section and other areas in the township?

22 A. That's correct.

23 Q. Based upon that study, have you done
24 certain mapping and reached certain conclusions with
25 regards to issues that are relevant to this hearing?

1 A. Yes, I have.

2 MR. KELLAHIN: We tender Mr. Gawloski as an
3 expert petroleum geologist.

4 EXAMINER STOGNER: Any objections?

5 MR. CAVIN: No, Mr. Examiner.

6 EXAMINER STOGNER: Mr. Gawloski is so
7 qualified.

8 Q. (BY MR. KELLAHIN) Mr. Gawloski, let me ask
9 you to take Mitchell Exhibit No. 1. Is this an
10 exhibit that you prepared?

11 A. Yes, it is.

12 Q. Identify for us the Section 28 that's the
13 subject or the topic of this hearing. Where is it?

14 A. Section 28 is in the lower portion of this
15 map. It is in Township 20 South, Range 33 East -- I
16 mean, there's a green dot showing the approximate
17 location of the well, the Tomahawk 28 Federal Com or
18 Federal #1.

19 Q. Give us a general overview of the
20 development and exploration that is occurring in this
21 area with regards to those gas formations below the
22 top of the Wolfcamp. What is happening to develop
23 those potential gas reserves?

24 A. From a Mitchell point of view or from
25 just --

1 Q. From anybody's point of view.

2 A. There is some Morrow activity ongoing in
3 the area, a lot of it by Mitchell Energy; some of it
4 by other operators. There's wells being drilled to
5 the north and some to the south and east, as well, for
6 the Morrow horizon in here.

7 Q. Using the legend, Mr. Gawloski, how have
8 you identified Morrow wells?

9 A. Currently active Morrow wells?

10 Q. Yes, sir.

11 A. Using the arrow. However, that's also for
12 other wells. It's not just for Morrow activity in
13 here.

14 Q. If I find a light blue dot, the legend says
15 that's a Morrow. A Morrow what?

16 A. A Morrow producer. It's produced gas out
17 of the Morrow formation.

18 Q. What is the nearest Morrow producer in this
19 area in relationship to Section 28?

20 A. There are two approximately the same
21 distance away, a well in Section 33, just to the
22 south. However, that well did not make any commercial
23 quantities of gas, just essentially a show. The other
24 well closest to it is our Mitchell Energy well, Top
25 Hat Federal Well, which has just been on line for

1 approximately a year right now.

2 So there's really not a whole lot of Morrow
3 wells within that general vicinity, producers.

4 Q. When I move north of 28 about three
5 sections and get up into Section 9, there's a blue dot
6 and then a red arrow?

7 A. That's correct.

8 Q. What is represented in that section?

9 A. The blue dot was a Mitchell Morrow
10 discovery. That was just completed, oh, approximately
11 three or four months ago, the Anasazi Federal Mine #1,
12 and we are currently in the process of developing
13 plans to drill an offset to this well.

14 Q. Let me talk to you for a moment about your
15 personal experience as an exploration geologist
16 looking for Morrow production in this area. How long
17 have you been engaged in that activity for your
18 company?

19 A. Ever since I started at Mitchell in 1984, I
20 have been engaged in Morrow exploration activity and
21 in years before that when I was working for Amoco
22 Production Company in the same area.

23 Q. Can you give us any of your personal
24 experience in how successful you are in applying your
25 geologic interpretations and geologic methodology to

1 successfully finding, locating, and ultimately
2 producing Morrow gas?

3 A. We have been successful in numerous Morrow
4 wells in this area and are currently ongoing drilling
5 wells in here right now at present. And the success
6 rate we've had in this area has been excellent.

7 Q. Give us a sense of the range of your
8 successes in the recent period. How many wells have
9 you personally been involved in picking locations for,
10 and what has been the success of those attempts?

11 A. We've had -- within the area, approximately
12 seven to eight Morrow wells that I've been responsible
13 for. And each one we have, are producing gas out of,
14 run pipe and produce gas out of it. Most of the wells
15 are new and the cum's of them are yet to be
16 determined.

17 Q. When you target Morrow production, is there
18 any particular portion of the Morrow that you're
19 looking at as a way to then determine where to locate
20 a well?

21 A. Yes. Our primary target in this area is
22 our package of Morrow sands, we call the Morrow B
23 interval, which most of the production in this area
24 does come out of.

25 Q. For you as an exploration geologist looking

1 for Morrow B, what geologic tools are you using by
2 which then to develop a strategy for exploration of
3 the Morrow?

4 A. We use -- primarily, we'll go in there and
5 isopach the Morrow B Section, and then we would
6 construct a structure map, using all available well
7 data. In our structure map, we use all available
8 seismic data that we have in the area, and it's quite
9 extensive in this particular area. We use that in
10 conjunction with the well data to make our structure
11 map.

12 And we also use cross-sections to show the
13 lateral continuity or discontinuity of the Morrow
14 sands.

15 Q. What is your exploration strategy or method
16 by which, having found an area that you want to
17 develop within a section, what decisions do you make
18 about how to drill for Morrow production?

19 A. When we go into an area like this, and this
20 is what we've done numerous occasions in here prior to
21 this well, we determine what our primary target
22 formation is in here. And, in this case, it's the
23 Morrow formation, and primarily the Morrow B sands
24 section.

25 We then determine the proration units,

1 establish for that, in this case, the Morrow being 320
2 acres. We then use an approach in here how to best
3 develop that section for the Morrow, using both our
4 tools that we have, using the isopach and the
5 structure maps.

6 Q. What is the objective that you're trying to
7 achieve with your selection of a spacing unit and the
8 orientation of that unit within a single section?

9 A. We're trying to achieve how best to develop
10 our primary target formation within that section.

11 Q. Is this a single well per section concept,
12 or is it a two well, 320-acre development concept or
13 exploration concept?

14 A. It's a two-well concept that we've used in
15 this area. It's something that we've done in the
16 past, and we would do in the future.

17 Q. What do you achieve by looking at the
18 orientation of spacing units whereby within a section
19 then you give yourself two spacing units and two
20 potential locations, one for each of those spacing
21 units?

22 A. Can you --

23 Q. Yes, sir. What's the objective, what is
24 the goal that you're trying to achieve within a
25 section by looking at the whole section as opposed to

1 a single 320 spacing unit?

2 A. We're trying to maximize our potential for
3 that target formation within a section.

4 Q. How do you do that?

5 A. We do that using our geological maps that
6 we have constructed for that area.

7 Q. Let me ask you now to turn to the structure
8 map. Again, is this a display that has been prepared
9 by you?

10 A. Yes, it has.

11 Q. Before we look at the specific conclusions
12 that you reach about 28, tell us how to read and
13 understand the information.

14 A. This is a structure map, again, using all
15 available well data, as well as the seismic data, and
16 you can see them mainly on the section lines, all the
17 seismic data that Mitchell has in this area. It's an
18 extensive database that we use in here to develop
19 regional trends for the Morrow. We use these maps in
20 a regional sense and then hone in on the area that
21 we're working on.

22 You can see that there's extensive
23 structural component structure in the area, numerous
24 faults and structures and things that show in this
25 area here.

1 Q. Analyze the structure map for us as it
2 applies to Section 28 and tell us how, if at all, that
3 information affected how you proposed to orient the
4 spacing unit in 28.

5 A. You can see in Section 28 -- it's the
6 section that has the green outline on it? As you move
7 into the northern half of Section 28, there's actually
8 a structural closure that is developed in Section 28.
9 And the northern part of that section is the best
10 developed structure.

11 As you move south in that section, you lose
12 a considerable amount of structure, which greatly
13 increases your risk in this area for finding Morrow
14 production.

15 Q. The arrow, the point of the arrow, is that
16 attempting to locate the standard location, or is this
17 locating the proposed unorthodox location?

18 A. That approximates the unorthodox location.

19 Q. The scale is so small, I guess it's hard to
20 see, but that is intended to represent the 1,650 from
21 the north line?

22 A. That's correct.

23 Q. As opposed to 1,980 from the north line?

24 Give us an understanding of the well
25 control information that you have to help you infer

1 the structure and the closure of the minus 9400 line
2 within Section 28. What's your control?

3 A. Well, there's a well in Section 27, a well
4 in Section 26, a well to the south in 33, and farther
5 to the north, our well in Section 9.

6 Q. Let's talk about the seismic control.
7 Where is that?

8 A. There's extensive seismic control east-west
9 along the southern part of Section 28, north-south
10 across the western portion of Section 28, another
11 east-west line running across Section 21, and in the
12 middle portion of Section 21, and another line,
13 east-west line along the northern portion of Section
14 21 and several other lines north-south through the
15 area. Very extensive seismic base we have here.

16 Q. Based upon the structure map, do you have
17 an opinion as to the level of risk factor the
18 examiner, in your recommendation, should assess
19 against any nonconsenting interest owner regardless of
20 where the well is located in Section 28?

21 A. The risk for drilling a well in this area
22 is that we are on, essentially on a structure that has
23 been untested. That would be the primary risk. The
24 closest well to us has tested the Morrow in Section 27
25 and did not produce out of the Morrow section. It did

1 produce out of the Atoka section.

2 Q. When you consider all those factors that
3 you as a geologist rely upon, what is the risk factor
4 in terms of a percentage as assessed by the Division
5 that you would recommend that be applied in this case?

6 A. I believe the maximum penalty should be
7 applied in this case, that being 200 percent plus
8 costs.

9 Q. Does the risk diminish so that the penalty
10 factor ought to be less than 200 percent, if you move
11 the location from the closest standard location to the
12 proposed unorthodox location?

13 A. No, I don't believe that should change at
14 all.

15 Q. Why not?

16 A. It's a minimal distance that you're moving
17 structurally, and the risk is still going to be there
18 because the structure is untested.

19 Q. Can you reach that same conclusion then
20 with regards to wherever the well is located within
21 the spacing unit, it's not going to have a material
22 effect so that the maximum penalty should be less than
23 200 percent?

24 A. That's correct.

25 Q. Let's turn now to the isopach information.

1 In addition to making a structural interpretation,
2 what else do you do?

3 A. I go into the Morrow section, and I isopach
4 what we call the Morrow B section. I take the
5 porosity cutoff of a density porosity of 7 percent,
6 which we used as a limitation for production, and we
7 isopach those values using all the available well
8 control that we have.

9 Q. And you have done that with this isopach
10 that's identified as Exhibit No. 3?

11 A. That's correct.

12 Q. This is your work?

13 A. That's correct.

14 Q. In making a decision in Section 28 about
15 how to orient the spacing units so that you can
16 achieve maximum development on 320 gas spacing for
17 that section, how does the isopach help you make those
18 choices?

19 A. The isopach is used in conjunction with the
20 structure map. You determine, you try to get the best
21 possible isopach value area that your thickest sand by
22 in there, and use that in conjunction with your
23 structure map to maximize your potential within
24 Section 28.

25 Q. Looking at the isopach, can you give us an

1 example or an illustration of the ranges of
2 differences you achieve with a well based upon
3 thickness of the Morrow B?

4 A. The Morrow B, the way I have it mapped, has
5 approximately 30 feet of thickness in the west half,
6 increases to approximately 50 and a little bit toward
7 the center part of the section. It goes back down to
8 approximately 40 feet on the eastern portion of the
9 section.

10 Q. In relation to offsetting or wells in the
11 area, I guess you have to go over to 26, two sections
12 away, what was the success of that well in relation to
13 thickness of the Morrow B sand?

14 A. That well was a successful Morrow test
15 based upon this same isopach that we used in this
16 area.

17 Q. And that had approximately 60 feet in it?

18 A. Yes.

19 Q. As we move south into Section 33, we find a
20 Morrow test in Section 33 in the southwest quarter
21 that is about 30 feet of thickness?

22 A. That's correct.

23 Q. Were you able to obtain a successful Morrow
24 well?

25 A. That well was essentially an extremely poor

1 producer, 226,000 cubic feet. So it really is a
2 nonproducer, just a little show of gas.

3 Q. How do you use the isopach to help you
4 decide the orientation of the spacing unit you want?

5 A. We use the isopach to try to get into the
6 thickest sand body that we can in the best structural
7 position and using our two-well concept to best
8 develop the section.

9 Q. If it is a north half-south half
10 orientation, how does the integration of the two
11 exhibits, the structure map and the isopach, affect
12 that decision?

13 A. The isopach value shows that the thick go
14 through the north-south. However, the structure map
15 shows a preferred orientation or a preferred structure
16 in the north half. So as you move south into the
17 section, you will be getting off structure, and it
18 would inspect your risk considerably.

19 So we'd use the isopach and structure map
20 in conjunction. And, therefore, the best locations
21 would be in the northwest quarter and northeast
22 quarter of Section 28.

23 Q. What happens if the orientation of the
24 spacing unit is such that there's a north half and a
25 south half? How does that affect your ability to

1 develop the whole section?

2 A. It would limit our ability to develop the
3 whole section. The first well would fit the mapping,
4 meet our criteria, but the south well would be at such
5 a risk that, based upon our mapping here right now, we
6 would not recommend a well if it was in the south
7 half.

8 Q. What do you achieve if you stand the
9 spacing units up and you have a west half and an east
10 half orientation to the 320 gas spacing units?

11 A. It gives us the opportunity to fully
12 develop the section. I have a location in the
13 northwest quarter and the northeast quarter.

14 Q. Each of which is upstructure from the south
15 half?

16 A. That's correct.

17 Q. And is comparable then in structural
18 position?

19 A. That's correct.

20 Q. Let's turn now to Exhibit No. 4 and look at
21 your stratigraphic cross-section. Before we discuss
22 the conclusions you reach about Exhibit No. 4, Mr.
23 Gawloski, show us the line of cross-section, what
24 wells you've picked.

25 A. This cross-section goes from the north end

1 across our Geronimo prospect. It's the well on the
2 far left. It goes through a well in Section 9, which
3 is our new discovery, the Mitchell Energy Anasazi
4 Federal #9 well, moves further south to our proposed
5 location in Section 28, and ties in a couple of the
6 wells in the Salt Lake south Morrow field, which is
7 the closest production to the south of us.

8 Q. Why have you chosen those wells to form a
9 line for the cross-section?

10 A. It gives us a link of production that we
11 have to the north and to the south, and it shows us
12 the character and nature of the sands that we are
13 chasing in this area.

14 Q. Excluding for a moment the Morrow B sand,
15 describe and characterize the potential in the other
16 Morrow sands for us.

17 A. There is potential in the other Morrow
18 packages, but we feel that it's somewhat limited in
19 the area. Our well in Section 9 did not have a very
20 good development of the Morrow C. So our primary
21 target in here is the Morrow B sand section.

22 Q. Let's look specifically at the Morrow B now
23 and describe that for us. What do you see about the
24 continuity of the sands from well to well?

25 A. The Morrow B or the sand package that lies

1 below that yellow line on the cross-section, and as
2 you can see as you go across this section here the
3 variability and discontinuous nature of these Morrow
4 sands. And we have more experience in this area and
5 have found that you need to develop this Morrow on a
6 320-acre proration to adequately develop the entire
7 section. The nature of these sands have a tendency to
8 come and go, and we do find new reservoirs in drilling
9 within the 320-acre proration unit.

10 Q. Based upon your experience in this area
11 with drilling Morrow wells, what is your conclusion
12 about the component of risk that you undertake in
13 drilling a well such as this?

14 A. Because of the nature of the Morrow in this
15 area, there is always a risk of not finding sands in
16 one area and finding them in another. The
17 discontinuous nature always increases the risk of
18 drilling for the Morrow in this area.

19 Q. Can you characterize this as step-out
20 development of the existing established Morrow
21 production?

22 A. To me, from our -- the way Mitchell is
23 looking at it, it is a wildcat well. We are drilling
24 north of a field, of the Salt Lake field, which we
25 feel has strong structural component to it and feel

1 that we're on another structural trend north of it
2 that has yet to be fully developed, and our closest
3 other production is up to the north where we are
4 currently active right now.

5 Q. Using this stratigraphic cross-section,
6 help us identify the interval that you have used to
7 isopach for Exhibit No. 3.

8 A. The interval I used to isopach is the
9 interval between what's marked on the exhibit as Top
10 of the Morrow B and Top of the Morrow C. That's the
11 interval that I used to isopach.

12 Q. Having taken that interval then, how do you
13 calculate the thickness within that interval by which
14 you then had prepared the isopach?

15 A. I go through that section and determine
16 what is the sand in here, and I've used the porosity
17 cutoff that is what we use as a standard for
18 production.

19 Q. That's the 7 percent?

20 A. 7 percent density. And then I essentially
21 go in there and add up the thicknesses within that
22 section.

23 Q. The isopach that's been generated then is a
24 net sand isopach?

25 A. A net sand isopach of this Morrow B

1 interval.

2 Q. Using the 7 percent cutoff?

3 A. That's correct.

4 Q. Let me ask you to turn to Exhibit No. 5
5 now. Exhibit 5 doesn't have the quarter section or
6 the section lines on it, and you're going to have to
7 help us not get confused in the display, Mr.
8 Gawloski. If you'll, before we talk about the
9 conclusions, look at 5 and tell us where it came
10 from. What is this?

11 A. This is a plat that was prepared by
12 archeologists. When you go into a federal leasehold
13 and you're proposing a well, you have to have an
14 archeological survey done on the location and the pad
15 site before you can proceed with your permitting.

16 Q. You had chosen for the development of the
17 section a well located in the west half 1,980 from the
18 north and 1,980 from the west?

19 A. That's correct.

20 Q. Where do we find that location on Exhibit
21 5?

22 A. It's marked in the center portion of the
23 diagram right there under the word "ridge" on dune
24 ridge, on the lower portion of the dune.

25 Q. Were your field people successful in

1 obtaining surface clearance for a well to be located
2 as you had initially proposed?

3 A. No, they were not.

4 Q. What happened?

5 A. First off, there is a topographical
6 consideration. There was a large dune ridge, and
7 that's shown in there by the dashed line, essentially
8 trending northeast-southwest, and that location was on
9 the edge of that dune ridge.

10 The other consideration in here, which goes
11 along with the topographical consideration, is an
12 archeological site, and you can see it has a
13 designation there, and it's shown by the bolder dark
14 line on the dune ridge. Essentially, the dune ridge
15 was a topographical feature that he found
16 archeological -- whatever -- artifacts on there. So
17 that we did not have clearance then to proceed with
18 that location.

19 Q. Were you able to locate a well that
20 satisfied the surface limitations within the west half
21 of Section 28?

22 A. That's correct.

23 Q. And where did you ultimately find that you
24 had an approvable surface location?

25 A. Moving a little bit to the north where the

1 location would be approximately 1,650 from the north
2 line instead of 1,980. That would give -- you can see
3 the box around that location is the boundary of the
4 well pad. That would be essentially the minimum
5 distance we could move from there and still conduct
6 our business in a manner that would have been approved
7 by the archeologist and probably the BLM.

8 Q. In assessing the risk, is there a material
9 difference or a change in the risk if you moved from
10 the closest standard location to this unorthodox
11 location?

12 A. No, the risk is about the same. It's a
13 minimal distance that we're moving here.

14 Q. The choices you've made about the
15 methodology for exploration of the section, the two-
16 well concept, is that made by you as a geologist
17 independent initially of any other limitations or
18 considerations?

19 A. No, sir. There's other considerations that
20 we use in conjunction with the geological information.

21 Q. Initially, however, what goes into the
22 decision that you make as a geologist about how to
23 orient the spacing units?

24 A. Initially, it's what I do with the
25 geological end of it is what I do initially, and then

1 if there's any other considerations, we address them.

2 Q. Apart from other considerations now,
3 initially then the decision is made upon your geologic
4 work independent of ownership and surface limitations?

5 A. That's correct.

6 Q. And what was that decision that you made
7 for Section 28?

8 A. That the best way to develop Section 28
9 would be to have stand-up proration units in the east
10 half and the west half and have a well posed in the
11 northwest quarter of that section.

12 Q. If that is approved by the examiner, what
13 does that allow Mitchell to do then with the
14 subsequent development of the section?

15 A. It allows Mitchell to then proceed with a
16 well. If deemed productive, the first well deemed
17 productive, we could then proceed with a well in the
18 northeast quarter of that section.

19 Q. Having made that initial decision, were
20 there any other informations or facts brought to you
21 subsequently that caused you to change your opinion
22 about the orientation of the spacing units?

23 A. A leasehold consideration was brought to my
24 attention of an unleased partial in the northeast
25 quarter.

1 Q. The topographic limitation was brought to
2 your attention?

3 A. That's correct.

4 Q. And you've had to adjust for that?

5 A. That's correct.

6 Q. Any other thing that's affected your choice
7 about how to orient the spacing units?

8 A. No.

9 Q. Having selected the orientation, summarize
10 for us the criteria then that gets you to the ultimate
11 conclusion about the stand-ups. What's the criteria?

12 A. The criteria is one that we used in this
13 area, that we have used in this area. We take our
14 geologic maps, cross-sections. We take the isopachs,
15 determine where the best -- area of best thickness in
16 the Morrow B, which is our primary target. We then
17 look at our structure map. And then we look at both
18 of those and take those into consideration to
19 determine what the best locations would be to
20 adequately develop the section.

21 And in this case, using their structure and
22 isopach, locations in the northwest quarter and
23 northeast quarter on the east and west half proration
24 units were the best way to fully develop Section 28.

25 Q. Describe for us the criteria you use in

1 selecting the well location for each of the two
2 spacing units once you've decided the orientation.

3 A. Well, once we decide the orientation, in
4 this case a west-half proration unit, we normally go
5 to what we feel is our best orthodox location, which
6 is what we did in this case. And then we submit that
7 to get permitted based upon clearance of BLM approval
8 of that location.

9 MR. KELLAHIN: That concludes my
10 examination of Mr. Gawloski. We would move the
11 introduction of Exhibits 1 through 5.

12 EXAMINER STOGNER: Exhibits 1 through 5
13 will be admitted into evidence at this time. Thank
14 you, Mr. Kellahin.

15 Mr. Cavin, your witness.

16 MR. CAVIN: Thank you, Mr. Examiner.

17 EXAMINATION

18 BY MR. CAVIN:

19 Q. Can you help me with your name, please.
20 I'm sorry, I'd just like to pronounce it correctly.

21 A. Ted Gawloski.

22 Q. Gawloski, okay. If I mispronounce it, you
23 have my apologies in advance.

24 A. I'm used to it.

25 Q. Well, Sealy is not a real winner either for

1 easy names to pronounce.

2 Let me refer you to Exhibit 5 as far as the
3 various locations you have looked at, and can you tell
4 me where is it on this map that you can't drill? I
5 guess I didn't understand that, from a topographical
6 --

7 A. The center portion of the plat, essentially
8 right under the "g" in "ridge" was the initial
9 proposed location, orthodox location.

10 Q. And that would be, right under the "g"
11 would be 1,980?

12 A. Right. You can see right to the right of
13 that, it says 1,980 from the north and west and the
14 arrow pointing there. That is the location.

15 Q. Is that where the crosshatch is?

16 A. Yes.

17 Q. The crosshatch is 1,980, 1,980?

18 A. Yes.

19 Q. So that crosshatch is on the ridge, so to
20 speak?

21 A. It's right on the edge of the ridge and
22 extremely close to the archeological site. The thing
23 we didn't have drawn here is the size of the well pad
24 which would be what you see on each of those other
25 ones; so the well pad would essentially be in the

1 middle of that dune ridge and archeological site.

2 Q. How large is that well pad?

3 A. It says up there 400 by 400.

4 Q. Okay, 400 by 400. Am I correct, if you
5 move the 1,980, 1,980 location south, you have to move
6 it south at least 200 feet because of the well pad?

7 A. That's approximately it, yes.

8 Q. So you have to have a well pad that's 400
9 by 400; is that pretty much --

10 A. That's what we normally do for our Morrow
11 wells. That's not my area of expertise, but he has
12 this drawn in here as such. That's what he would do.

13 Q. So that's standard for your Morrow wells?

14 A. I'm led to believe that, yes.

15 Q. Do you make any exceptions for these
16 location sizes, your pad, I should say?

17 A. Very rarely, because I do know this, you
18 have to have so much spacing out there for safety
19 reasons that you have to have enough room to do that,
20 and this is probably pretty standard for BLM deep gas
21 wells.

22 Q. Can you tell me, and I should probably know
23 this, but IF #1 means?

24 A. That is an isolated find, I believe, is how
25 he describes that. There's isolated finds outside of

1 that dune ridge that he found and he's numbered.

2 Q. And IF #2 is the same sort of thing?

3 A. Yes.

4 Q. Okay. And it looks like that's an access
5 road that passes through there?

6 A. That's correct.

7 Q. The location 2,180 by 2,180, that is what's
8 acceptable for archeological and topographical
9 reasons; is that right?

10 A. That's correct.

11 Q. But not for geologic reasons?

12 A. That's correct. Well, there was two -- we
13 had two locations here, and we chose the northern one
14 based upon geological considerations.

15 Q. But 2,180 and 2,180 is acceptable from
16 archeological --

17 A. Yes.

18 Q. Can you tell me, I think you've said you
19 work in the Permian Basin area. What other areas do
20 you work?

21 A. I've worked the southeast New Mexico for
22 all 12 of my years as a geologist.

23 Q. So that's basically 100 percent of your
24 work?

25 A. It's been in the Delaware Basin, southeast

1 New Mexico, that's correct.

2 Q. It sounds like you've got quite an
3 impressive amount of geologic data. Is that something
4 you would share with the parties you're seeking to
5 join, in your interpretations?

6 A. It's something we do not normally do unless
7 we're bound by some sort of agreement. The other
8 parties usually make up their own decisions, have
9 their own staff of geologists and usually will do that
10 themselves. So we don't normally do that.

11 Q. Would you consider it in this case if it
12 would help facilitate the -- what would Mitchell's
13 position be?

14 A. We already did. I sent a portion of this
15 structure map to geologists at Strata to help in these
16 discussions we were having so that we might alleviate
17 some of these problems, and I sent a portion of that
18 structure map up to them, and it was confirmed that he
19 did receive that map.

20 It's something that we sometimes do to help
21 alleviate a problem in an area to get something going,
22 but normally it's not something that we do. It's more
23 above and beyond what we usually do.

24 Q. Did you share that information with Maralo
25 and is it Santa Fe that your other partner is?

1 A. That's correct. We did not -- they have
2 their own geologists, and they work that up
3 themselves.

4 Q. Do they have access to the information that
5 your maps are based on?

6 A. I do not know. I'm sure they have the well
7 control. Now, the seismic data, I do not know. I
8 cannot speak for them on that. I know we have a very
9 extensive seismic database in this area.

10 Q. I would refer you to your Exhibit No. 2,
11 and I take it this is a structure map showing the top
12 of the Morrow. Now, can you tell me, if you could,
13 where would you locate this well if you could pick the
14 prime location within this structure without
15 considerations to the north line?

16 A. Without considerations -- you would still
17 have to be within legal bounds of a location. You'd
18 have to have some sort of consideration of the north
19 line.

20 Q. I guess I'm trying to get your opinion,
21 what is the best location, legal location, if you had
22 a north half proration unit in the north half of
23 Section 28 according to your structure map?

24 A. If you were looking at it from a one-well
25 standpoint, you could drill a location a little bit

1 better on the structure, but our methodology in here
2 is to maximize our potential for the sections. And
3 we've done that with several wells in this area,
4 several Morrow wells, including the well in Section 9,
5 and we have not changed our approach for this location
6 at all.

7 Q. So basically what you're saying is, if you
8 had to pick the best structural position in 28 that
9 was a legal location for the north half, it would be
10 further north than the proposed location?

11 A. You could move it a little further north if
12 you were looking at it from a one-well standpoint.

13 Q. And that would be a better geologic
14 location for this one well?

15 A. For this one well.

16 Q. So it's your opinion that the risk should
17 be the same throughout any part of Section 28, and
18 that's the 200 percent plus costs?

19 A. That's correct.

20 Q. And it's your opinion that the south half
21 location is just too risky, and you don't see any
22 geologic merit to that?

23 A. If we were forced to do north half-south
24 half, based upon this mapping, I would not recommend
25 it to my management. Structure in here does play an

1 important role. The field on the south and west on
2 this map is, as you can see, on a structural feature
3 at Salt Lake South Field, and as you get off of that
4 structure, you do get wells that you get into some
5 zones that do not produce and are wet.

6 Q. It appears that some of these wells are
7 pretty good producers that are offstructure; is that
8 correct?

9 A. Which wells are you referring to?

10 Q. Well, I guess the -- up in Section 14 up in
11 that Quail Ridge area, those wells up there, it would
12 appear they're somewhat offstructure?

13 A. That well is on the edge of a structure. I
14 would interpret it as being on the edge of a
15 structure, and there's stratigraphic and structural
16 components to the wells in here.

17 Q. How about the well in Section 19 of that
18 same township and range?

19 A. There is no producer in Section 19 of that
20 township and range. Which one are you referring to?

21 Q. Let me get my bearings here. I believe
22 that would be 19-33. Let me confirm that for you.

23 A. That well in 19 of 19-33 is an extremely
24 poor producer. Eight million out of the Morrow I
25 would not call a good Morrow producer.

1 Q. Eight?

2 A. Eight million. That's something we
3 certainly would not call -- I'm sure you can go
4 through here and find one or two exceptions, but
5 you're going to find most of them that are going to be
6 either on or on the edge of a structure, and the well
7 field to the south definitely has a structural
8 component to it.

9 Q. So I guess your position is it's structural
10 and stratigraphic?

11 A. Structure plays a very important part in
12 this area, and I think it's obvious from the map here.

13 Q. What would be more significant, the age of
14 structure or the top of the structure, in your opinion
15 -- I'm sorry, the edge?

16 A. The edge of the structure versus the top of
17 the structure?

18 Q. Um-hm. Let me just rephrase this. If you
19 had your druthers, you're saying you'd come right in
20 at the very top of the structure?

21 A. That's not correct. If I was looking at
22 this one map by itself, that may be what you would
23 do. That is not the way we do business. I can find a
24 structure out here that has no sand in it, and it's
25 not going to do me any good to drill it. So I do not

1 use this map by itself.

2 The well in Section 5 is in a nice
3 structural position, and it had very little sand in
4 it; so it didn't do any good to be on the structure.
5 You've got to use all the tools you have available to
6 you. In this case, you use your isopach and your
7 structure.

8 Q. Do you feel like this is a pretty precise
9 art here to pick these locations?

10 A. This is as precise as we can get it with
11 the data we have.

12 Q. Is the -- and I believe this is the correct
13 name -- the Anasazi well up in Section 9 to the north,
14 Section 28, is that onstructure or offstructure or on
15 the edge?

16 A. It came in mapped on the edge of a
17 structure. And, again, this is a prime example of how
18 we work a section in this area. We determined that
19 this section with the isopach and the structure to
20 maximize the development of that section, we were
21 going to have lay-down proration units, and we're
22 currently in the process of permitting a well in the
23 south half of Section 9, again, under the same
24 methodology as we're doing in Section 28, get a good
25 thickness necessary of sand and in it a good

1 structural position.

2 Q. But your well you're proposing in the south
3 half of 9 would be as far offstructure as the
4 alternate location you propose in Section 28; is that
5 correct?

6 A. As far offstructure?

7 Q. Let me see. You said you proposed a well
8 in Section 9?

9 A. That's correct.

10 Q. In the south half?

11 A. That's correct.

12 Q. Now, there were two locations that you told
13 me were approved on the Exhibit 5?

14 A. I never said they were approved yet. They
15 were proposed locations.

16 Q. Would be acceptable as far as topographic
17 and archeological?

18 A. Yes.

19 Q. Now, based on your mapping, the location
20 2,180 from north line, 2,180 from the west line, my
21 question is, you're saying that's too far
22 offstructure, I believe?

23 A. No, I didn't say that. I said it is
24 farther offstructure. If I was going to move the
25 location, if I had two choices to move the location, I

1 would move it to get a little bit better structural
2 position. That's just a good geological decision to
3 make. Why move further downstructure when you don't
4 have to?

5 Q. So if I heard you correctly, your primary
6 reason from a geologic standpoint for this location as
7 opposed -- or, I'm sorry, a west half spacing unit is
8 so that you can get two wells in the north half of
9 Section 28?

10 A. That's correct.

11 Q. And this we can talk to Mr. Smith about
12 this, to recall him, but under the operating
13 agreement, would you have any problem sharing your
14 geologic information with the participants? Would
15 that be a problem for the participants who participate
16 in the well you're proposing?

17 A. We are doing that right now. I believe
18 we're sharing the geologic data right now. It is not
19 something we normally do because we take a lot of
20 time, and we have a lot more data than most people do
21 to do this. And we've already gone above and beyond
22 and shared structure maps with seismic data on there
23 that we don't normally do.

24 We've sort of bent over backwards to try to
25 work with you, with Strata on this; so it's not

1 something we normally do, but we're doing it right
2 now.

3 MR. CAVIN: I have no further questions,
4 Mr. Examiner.

5 EXAMINER STOGNER: Thank you Mr. Cavin.
6 Mr. Kellahin, any redirect?

7 Mr. Kellahin?

8 MR. STOVALL: He already said no, but I
9 don't have any.

10 EXAMINER STOGNER: Mr. Stovall, my
11 apologies. I have no other questions of this
12 witness.

13 At this particular time, we'll take a
14 recess for lunch until --

15 MR. STOVALL: Tom, how long is your
16 engineer?

17 MR. KELLAHIN: Five minutes. He's going to
18 authenticate the AFE. If that's not a dispute, maybe
19 we can just put it in the record.

20 EXAMINER STOGNER: Let's go ahead and hear
21 the engineer's testimony at this time.

22 (Thereupon, a discussion was held
23 off the record.)

24 MR. KELLAHIN: Mr. Examiner, with the
25 stipulation of opposing counsel that Mitchell's

1 Exhibit 18 may be introduced and accepted as
2 reasonable cost for the drilling and completion of
3 this well, I will choose not to present Mr. Richard,
4 the engineer who would otherwise authenticate this
5 exhibit.

6 With that stipulation then we would seek
7 the introduction of Exhibit No. 18.

8 MR. STOVALL: Mr. Kellahin, who can answer
9 the current status of the APD, Application for Permit
10 to Drill?

11 MR. KELLAHIN: We've got somebody here that
12 can.

13 EXAMINER STOGNER: I thought your
14 engineering witness was going to do that at this time.

15 MR. KELLAHIN: No. He was going to
16 authenticate this AFE.

17 EXAMINER STOGNER: As far as authenticity
18 of the AFE, I have no --

19 MR. STOVALL: We can admit Exhibit 18 as
20 the proposed Authorization For Expenditure without
21 objection and contest.

22 MR. KELLAHIN: Our APD with the BLM is on
23 file and has not yet been approved. I think that's a
24 correct representation.

25 EXAMINER STOGNER: I'd like to hear from

1 your witness, if you've got one.

2 MR. STOVALL: Has he been sworn?

3 MR. KELLAHIN: We may have to take a break
4 and put him on after lunch and get our act together on
5 APD because I wasn't prepared to present the status of
6 approval of the APD.

7 MR. STOVALL: Mr. Kellahin, so you can
8 prepare properly, since you are not, the concerns that
9 we're expressing with this is with respect to the
10 status of approval of the specific location and
11 whether you've got the clearances necessary or whether
12 it's still in a review or it's simply an
13 administrative process to get the approval done.

14 MR. KELLAHIN: I need to double-check and
15 make sure we give you the right answer.

16 MR. STOVALL: With those considerations,
17 that's what you need to talk to your --

18 EXAMINER STOGNER: So with that, we'll take
19 a break for lunch and reconvene as 1:45

20 (Thereupon, the lunch recess was taken.)

21 EXAMINER STOGNER: The hearing will come to
22 order. Mr. Kellahin?

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

24 MR. STOVALL: Has this witness been sworn,
25 Mr. Kellahin?

1 MR. KELLAHIN: No, sir, he has not. I'd
2 like to call Mr. Mark Stephenson at this time.

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

6 EXAMINATION

7 BY MR. KELLAHIN:

8 Q. Mr. Stephenson, would you please state your
9 name and occupation?

10 A. My name is Mark Stephenson. That's spelled
11 with a p-h instead of a v. I'm employed by Mitchell
12 Energy Corporation as the manager of the production
13 regulatory affairs department.

14 Q. Do you have a technical degree in any
15 professional area, Mr. Stephenson?

16 A. No, sir, I don't. I have a business degree
17 from Sam Houston State University in Huntsville,
18 Texas. I graduated in December of 1979, and I've been
19 employed by Mitchell Energy Corporation since January
20 of 1980, various capacities in the field of regulatory
21 affairs. I've been in my current capacity as manager
22 of the production regulatory affairs department since
23 January of 1988.

24 Q. As part of your duties and among your
25 experiences, have you participated on behalf of your

1 company with regards to drilling, permitting, and
2 examining rules and regulations for oil and gas wells
3 to be drilled in what is called the Division Order
4 R-111-P area?

5 A. Yes, sir, I have.

6 Q. Are you also familiar with the Secretary of
7 the Interior's Federal Potash Enclave and the rules
8 and regulations that apply to drilling in those areas?

9 A. Unfortunately, yes, I'm very familiar with
10 that order also.

11 Q. With regards to your company's efforts to
12 obtain an approved APD from the Bureau of Land
13 Management for the drilling of a specific well, have
14 you been involved in that process?

15 A. Yes, I have.

16 MR. KELLAHIN: We tender Mr. Stephenson as
17 an expert in regulatory affairs dealing with drilling
18 in the potash area.

19 EXAMINER STOGNER: Any objections?

20 MR. CAVIN: No, sir.

21 EXAMINER STOGNER: So qualified.

22 Q. (BY MR. KELLAHIN) Mr. Stephenson, let me
23 ask you, sir, to identify for the record what has been
24 marked as Mitchell Exhibit No. 20.

25 A. Exhibit No. 20 is a copy of the

1 Application for Permit to Drill for the subject well.
2 It was filed by Mitchell with the Bureau of Land
3 Management's Carlsbad office on November 20, 1992.

4 Q. This APD was filed over the signature of
5 George Mullen. Who is George Mullen?

6 A. George Mullen is an employee of my
7 department. He is the one who files most of the APD's
8 in the southeast New Mexico area. Occasionally I file
9 a few of those. In this particular case, Mr. Mullen
10 is the one that filed this APD.

11 Q. This request was filed under letter dated
12 November 20 of 1992, and you're seeking approval of
13 the location as specified before this examiner, being
14 the unorthodox well location we've described?

15 A. Yes, sir, that's correct.

16 Q. As to that location, what are the
17 applicable rules as you know them concerning drilling
18 in the potash area or within R-111-P? Where is this
19 acreage?

20 A. This particular acreage is located on
21 federal acreage. There's no state acreage involved in
22 Section 28. And, as such, we're really operating
23 under the '86 secretarial order rather than R-111-P.

24 Q. Where are we in relation to R-111-P
25 acreage? Are we within or without that boundary?

1 A. We're actually within the boundary of the
2 designated R-111-P area.

3 Q. But you are more than a mile away from an
4 LMR?

5 A. I'm not certain that we're more than a mile
6 from an LMR.

7 Q. With regards to the notice requirements
8 under R-111-P, what is the requirement that applies to
9 this tract and what, if anything, have you done?

10 A. What we do and our procedure basically on
11 permitting wells with the BLM, wells that are subject
12 to the 1986 secretarial order, the BLM has less formal
13 guidelines on permitting wells within the designated
14 potash area, that area designated under the '86
15 secretarial order. They don't have strict guidelines
16 as far as notice requirements are concerned, as you
17 have, for example, in R-111-P.

18 Our normal course of action for any well
19 within the designated secretarial area, potash area,
20 is to contact the BLM prior to the time we file the
21 Application for Permit to Drill. We consult with the
22 mine engineers in the BLM's Carlsbad office.

23 Q. Was that done in this case?

24 A. Yes, sir, it was. I did that myself in an
25 attempt to determine whether or not the BLM would

1 envision any difficulty with respect to this location
2 due to potash restrictions. We do that in an effort
3 to save ourselves and BLM some time and trouble, if
4 possible. There's some cases where it's very clearly
5 going to create a problem, say, if you're encroaching
6 upon an LMR or a certain part of the enclave. There's
7 other areas where I think they can look at the
8 information they have in that office and give you a
9 fairly good educated guess as to whether or not they
10 would anticipate any problem with permitting the well
11 at that location. That's part of what we do.

12 The other part of what we do is we
13 determine through contact within the parties that
14 would be required to be notified of the application,
15 and we give notice to those parties.

16 Q. Was that done in this case?

17 A. Yes, sir, it was.

18 Q. Let me direct your attention to Exhibit 21
19 and have you identify and describe that exhibit.

20 A. Exhibit No. 21 is a letter dated November
21 17, 1992. It's addressed to Mr. Randy Foote with
22 Mississippi Chemical Corporation in Carlsbad, New
23 Mexico. It's a letter giving notice to Mr. Foote and
24 Mississippi Chemical Corporation that Mitchell
25 intended to file a Permit to Drill with the BLM at

1 this location.

2 Q. What, if any, response have you received
3 from Mississippi Chemical Corporation concerning this
4 application?

5 A. We have filed no response. We have
6 received no response at all, affirmative or negative,
7 no indication of protest from Mississippi Chemical.

8 We do periodically check on the status of
9 these APD's. As you can see, this particular
10 application has been pending for over two months now,
11 and we did communicate with the Carlsbad office of the
12 BLM last week, and we're advised that the application
13 was still pending, but we are informed that it had
14 been reviewed with respect to potash restrictions, and
15 there didn't appear to be a problem there. Of course,
16 that won't be determined definitively until the permit
17 is actually issued, but that's what we were told last
18 week.

19 Q. In terms of obtaining an approvable APD,
20 are you aware of any other regulations, restrictions,
21 or limitations on the approval of the APD?

22 A. No, sir, I'm not.

23 Q. Have you satisfied the requirements for the
24 surface use in terms of its location with regards to
25 archeological sites or surface limitations such as the

1 dunes involved in this case?

2 A. I believe we have. As has been previously
3 testified, this site has been reviewed by an
4 archeologist with the BLM or one that was retained to
5 conduct an archeological survey on behalf of the BLM.
6 And as a result of that archeological survey, we had
7 to move the location. But my understanding is that
8 the proposed location is acceptable with the BLM.

9 Q. Based upon your current information on this
10 particular proposal and your experience in general
11 with this type of permitting, what is your conclusion
12 about the approvability of this location as we've
13 requested it from the examiner?

14 A. After several checks with the BLM, again,
15 we have no indication that there's any problem in
16 permitting this well. My expectation would be that
17 this permit will be approved.

18 MR. KELLAHIN: That concludes my
19 examination of Mr. Stephenson. Move the introduction
20 of Mitchell's Exhibits 20 and 21.

21 EXAMINER STOGNER: Thank you, Mr.
22 Kellahin. Do you have any questions?

23 MR. CAVIN: Yes, sir.

24 EXAMINATION

25 BY MR. CAVIN:

1 Q. Mr. Stephenson, can you tell me where the
2 -- I'm looking at Exhibit 20, and it's the map with
3 the one-mile radius, I guess. Can you tell me where
4 the LMR is just for --

5 A. Well, I don't know how familiar you are
6 with BLM regulations or the OCD regulations on potash
7 and specifically with respect to LMR's, but LMR's are
8 considered confidential by the potash companies and
9 the regulatory agencies, and that's proprietary
10 information. We don't have that information.

11 What we have to do is rely on the agencies
12 to tell us whether or not we're within a certain
13 distance from the LMR.

14 Q. Okay. When do you expect to receive
15 approval based on your experience?

16 A. Based on our communication with the BLM
17 last week, I would think it would be in the next
18 couple of weeks.

19 Q. Can you tell me, Mr. Stephenson, where the
20 proposed location is with respect to either proven or
21 probable potash reserves?

22 A. I don't have a copy of the BLM's 1984
23 potash map in front of me. I think the examiner may
24 have one. I'd be happy to look at his map and try to
25 help you with that question.

1 MR. STOVALL: Before we even bring that
2 into the thing, what's the relevance of that to the
3 forced pooling application?

4 MR. CAVIN: Well, I guess if I knew a
5 little more about the potash, it might move our
6 location one way or another. I just don't know.

7 MR. STOVALL: If the location gets
8 approved, it gets approved by the BLM, and we don't
9 have any input into that whatsoever because it's all
10 federal land. If it were state or fee lands, then we
11 would have an approval process, the OCD.

12 MR. CAVIN: Just as to the casing then is
13 all the OCD has involvement in or not even that?

14 MR. STOVALL: Well, even the casing. This
15 is a federally regulated well. The only thing the OCD
16 really has jurisdiction over with respect to this well
17 is the consolidation of interests. Although BLM and
18 OCD are generally consistent on those requirements,
19 they are administered in this case by the BLM.

20 MR. CAVIN: So it's not a matter to be
21 decided by the OCD?

22 MR. STOVALL: Correct.

23 MR. CAVIN: I have no further questions.

24 EXAMINATION

25 BY MR. STOGNER:

1 Q. Mr. Stephenson, really what I asked you up
2 here today for was essentially, in looking at Exhibit
3 No. 5, 1,980, 1,980 is marked on this exhibit?

4 A. Yes, sir.

5 Q. What I wanted to find out was, did the BLM
6 come out and request you move this location? You had
7 two locations to choose from. I was just trying to
8 find what the status was as opposed to the surface
9 location and what kind of BLM requirements were made
10 and what were the steps as far as the on-site review
11 and how much did Mitchell Energy really have a say in
12 moving this location?

13 A. Okay. I'd be happy to go through that with
14 you, Mr. Examiner.

15 Q. Just keep it brief but do cover it.

16 A. All right. Well, anytime we drill a well
17 on federal acreage, we're required to have an
18 archeological survey conducted. We did retain an
19 archeologist to do that here. As a result of this
20 survey, they determined that the original proposed
21 location was not acceptable due to topographic and
22 archeological reasons.

23 When they do find a location unacceptable,
24 we do try to give them alternate locations to look at
25 or at least an area that would be acceptable. In this

1 particular case, the archeologist came up with two
2 alternate locations. We looked at, I guess, the
3 options and decided that the northern location,
4 northern alternative here, was the best option in this
5 particular case.

6 Q. Now, this option that was, has it had an
7 on-site review by the BLM personnel at this point?

8 A. By the archeologist?

9 Q. Anybody else in the BLM's bureaucracy that
10 required on-site. I know it changes in different
11 areas.

12 A. I don't know the answer to that, Mr.
13 Stogner. I do know the archeologist has approved it.
14 They do have to do an environmental assessment, and
15 I'm not sure whether that has been completed at this
16 particular location. Again, our last communication
17 with the BLM indicated that there appeared to be no
18 problem with this location.

19 EXAMINATION

20 BY MR. STOVALL:

21 Q. There are more than just archeological
22 considerations?

23 A. That's right. And during a permitting
24 process, we don't try to communicate with each
25 individual that's involved in the permitting process

1 at the BLM. That would just be impossible to track
2 that.

3 What we do try to do is find out what stage
4 of the permitting process it's in and when we can
5 anticipate approval, or if there's any complications,
6 we certainly want to know about that, but we don't try
7 to monitor these things with every person at the BLM
8 that touches the paper.

9 Q. In your experience with the BLM and based
10 on where you are at this stage of the process, do you
11 believe you would have heard from them if the surface
12 location were unacceptable for any reason?

13 A. Yes, sir. I can certainly say that in the
14 past, anytime that they determine there's a problem
15 with the permit, they're very expeditious in advising
16 you of such.

17 Q. Both locations are unorthodox; is that
18 correct?

19 A. Both locations?

20 Q. Both of the alternate locations, the
21 southern one and the northern one? If I'm reading
22 your measurements right, it's a standard size section,
23 you're too close to the east line of the proration
24 unit at 2,180?

25 A. That's correct.

1 EXAMINER STOGNER: That's all I have for
2 this witness. Any other questions for Mr. Stephenson?

3 MR. KELLAHIN: No, sir.

4 EXAMINER STOGNER: Can he be excused?

5 MR. CAVIN: May I ask one question, please,
6 Mr. Examiner?

7 FURTHER EXAMINATION

8 BY MR. CAVIN:

9 Q. We heard earlier about the pad size. It's
10 400 by 400. Is that a requirement of the BLM, or is
11 that a Mitchell practice?

12 A. I think that's something that's probably
13 jointly determined by both parties. I can tell you
14 that 400 by 400 is our standard pad size for a Morrow
15 well location.

16 MR. CAVIN: Okay.

17 EXAMINER STOGNER: Any other questions?

18 MR. CAVIN: No further questions, sir.

19 EXAMINER STOGNER: Mr. Stephenson may be
20 excused. Mr. Kellahin, do you have anything further?

21 MR. KELLAHIN: No, sir, we have nothing
22 further to present in evidence.

23 EXAMINER STOGNER: Okay, Mr. Cavin.

24 MR. CAVIN: Mr. Examiner, our first witness
25 is Mark Murphy, president of Strata Production

1 Company.

2 MARK MURPHY,

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

5 EXAMINATION

6 BY MR. CAVIN:

7 Q. Mr. Murphy, can you please tell the
8 examiner your background in the oil and gas business?

9 A. Yes. My name is Mark Bertram Murphy. I'm
10 president of Strata Production Company. I've been
11 involved in the oil and gas business since I was 15
12 years old when I started as a roustabout in
13 southeastern New Mexico and west Texas. My family has
14 been actively involved in oil and gas ventures in
15 southeastern New Mexico and west Texas since 1957.

16 I've worked as a landman for Eagle Oil and
17 Gas out of Dallas, Texas, a Dallas independent, and
18 Robb Hart Oil and Gas out of Lockhart, Texas. In
19 1983, I joined my father and sister in a New Mexico
20 oil and gas company by the name of Murphy Operating
21 Corporation. We operated at our peak approximately
22 400 wells, primarily in southeastern New Mexico and
23 west Texas. We appeared numerous times at the Oil
24 Conservation Commission, seeking unitization approval
25 on waterfloods, primarily, San Andres waterfloods

1 located in Roosevelt and Chaves Counties.

2 I currently serve as president and have
3 since late 1991, as president of Strata Production
4 Company. We operate approximately 70 wells. We
5 produce a little over 2,000 barrels a day.

6 I serve as an industry adviser to the
7 Petroleum Recovery Research Center at New Mexico Tech
8 in Socorro. I've testified in front of numerous
9 legislative hearings on issues from the enhanced oil
10 recovery legislation that was passed a couple years
11 ago to state land policy to federal land policy. I'm
12 currently a past board member and treasurer of the New
13 Mexico Oil and Gas Association. I'm currently the
14 director and vice president of the Independent
15 Petroleum Association of New Mexico.

16 I've served as a three-year term with the
17 National Public Lands Advisory Council, which advises
18 the Bureau of Land Management and the Department of
19 Interior, specifically in the last administration,
20 Secretary Lujan and Director Sy Jamison on federal
21 lands policy. I served as vice chairman for that
22 council. Last year I served as chairman for that
23 council. I've been reappointed for a three-year
24 term.

25 I could go on, but I hope that will do it.

1 MR. CAVIN: Mr. Examiner, I'd like to
2 tender Mr. Murphy as an expert qualified to testify on
3 land matters and also as an oil and gas operator.

4 EXAMINER STOGNER: Are there any
5 objections?

6 MR. KELLAHIN: Is Mr. Murphy going to be
7 testifying about geologic or engineering aspects with
8 regards to this case?

9 MR. CAVIN: No.

10 MR. KELLAHIN: No objection.

11 EXAMINER STOGNER: Mr. Murphy is so
12 qualified.

13 THE WITNESS: Thank you.

14 Q. (BY MR. CAVIN) Mr. Murphy, I would refer
15 you to what is marked as Strata Exhibit A and ask if
16 you could describe that for the examiner?

17 A. Yes. Exhibit A is a reproduction of a
18 Midland Map Company, 1 inch I believe to 4,000 scale,
19 for a portion of Lea County and specifically shows
20 Township 20 South, Range 33 East. Somewhat centered
21 on that map is Section 28.

22 It is color-coded. The pink acreage is
23 acreage that Mitchell apparently has an interest in.
24 There are three leases involved in that. The one
25 marked No. 1 expires April 1, 1994, and I believe it's

1 Lease No. 57280. No. 2 expires 9-1-95, I believe;
2 it's lease No. 62228. And No. 3 expires 10-1-93, and
3 it's lease No. 77074.

4 The lease shown in blue, which is the
5 southwest quarter of the northeast quarter of Section
6 28, expired on or about July 1 of 1992. The Midland
7 map indicates that the southeast of the southeast is
8 owned by one Bulldog Energy. It's shown in yellow.
9 It expires 4-1-96. And Strata's lease No. 82927 is
10 shown in green, and it expires November 1, 1994.

11 During our initial conversations, my
12 initial conversations with Mr. Smith of Mitchell, I
13 suggested to him that they consider a north half
14 proration unit. That, based on my understanding of
15 the arrangement between Mitchell and Santa Fe and
16 Maralo, had that been done, would result in Mitchell
17 owning 50 percent, Santa Fe owning 25 percent, and
18 Maralo owning 25 percent.

19 At one point it was pointed out to me that
20 that lease had expired on July 1 of 1992, some seven
21 months ago, ample time, in my opinion, to nominate and
22 purchase that lease. Once again, I believe it was
23 testified this morning that a request was made
24 sometime in September, some two months after the lease
25 had expired.

1 Had a south half proration unit been
2 formed, then Mitchell would own approximately 25
3 percent, Santa Fe and Maralo would own approximately
4 12-1/2 percent apiece, Strata would own 37-1/2
5 percent, Bulldog would own 12-1/2 percent.

6 Q. When were you first contacted by Mitchell,
7 Mr. Murphy, in connection with their proposed well?

8 A. If I could, I would like to refer to our
9 Exhibit No. 2, which is Strata Production Company's
10 letter dated January 12, 1993. It has also been
11 entered this morning as Mitchell's Exhibit No. 16.

12 Q. Okay.

13 A. In this letter beginning on page 2, I
14 summarized the telephone conversations and relevant
15 correspondence --

16 Q. Can I ask you, before you begin, do you
17 keep a telephone log, Mr. Murphy?

18 A. Yes, I do.

19 Q. Thank you.

20 A. On October 26, Mr. Mitchell -- excuse me --
21 Mr. Smith with Mitchell contacted me and said that
22 they were considering -- "they" being Mitchell -- were
23 considering drilling a Morrow well somewhere in the
24 northwest quarter of Section 28, and that they would
25 like to form a west half proration unit, if I recall,

1 and that a portion of our lease being the south half
2 of the southwest quarter be included therein in that
3 proration unit.

4 I advised them at that time that we would
5 probably not participate but that we would consider
6 it. We would also consider or farming out. I
7 informed Mr. Smith at that time that we had other
8 partners; that until a deal, specific deal was
9 negotiated that we could recommend, that I couldn't
10 represent those partners; that, however, historically,
11 normally when we reached an agreement that we could
12 recommend to our partners, they would, in most cases,
13 go along with that deal, but I could not guarantee
14 that.

15 Since we're on this subject, I would else
16 bring to your attention Mitchell's Exhibit No. 11,
17 which is Strata correspondence dated December 9,
18 1992. The last sentence in the bottom of page 1 --
19 and I don't have it in front of me -- but it goes on
20 to say that any terms would have to be approved by
21 Strata's partners, and I believe the word "partners"
22 is on the top of page 2 of that letter.

23 Q. Let me just ask you, in the process --

24 A. Sure.

25 Q. -- did you ever say anything in connection

1 with these conversations that would indicate that you
2 had the unfettered authority to represent these
3 partners?

4 A. Absolutely not. As a matter of fact, I
5 informed Mr. Smith to the contrary. Each of these
6 partners had their own interest in here. That there
7 were numerous partners; I believe I said 10 or 15. I
8 think the actual number may be closer to 16. But that
9 the process we normally go through in this case is
10 that we would negotiate to the best of our ability.
11 If we felt like that we could recommend the deal to
12 our partners, I'd be happy to try to facilitate the
13 deal by working with my partners directly.

14 Q. Why don't you continue and tell me what
15 happened next?

16 A. We had a series of telephone conversations,
17 and they're summarized under Nos. 2 and 3 of Strata's
18 Exhibit 2, Mitchell's Exhibit 16, where we went back
19 and forth on various terms.

20 At one point on December 16, as a result of
21 Strata's correspondence dated December 9, which is
22 Mitchell's Exhibit 11, Mr. Smith called me and said
23 that they were inclined to go along with our farmout
24 proposal; however, it was subject to certain
25 conditions. And the condition that he mentioned was

1 that we would be required to convert all of our
2 override to working interest.

3 I reminded him that we had numerous
4 partners, and that each partner may want to do
5 something different. Some may elect to convert at
6 payout; some may not, and that that would be extremely
7 difficult to do. I reminded him of these partners
8 also in the context of administrative burdens that it
9 would take and suggested that they reconsider a
10 purchase of the lease.

11 Q. Did Mr. Smith ever ask for a list of these
12 partners?

13 A. No, he did not.

14 Q. Did you ever do anything to indicate to Mr.
15 Smith you would provide that list?

16 A. Well, yeah, he did not up to this point.
17 We had a subsequent conversation on January 13. And
18 at that point, in response to a letter where I
19 suggested that he contact the partners directly, I
20 asked if he was going to do that. He said no, that he
21 had no intention of doing that; that they felt like
22 they had met the notice requirements. I told him that
23 he was aware of these partners all along. He said
24 that he had never been provided a list of those
25 partners.

1 So I wrote a letter dated January 13, I
2 believe, but I don't have the Mitchell exhibit number,
3 but it was entered into the record this morning, which
4 listed the parties, their addresses, and their
5 interests.

6 Q. Sorry to divert you. Go ahead --

7 A. That's okay. Once we had made agreement on
8 our deal, I contacted, either myself or other people
9 in Strata, contacted the partners outlying the deal
10 terms to them. Everybody was agreeable to doing it.
11 We went ahead and drafted the letter agreement dated
12 December 30.

13 Prior to sending that letter agreement, I
14 called Mr. Smith and said -- and reviewed the letter
15 agreement, specifically reviewing with him the
16 overriding royalty interest pooling provision. He
17 responded that when he had gone back to management, he
18 had failed to bring that to their attention but to go
19 ahead and send the letter anyway. And so I did.

20 I didn't hear anything from him until I got
21 the January 5th, I guess the next day, Mitchell
22 correspondence. I was surprised to get that
23 correspondence because it basically did not reflect
24 the deal terms that we had agreed to. I had just
25 spent a lot of time and effort constructing a letter

1 agreement, the December 30th letter agreement, and we
2 talked on January 5th just shortly after that
3 agreement was faxed to me.

4 That conversation is summarized under No.
5 13 on page 5 of Mitchell's Exhibit No. 16.

6 Q. Let me ask you a question regarding the
7 letter dated December 30, '92, which is really a
8 letter agreement, because there's been some question
9 raised regarding paragraph 7 of the letter agreement.
10 Where did you get that provision, that language?

11 A. From a previous letter agreement that we
12 did with another company.

13 Q. Was that a lease sale?

14 A. Yes, it was. It was a federal lease sale.

15 Q. Was it your intention for this to be deal
16 specific, or was this to represent that you had
17 authority to make any kind of deal that they wanted to
18 make?

19 A. It was deal specific.

20 Q. And that was certainly your intention,
21 wasn't it?

22 A. That was certainly my intention, and until
23 we communicated -- I had no -- I never represented
24 that I could bind the other parties until they
25 approved the terms of the deal. And once we arrived

1 at terms that I thought we had agreed upon, and I
2 communicated that deal to the parties, they agreed.
3 And at that point then I could represent them and did
4 so in that letter because I had their approval to do
5 so on those specific terms.

6 Q. What's the big deal between override and
7 working interest? Why would they mind not taking an
8 interest under the farmout?

9 A. They would be subject to operating
10 agreements and other contractual agreements, and I
11 simply would not feel comfortable in -- I could not
12 represent their interest. They'd have to sign those
13 things as individuals.

14 Q. Who are these parties, as a general rule?

15 A. As a general rule, they're long-term
16 investors of Strata.

17 Q. So you had some familiarity with what they
18 typically invest in?

19 A. Absolutely.

20 Q. Do you find them to be the kind of folks to
21 take working interest with big companies?

22 A. Generally not.

23 Q. That's all the questions for that.

24 Could you explain for me, again, I got a
25 little bit confused there, the chronology on the

1 farmout agreement and how exactly it was that that
2 didn't work out?

3 A. Oh, the farmout agreement terms. We sent a
4 letter, I believe it's dated December 9, it's Mitchell
5 Exhibit No. 11, whereby we proposed to either sell or
6 farm out. And then that resulted in our telephone
7 conversation of December 16. And that's when Mr.
8 Smith advised me that they would be inclined to accept
9 the farmout provisions. However, it was a conditional
10 acceptance, which I've always taken to be a
11 counterproposal. And the condition was that all of
12 the override had to be converted to working interest.

13 Q. Did you think that \$150 was a fair price?

14 A. Absolutely. As a matter of fact, and once
15 again it's summarized, telephone conversation, this is
16 No. 3 on page 2 of Mitchell Exhibit No. 16 -- that Mr.
17 Smith said he felt that the acreage price of \$300 an
18 acre originally was excessive. I informed him that I
19 did not feel it was excessive, that it was consistent,
20 if not lower, to what recent state and federal sales
21 had brought in this area. I was familiar that
22 Meridian had purchased the Exxon acreage in Section
23 32, which is immediately adjacent to the Strata
24 acreage for \$1,000 an acre. I'm not sure -- I'm sure
25 I did not specifically mention that, but what my point

1 was is that it was not out of line.

2 When he came back with \$150 an acre, he
3 said that was somewhat higher than what he had been
4 paying to the north; however, the acreage to the north
5 generally is not involved in what is now a very hot
6 play concerning Delaware and Bone Springs, primarily
7 Delaware rights.

8 Q. So you have some familiarity with this area
9 in general?

10 A. Yes, I do. We operate approximately ten
11 wells in Sections 32 and 33 of 20-33 and Section 4 of
12 whatever the township is immediately to the south.

13 Q. These partners that are listed in your
14 January 13 letter, which is Mitchell Exhibit 17, are
15 these long-term partners that have had an interest in
16 this property, or are these just people you just went
17 out and sold it to?

18 A. These are long-term partners. As a matter
19 of fact, those partners actually own a similar
20 interest in Section 33 immediately offset. They were
21 existing partners in Section 33 when this came up for
22 bid. Even though we did not have a formal area of
23 mutual interest, we offered it to those partners so
24 they could participate.

25 Q. Is there anything you said to Mr. Smith

1 throughout these conversations you think could be
2 construed as the kind of representation that he
3 indicated you made as to your authority to deal for
4 these partners?

5 A. Absolutely not and to the contrary. I told
6 him all along that we had numerous partners; that the
7 way we've handled this in the past is that we'd
8 negotiate the best deal we could, and we'd either
9 recommend it or not recommend it to our partners. But
10 that I could not bind them in any way, but as a
11 general rule that they would go along with our
12 recommendation.

13 Q. Do you have experience in this area? Do
14 you deal with any parties where you have undisclosed
15 owners or parties contacting you to see whether you're
16 interested in selling a lease or farming out?

17 A. Absolutely. As a matter of fact, many
18 times in leasehold situations like this, you don't
19 immediately make assignments to all the parties until
20 a well is drilled or some action taken. So if you do
21 sell it, you only have to handle one assignment from
22 Strata to whoever the purchaser is. If we assign this
23 out to all these parties, they would have to gather up
24 -- we'd have to gather up 15 assignments into
25 Mitchell or to whomever.

1 Q. Is there anything further you'd like to say
2 with respect to the January 12 letter, Mr. Murphy?

3 A. Excuse me just a second. Let me review it
4 here quickly.

5 Q. We can come back to it later.

6 A. Not at this time. I may wish to return to
7 it later.

8 Q. Okay. Next I'd refer you to what is marked
9 as Strata Exhibit C, and that's a Model Form Operating
10 Agreement.

11 A. Yes, sir.

12 MR. STOVALL: Exhibit C or Exhibit 3, Mr.
13 Cavin?

14 THE WITNESS: Well, I hope -- have we.

15 MR. STOVALL: Change them to numeric,
16 please.

17 MR. CAVIN: I apologize for that. It
18 should be Exhibit 3.

19 THE WITNESS: Yes. This was an operating
20 agreement that was forwarded to me by Mr. Smith at
21 Mitchell.

22 Q. (BY MR. CAVIN) Are there any provisions
23 that you feel unusual, particularly in the context of
24 a forced pool where you really don't have any choice
25 and you're being sort of married by shotgun, so to

1 speak?

2 A. There's a number of provisions that I find
3 unusual. The first, I draw your attention to Article
4 V.B.1. as found on page 4. This has to do with the
5 Resignation or Removal of the Operator. It's industry
6 practice that -- and it's on the preprinted form --
7 this has been deleted and stricken in this case, if
8 the operator fails and refuses to carry out its
9 duties, then the remaining parties have the right to
10 vote the operator out. In this case, it puts the
11 burden of actually have to bring a suit, actually
12 initiating some sort of legal action. That would be a
13 very difficult burden on a small independent oil and
14 gas company.

15 Q. Have you ever seen a provision like that?

16 A. No.

17 Q. How many operating agreements have you
18 reviewed in your capacity as an operator over the
19 years?

20 A. Hundreds.

21 I would also draw your attention to Article
22 VI.B.1. This article basically says an operator
23 should only use its best efforts to provide
24 nonoperators 24 hours advance notice of any work to be
25 conducted on Saturday, Sunday, and legal holidays.

1 It is common practice in the oil and gas
2 industry, recognizing that it's a seven day a week, 24
3 hour business, that you always provide weekend and
4 nighttime numbers in case of discussion or
5 notification is required. This lessens that burden on
6 the operator having to make proper notice and consult
7 its partners.

8 I also draw your attention to Article XVI.
9 It's the Other Provisions towards the back of the
10 operating agreement. This is -- excuse me. Did I say
11 XVI? It's XV. Excuse me.

12 This provision provides that if the
13 operator's interest is under common control of another
14 company or transferred, then the voting provisions of
15 the operating agreement are not necessary. In other
16 words, the operations go with the operator, and in
17 this case Mitchell.

18 That is not so unusual really, but what is
19 somewhat unusual is, if they sell "substantially all,"
20 and I'm quoting, "substantially all of operator's oil
21 and gas properties, then the transferee shall
22 automatically become the successor operator without
23 the approval of the nonoperators."

24 This does not give the partners a chance to
25 vote on this new operator. In other words, we're

1 basically -- whoever Mitchell, should they elect and
2 decide to sell to somebody else, that becomes the
3 partner's operator whether we like it or not.

4 Q. So it's anybody? There's no limitations
5 that you're aware of?

6 A. No limitations.

7 Q. How would that normally be handled?

8 A. Normally, when you sell a property like
9 that, you no longer own an interest in the contract
10 area. Therefore, then the partners would vote on whom
11 the operator would be.

12 Q. Okay.

13 A. I'd also draw your attention to Exhibit C,
14 COPAS Form Accounting Procedure Joint Operations, page
15 4, provision III, Overhead, which is 1.A.(1). I'm
16 referring to the drilling well rate of \$6,500 and the
17 producing well rate of \$650 per month.

18 At this time I'd like to reference Strata's
19 Exhibit No. 4 (indicated). This was faxed to us by
20 Ernst & Young. I did not have -- and I believe they
21 were referred to this morning as Ernst & Whinney.
22 They are now known as Ernst & Young. They publish the
23 monthly drilling and monthly producing well rates.

24 You'll note that the 1992 brochure has not
25 come out, or at least I have not received it. So the

1 one that I had before was 1991. We did, however, call
2 Ernst & Young and asked them to fax us their most
3 recent, and you'll note that it has the 1992 amounts
4 on there. It shows the median drilling rate for a gas
5 well in west Texas and eastern New Mexico to be
6 \$5,000, and the producing rate, the median, to be
7 \$500.

8 Q. Are those numbers actually going the other
9 way? I look at '91. Can you tell me, are they
10 decreasing from '91 to '92, or am I misreading this?

11 A. The '91 and '92 median on the drilling well
12 rates were the same. The mean increased, it appears
13 to me.

14 Q. From '91 to '92?

15 A. Yes. It depends on whether you're talking
16 about the median or the mean. The 1991 median for
17 10,000 to 15,000 foot wells was \$5,000. The 1992 was
18 also \$5,000.

19 Q. Are you looking at oil or gas?

20 A. I'm looking at gas.

21 Q. I'm sorry, can you tell me again what the
22 median is for that depth well?

23 A. 1991 is \$5,000. 1992 is \$5,000.

24 Q. And then?

25 A. Producing well rates, 1991 median is 513,

1 1992 median is 500.

2 Q. You're right. I'm sorry. I was reading --
3 I guess I need bifocals.

4 Let me ask you, it's my understanding from
5 testimony earlier this morning that the \$6,500 and the
6 \$650 is the charge made to Mitchell's other partners.
7 Is there any problem -- you're an operator -- is there
8 any problem for most accounting systems breaking that
9 out and charging different people different operating
10 rents?

11 A. No. As a matter of fact, it's fairly
12 common. In many cases, you have to -- especially in
13 some of the older properties, you have to administer
14 many times two or more operating agreements. They not
15 only have different overhead rates; they also have
16 different conditions and procedures. So that's fairly
17 common.

18 Q. Would you have a rate to propose to
19 Mitchell under that agreement?

20 A. I take issue with their rate, and I cite as
21 the industry standard the Ernst & Young amounts which
22 are shown as Exhibit 4.

23 Q. Are there any other comments regarding the
24 operating agreement?

25 A. No.

1 Q. Next I would refer you to Exhibit 5, Strata
2 Exhibit 5, and ask if you would describe that for the
3 examiner?

4 A. Yes. That's a notice of staking for the
5 Pavo No. 2 to be located 810 feet from the south line
6 and 1,980 from the west line. This well, a formal APD
7 has not been submitted yet, but the BLM and the
8 archeologist have approved the drill site.

9 Q. Is that an orthodox location for a south
10 half spacing unit?

11 A. Yes, it is.

12 I'd like to, during our conversation -- and
13 I say "our" -- my conversation with Mr. Smith of
14 November 18 -- this is shown as No. 3 on page 2 of
15 Strata's Exhibit No. 2 -- I had stated early on in our
16 conversations that we would prefer that Mitchell form
17 a north half proration unit and leave the Strata lease
18 out of it so that we would have -- one option, of
19 course, is to drill a well in the south half.

20 He said that they intended to form the west
21 half proration unit based on lease exploration
22 considerations. And that was the exploration of the
23 northwest quarter of the the southwest quarter in
24 October of 1983. I said that we did not see any
25 technical basis for that and asked him to reconsider.

1 Later on he pointed out to me -- during one
2 of the points of my December 30, 1992, letter
3 agreement was the sharing of geologic information,
4 which is relatively customary in the industry -- he
5 pointed out that there was an expired lease, the
6 southwest quarter of the northeast quarter shown as
7 lease No. 2 -- excuse me, it's colored blue on Exhibit
8 A.

9 Q. Exhibit 1?

10 A. Exhibit 1, excuse me. He said that they
11 were concerned that if the information got out, that
12 when that lease did come available, that they would
13 have additional competition as a result of the
14 knowledge of the geologic information on the well they
15 proposed in the northwest quarter. And I suggested
16 the way to handle that, that it was not our intent to
17 go and try to compete with them there, that we would
18 be happy to sign a confidentiality and non-compete
19 provision as it pertains to that information in that
20 lease.

21 Q. If you could complete the sale that you
22 proposed; was that the context?

23 A. That's exactly right.

24 Q. What are your plans with this location?
25 You state 1,980 from the west line and 810 from the

1 south line of Section 28.

2 A. We are going to seek a voluntary approval
3 of a south half proration unit, and absent that, then
4 we will move for compulsory pooling.

5 Q. For what?

6 A. For the south half of Section 28.

7 Q. What type of well are you contemplating
8 there?

9 A. A Morrow well.

10 Q. Is it your feeling that Mitchell has made a
11 good faith effort to provide notice to all interested
12 parties, Mr. Murphy?

13 A. No, it's not. I had informed Mr. Smith all
14 along that we had undisclosed owners. I had asked,
15 and I would have to check the correspondence, but I
16 believe -- excuse me.

17 MR. KELLAHIN: While Mr. Murphy is
18 searching for his response to the question, I will
19 introduce an objection. I don't think it's the
20 province of this witness to determine whether or not
21 the notification is correct.

22 EXAMINER STOGNER: I agree with Mr.
23 Kellahin. I believe you have already stipulated, Mr.
24 Cavin, that Strata has no problem with the
25 notification today or as far as Strata's interest.

1 You might want to move on, please.

2 MR. CAVIN: Okay.

3 Q. Mr. Murphy, is there anything in Mitchell's
4 exhibits that you would like to refer to? Do you have
5 a copy of those?

6 A. No, I do not have a copy.

7 Q. For further comment (indicated)?

8 A. I don't believe so at this time.

9 Q. Any further testimony you'd like to put on
10 the record?

11 A. No, sir.

12 MR. CAVIN: Mr. Examiner, at this time I
13 would like to move to admit Strata Exhibits 1 through
14 5.

15 EXAMINER STOGNER: Are there any
16 objections?

17 MR. KELLAHIN: No objections.

18 EXAMINER STOGNER: Exhibits 1 through 5
19 will be admitted at this time.

20 Mr. Kellahin?

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

22 EXAMINATION

23 BY MR. KELLAHIN:

24 Q. Mr. Murphy, was the Hinkle law firm
25 attorney correct in his analysis of the abstracts and

1 the ownership when he concluded in his title opinion,
2 which is presented as Mitchell Exhibit 7, that as of
3 the appropriate date of that title opinion, the
4 working interest ownership or the operating rights, if
5 you will, for that portion of the south half of the
6 southwest quarter that was proposed to be included in
7 the west half spacing unit was owned and controlled by
8 Strata Production Company?

9 A. He lists here that we're -- I think the
10 term is record title holder or leasehold holder.

11 Q. Yes. Is that correct?

12 A. That's correct.

13 Q. And at that point had you as record title
14 owner of that lease assigned out any of the working
15 interest ownership in that lease?

16 A. No.

17 Q. So the operating rights and the record
18 title were still held by Strata Production Company?

19 A. That's right, with the proviso that Mr.
20 Smith had been given notice that there were
21 undisclosed owners.

22 Q. You told him there were silent interest
23 owners that -- the identity of those individuals was
24 not disclosed to him?

25 A. It was not disclosed until he requested

1 them during a telephone conversation of January 13.

2 And, by the way, I take objection to the term "silent
3 partners." I never used that term.

4 Q. Undisclosed partners?

5 A. I believe the term was, we have partners in
6 this lease.

7 Q. And you did not disclose to Mr. Smith the
8 name and address of those individuals or companies?

9 A. Not until so requested, no.

10 Q. Is Elliott and Waldron Title & Abstract
11 Company correct in their certification that for the
12 period from November 6, of '92, ending on January 19,
13 1993, that their search of the Lea County records
14 shows that, as of public record information, Strata
15 Production Company is still the owner of the federal
16 lease record title and operating rights?

17 A. To the best of my knowledge, yes.

18 Q. The Joint Operating Agreement that you've
19 described in your testimony, the one that Mr. Smith
20 provided to you?

21 A. Um-hm.

22 Q. You've given us three or four items of
23 concern to you. If we change all those, will that
24 cause you to commit Strata's interest to the west half
25 spacing unit? Will that solve the problem?

1 A. No. We have been -- I point these out
2 because of it being shown as a model form and the
3 number of changes that have been made to this model
4 form. It is our position that we would maintain that
5 the proration unit be a north half proration unit;
6 that the footage location that is proposed by Mitchell
7 is orthodox for a north half proration unit.

8 Q. So the language and terms of the Joint
9 Operating Agreement is not the dispositive issue that
10 resolves this matter?

11 A. No.

12 Q. The unorthodox well location that Mitchell
13 is seeking approval for in fact moves farther away
14 from any acreage that Strata controls?

15 A. It moves to the north, that's true.

16 Q. Away from you?

17 A. That's correct.

18 Q. You described a while ago that there were
19 ten wells in this area in which Strata Production
20 Company either had an interest in or operated? Did
21 you say --

22 A. We serve as operator and have an interest
23 in.

24 Q. Are any of those Morrow gas wells?

25 A. New Mexico Federal #1, which is located in

1 Section 4, was a Morrow gas well. It was recompleted
2 in the Bone Springs and later in the Delaware.

3 Q. At the time it was a Morrow well, did you
4 act as the operator?

5 A. I believe that well was purchased or farmed
6 out -- I can't recall -- from Grace Petroleum, and I
7 am unsure as to the status when we took possession.

8 Q. It was originally drilled by Grace
9 Petroleum?

10 A. That's what I recall, yes, sir.

11 MR. STOVALL: Excuse me just a second, make
12 sure that we know what you're talking about. Is that
13 1 in 33, 20-33, Mr. Murphy?

14 THE WITNESS: No, I'm sorry. It would be
15 New Mexico Federal #1. It would be in Section 4 down
16 to the southwest of the colored acreage. It's shown
17 with a circle around it as a discovery well.

18 MR. KELLAHIN: I can help you find that on
19 Exhibit --

20 MR. STOVALL: That's in that 32, what is
21 it, 19 and I guess -- 21 and 32; is that corerct?

22 EXAMINER STOGNER: Long section to the
23 south?

24 THE WITNESS: Yes, sir, that's correct.

25 MR. STOVALL: It's in the northwest corner

1 of Section 4?

2 EXAMINER STOGNER: That would be Lot 6 of
3 that long section?

4 MR. STOVALL: You're looking, Mr. Kellahin,
5 at Mitchell Exhibit 1, I think?

6 MR. KELLAHIN: Mitchell Exhibit 1 shows
7 that same well, Mr. Stovall.

8 MR. STOVALL: Just to know where we are in
9 relation to -- please continue.

10 Q. (BY MR. KELLAHIN) Within the area, and
11 we're looking at, I guess, your Exhibit No. 1, is it,
12 sir? Is that what you mean by -- or Exhibit A, yeah,
13 that one?

14 A. Exhibit 1. I believe I referred to it as A
15 before.

16 Q. Within that area, does Strata Production
17 Company currently operate any producing Morrow gas
18 wells?

19 A. Not shown on this, I don't believe so
20 that's shown on this map. There would be one slightly
21 off of the map to the west. I believe it's the Snowy
22 Federal #1. I can't remember the precise location,
23 but it would be a mile or two west of the edge of the
24 map.

25 Q. Are you the operator of that well?

1 A. And actually I think that well has recently
2 been recompleted in the Wolfcamp, if I recall.

3 Q. When you look at Mr. Gawloski's Exhibit No.
4 1, the Mitchell exhibit, are there any wells on that
5 plat that are producing Morrow gas wells that Strata
6 Production Company operates?

7 A. There's a lot of wells shown on this map,
8 and I haven't spent -- I didn't think about this. I
9 haven't spent a lot of time, but I don't believe so.

10 Q. Do you have a working interest in any of
11 the Morrow gas wells shown on either one of those
12 displays?

13 A. Absent the New Mexico Federal #1 and the --
14 oh, you mean wells operated by somebody else that we
15 may own a working interest in?

16 Q. Yes, sir.

17 A. I don't believe so.

18 Q. Let me go to the topic of the overhead
19 rates?

20 A. Yes.

21 Q. Have you taken the Ernst & Young
22 tabulation, which I understood is 1991 information --

23 A. 1992.

24 Q. Have you taken that information and applied
25 the escalator to it under the COPAS attachment?

1 A. The escalator will not take effect until
2 April of 1993. So those rates are current for '92,
3 and normally the operating agreement, the excalation
4 provision, once a rate has been agreed to, escalates
5 annually the 1st day of April.

6 Q. It's consistent with the custom and
7 practice to have these operating agreements to have
8 COPAS attachments to them that have these escalators
9 in them?

10 A. Yes. If you're asking whether the COPAS
11 form is a model form that's used quite a bit in the
12 industry, the answer is yes.

13 Q. Yes. And it has an escalator in it?

14 A. Yes, it does.

15 Q. Is it unusual to you as an expert in this
16 area to find on Mitchell Exhibit 9 that an original
17 Joint Operating Agreement in fact had the overhead
18 rates escalated?

19 A. No, it's not unusual. Once an agreement
20 has been reached between parties, since you can't
21 pre-determine what the escalator will be, it's
22 provided by Ernst & Young annually. However, that is
23 not to say that a party coming into an agreement is
24 bound the same way the parties have already -- that
25 are already part of that agreement are bound.

1 Q. Exhibit No. 5?

2 A. Yes.

3 Q. The Division Form C-102?

4 A. Yes.

5 Q. How come that's not fully completed?

6 A. Well, it's completed as far as the staking
7 and a plat. This is what I had in my file.

8 Q. Have you filed that yet?

9 A. I don't know. I don't believe so, but I --
10 well, no, I take that back. We filed three of them.
11 We filed the Pavo 1, Pavo 2, and Pavo 3 in each
12 proration unit of Section 28 along our lease, the
13 southwest quarter -- southwest southwest, southeast,
14 and so forth.

15 Q. I need to get that back from you so we can
16 figure this out. Do you have another copy?

17 MR. CAVIN: Let me see. Oh, yes we've got
18 one.

19 Q. (BY MR. KELLAHIN) Tell me again now, in
20 Section 28, you've got this Pavo Federal 2 which is
21 down here in the southeast of the southwest. You've
22 got that one on this C-102. You said there were some
23 others?

24 A. Yes. There's one in the southwest of the
25 southwest.

1 Q. Southwest southwest, okay?

2 A. Southeast southwest, and southwest
3 southeast. There's one in each of those 40's. No,
4 excuse me, not that one but that one.

5 Q. Okay. You haven't declared a spacing unit
6 for the Pavo Federal #2 on the form?

7 A. I didn't complete this form, but no, I
8 don't see one on there. The reason that we've staked
9 those wells is that Meridian is currently drilling
10 some Delaware wells in Section 32. I believe they
11 have four locations staked. They've completed two of
12 those.

13 Q. These are Delaware stakings?

14 A. These are Delaware stakings with the intent
15 that the Pavo #2 could either be drilled to the
16 Delaware, if it's successful, or to the Morrow. In
17 other words, a deep well would more than likely be
18 drilled if there are shallow proven pays.

19 Q. And your plan then would be a south half
20 dedication?

21 A. That's correct.

22 Q. When are you going to share that plan with
23 Mitchell?

24 A. We are right now.

25 Q. Prior to this very moment, have you ever

1 proposed that as a Morrow well submission?

2 A. We're watching the drilling activity out
3 there, Mr. Kellahin, trying to determine what is
4 prudent for us to do.

5 Q. Have you filed an APD?

6 A. No, we have not. We have not filed any
7 APD's because we have not determined the depths that
8 these wells will be drilled.

9 MR. KELLAHIN: No further questions.

10 EXAMINER STOGNER: Mr. Cavin, any
11 redirect?

12 FURTHER EXAMINATION

13 BY MR. CAVIN:

14 Q. Yes. Why is it you haven't filed an APD?
15 It's just seven days ago that negotiations broke
16 down. Were you still trying to work something out?

17 A. Well, that and there's two other wells.
18 Mitchell has just completed their well in the
19 northeast of the southwest, and they have also got two
20 wells staked. I do not know the status of the
21 drilling. One in the southwest of the northeast and
22 one in the southeast of the northeast of Section 32.

23 We also have plans to work on it over our
24 Gavilan Federal #1 which is in Section 33.

25 Q. What about Section 32 lands that Meridian

1 just acquired? You've worked pretty close with
2 Meridian. Do you know if they have any plans in
3 Section 32?

4 A. My understanding is they have drilled and
5 completed their second well, and they have two more
6 staked.

7 Q. So there's a lot going on out in this area?

8 A. That's correct. There's a tremendous
9 amount of Delaware activity out in this area.

10 Q. Have you critically reviewed the gas
11 balancing agreement and some of the other provisions,
12 the special provisions of the operating agreement?

13 A. No, I have not. The only thing I noted on
14 the gas balancing agreement, it is not the model form
15 that we use. I believe -- and it may be reprinted by
16 Mitchell, using the same language. I just don't know,
17 but there is a model form, I believe, that's been done
18 by Mountain States Legal Foundation or Rocky Mountain
19 Oil and Gas or RMOGA or somebody, but there is a model
20 form that we're used to using. And I have not
21 reviewed that against the gas balancing agreement.

22 Q. Would you propose, if a gas balancing
23 agreement is even necessary, would you propose that
24 model form as opposed to -- since you're familiar with
25 it and since it is a model form, as opposed to this

1 gas balancing agreement?

2 A. I don't know without reviewing this gas
3 balancing agreement. It may be substantially the same
4 as the model form agreement. I'm not sure.

5 MR. CAVIN: I have no further questions.

6 EXAMINER STOGNER: Mr. Stovall?

7 MR. STOVALL: All of my questions have been
8 answered.

9 (Thereupon, a discussion was held
10 off the record.)

11 EXAMINER STOGNER: I have no questions of
12 Mr. Murphy at this time. Any other questions? He may
13 be excused.

14 Mr. Cavin?

15 MR. CAVIN: Mr. Examiner, I'd like to call
16 George Scott as a witness.

17 MR. STOVALL: Mr. Scott, would you sit at
18 the end of the table, please.

19 GEORGE L. SCOTT, JR.

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

22 EXAMINATION

23 BY MR. CAVIN:

24 Q. Mr. Scott, could you state for the examiner
25 your background in the oil and gas industry?

1 MR. STOVALL: State your name first,
2 please.

3 THE WITNESS: George L. Scott, Jr.,
4 Roswell, New Mexico.

5 Q. (BY MR. CAVIN) And your association with
6 Strata?

7 A. With Strata, I own some of the stock in
8 Strata. Also my organization, Scott Exploration, is
9 involved with Strata in the sense that we try to
10 originate prospects, and Strata operates them.

11 Q. Could you give us -- state your background
12 in the oil and gas industry, please, Mr. Scott.

13 A. It goes back to 1952. I have a B.S. and an
14 M.S. in geology from the University of Oklahoma. I
15 worked nine years for the old Humble Company. That's
16 Exxon now. And I've been an independent for nearly 30
17 years in Roswell, New Mexico.

18 MR. CAVIN: Mr. Examiner, I would tender
19 Mr. Scott as an expert in petroleum geology.

20 EXAMINER STOGNER: Any objections, Mr.
21 Kellahin?

22 MR. KELLAHIN: No objection.

23 EXAMINER STOGNER: Mr. Scott, let me make
24 sure I've got this straight. You're here today with
25 Mr. Cavin as a geologist, or you're here with Strata

1 today as a geologist?

2 THE WITNESS: Yes.

3 EXAMINER STOGNER: Is that correct?

4 THE WITNESS: Yes.

5 EXAMINER STOGNER: Thank you. You may
6 proceed.

7 Q. (BY MR. CAVIN) Mr. Scott, I was wondering
8 if you could refer to the various exhibits that
9 Mitchell presented earlier in the day, and let's see
10 if we can go over those.

11 MR. KELLAHIN: Do you want an extra copy of
12 those?

13 MR. CAVIN: That would be great. As you
14 can tell, I've memorized them but --

15 Q. Mr. Scott, if you would, please, I'd like
16 to refer you to the structure map that was prepared by
17 Mitchell Energy, Exhibit No. 2. It was admitted
18 earlier as Exhibit No. 2, and ask if you would
19 describe the critical wells, as far as Strata is
20 concerned, please, and tell me what role you think
21 structure plays in --

22 A. Okay. Let me preface, if I might, my
23 remarks by saying that we have a lot of respect for
24 Mr. Gawloski as a geologist. I know the geologists
25 that work for me have been in contact with him over

1 the years over various matters. And in looking at his
2 map, I basically -- we're talking here now about the
3 structure map -- I have no serious objection to the
4 way he interpreted this. There's always a little
5 difference in how geologists will contour maps.

6 The one thing that I would question a
7 little bit here is in the vicinity of the prospect in
8 Section 28, he made -- used the phrase, there was
9 "extensive" seismic. I wouldn't consider that you
10 have extensive seismic here. There is no north-south
11 line down the middle of Section 28, nor along the east
12 line of Section 28, nor north-south line in the middle
13 of Section 27 to the east.

14 So although there is fairly good, perhaps
15 we would say, seismic coverage, it's certainly not
16 extensive. And as to exactly how the structure would
17 result in the north half of Section 28 when it's all
18 said and done could be a little bit different than the
19 way he has it mapped. But by and large, I can find no
20 fault with the way he contoured.

21 Q. Mr. Scott, it seems that the decision is
22 based primarily on, first of all, two wells in the
23 north half and, secondly, on structure. Can you tell
24 me, in your opinion, how important structure is?

25 A. There are lots of Morrow wells that are low

1 structure wells. This is true in eastern Eddy County
2 and southwestern Lea County. There are wells that are
3 on top of the structure. There are wells on the flank
4 of structures. And this exhibit that they have
5 furnished us, Exhibit 2, shows many wells that are
6 down the flank or way down the nose, the plunge, the
7 structural plunge of these closed features that they
8 show here.

9 I personally don't consider it critical
10 whether you drill on top of a closed feature or not.
11 The sands are all lenticular, and the controlling
12 facet, criteria, in my opinion, on Morrow sand
13 production is whether or not you get the sand
14 channel. And those may occur low on the flank of the
15 structure as well as over the crest of a structure.

16 So I guess one could say, well, yes, I'd
17 prefer to catch a sand channel up high on a feature,
18 but, as a practical matter, we find them all over the
19 area out here. And many times the sands are actually
20 thicker and better developed in the structural lows.

21 Q. Mr. Scott, do you have much experience in
22 the Morrow, dealing with the Morrow formation?

23 A. Over the years, many times I've been
24 involved in the Morrow. I've made a lot of structural
25 maps. I've worked for -- when I was doing largely

1 consulting, I did work for many clients, structural
2 mapping, porosity isopaching cross-sections,
3 recommending locations, recommending reentries, and
4 then I have acquired some interest in Morrow wells,
5 too, as a result of this.

6 Q. So you have some -- how many wells would
7 you say we're talking about over the years?

8 A. Well, that's a tough one. I don't know.
9 Goodness. I've looked at and examined probably
10 several hundred Morrow wells in the course of my
11 investigations. I've been involved in, oh, I guess
12 four or five Morrow deals, perhaps, and been closely
13 associated with people drilling Morrow wells or
14 putting Morrow prospects together.

15 Q. Could you look at the production map, which
16 is Mitchell Exhibit 1, and also the structure map at
17 the same time and show us which wells -- I'd like to
18 have an idea of which of the wells are good producers
19 that are offstructure. Just give us a quick review,
20 if you would.

21 A. I haven't sat down and made a detailed
22 study of which are good wells and what are bad wells.
23 And when you say good wells and bad wells, that
24 depends on the price of gas.

25 Q. Sure.

1 A. You know, a well that's not too swift at 90
2 cents a thousand can be a hell of a well at \$5 a
3 thousand. So that enters into your judgment. All I
4 could submit to you is, in looking at the map here,
5 and all the wells are indicated as Morrow completions,
6 there are many of them that are on the flank of
7 structures and even in synclinal lows.

8 Q. Is it your conclusion then that structure,
9 while it may be a factor, it's certainly not the
10 controlling factor in a Morrow gas well?

11 A. Well, you've got to have the reservoir
12 rock. You've got to be in one of these sand
13 channels.

14 I guess you could give equal consideration,
15 perhaps, to structural position as well as your sand,
16 but I can tell you that many of the channels are found
17 on the flanks of structures.

18 I would like to submit in regard to that an
19 exhibit here. This is not a particularly fancy
20 exhibit, but we made a quick copy of this before we
21 left Roswell yesterday, and I would like to show you
22 an area in the next township south of here where
23 Morrow wells do not appear to have any close
24 structural association.

25 MR. CAVIN: We'd like to admit this as

1 Exhibit 6, Mr. Examiner, if there's no objection.

2 EXAMINER STOGNER: Are there any
3 objections, Mr. Kellahin?

4 MR. KELLAHIN: Has the witness
5 authenticated the exhibit?

6 THE WITNESS: Me? Yes. It was done
7 directly under my supervision.

8 MR. KELLAHIN: No objections.

9 EXAMINER STOGNER: No. 6 will be admitted.

10 Q. (BY MR. CAVIN) Could you tell us what is
11 contained on Exhibit 6, Mr. Scott?

12 A. Well, that is map contoured on top of the
13 Morrow Clastic Unit, an important division of the
14 Morrow, and a fairly good structural marker. And
15 encircled in orange are a number of Morrow wells. And
16 all you see are some minor structural nosing and minor
17 reentrance, southeast plunging dip. So I would submit
18 that probably the stratigraphy, the development of the
19 sands is equally important there.

20 Also, I noticed on the porosity, on the
21 isopach map, the sand isopach map --

22 Q. Which exhibit is that, please, Mr. Scott.

23 A. That is Exhibit No. 3.

24 Q. Mitchell Exhibit No. 3?

25 A. Yes -- that they display an area of very

1 thin sandstone down here coming across the southeast
2 corner of Section 32, trending right across the top of
3 the structure. So you can drill right on top of these
4 structures and not encounter with sand development.

5 Q. What else can you tell us about Mitchell
6 Exhibit 3, Mr. Scott, that would indicate that --

7 A. Well, Exhibit 3 --

8 MR. KELLAHIN: Excuse me, there wasn't a
9 question there.

10 Q. (BY MR. CAVIN) -- that would indicate that
11 the location proposed by Mitchell is maybe not the end
12 all or perhaps the best location?

13 A. Okay. On this exhibit, there is very
14 little well control in the vicinity of Section 28 or
15 21 or 20 or 16 or 17, back over to the east in 15,
16 22. This is a subsurface isopach map based on well
17 control, and yet the well control is very, very sparse
18 out there.

19 And this map, the isopach map purports to
20 show the thick and thins of the sands and I suppose a
21 representation of the way these channels, these
22 lenticular sand bodies in the Morrow, are developed.
23 And this approach is a valid approach, in my opinion.
24 I just want to point out that the well control is
25 very, very scarce out in here. There is no way of

1 predicting at this location that there's going to be
2 45 feet of net sand. There may be 80, or there may be
3 none based on contouring from well control.

4 Now, we all think in terms of trends,
5 sandstone trends, and it would appear that Mr.
6 Gawloski, down at the south here, saw a thick and made
7 an effort to connect it up with a thick six miles
8 north. And that might be a little risky, you know.
9 That would be my comment there.

10 Another thing about these kinds of maps, if
11 you'll look at the cross-section exhibit, these sands
12 do not all occur in the same place in this Morrow B
13 Unit. This type of map is a lumping map. You take
14 all of the sands in a particular interval and a
15 particular well, and then you contour to those values
16 from well to well. It doesn't mean that these are
17 going to be the same sands. These individual sands
18 may have completely different trends and orientations
19 than you would -- you might expect from looking at a
20 map like this.

21 Now, once again, this is about all you can
22 do with the Morrow until you actually drill some
23 wells. And then once you've drilled some close-in
24 wells, you can contour individual sands and work your
25 trends. But it's based on very poor remote well

1 control. So there is an element of risk right there
2 in Section 28 as to what you're going to find.

3 Q. What would you say about the Morrow
4 location that Mr. Murphy discussed earlier that Strata
5 is proposing in the southwest -- I'm sorry, the
6 southeast quarter of the southwest quarter of Section
7 28 based on the isopach map prepared by Mitchell and
8 also the structure map?

9 A. Well, the isopach map would indicate about
10 the same thickness of sand as for a location in the
11 north half, and the structure map would indicate you
12 would be coming down the flank of the structure, but
13 you're still without being the lowest position
14 structurally compared to areas adjacent there several
15 miles away.

16 So to answer your question simply, you
17 would be drilling on the flank of a closed structure,
18 just like many of the wells that are on this map.

19 Q. Is there anything you would like to add as
20 far as the structure map is concerned, Mr. Scott, as
21 far as your evaluation of it?

22 A. I believe that I've pretty well covered
23 that. I can't think of any other thing here. Let me
24 check my notes.

25 I guess I could state the obvious. If you

1 made a good well in the north half of the section, I
2 sure would feel safe about drilling in the south half.
3 You know, it gives us an important control well out
4 there.

5 Q. Would you see a need to drill another well
6 in the north half if you make a good well where they
7 have proposed?

8 A. I would not see a necessity to, no. Once
9 again, things like that depend on how thick your sands
10 are, what you think the orientation of those sands
11 are. And in this day and time, there are logging
12 techniques we can employ that give us trends of these
13 sand trends. Both Schlumberger and Halliburton have
14 logging tools that give you orientation of these sand
15 bodies.

16 So depending on the information gained from
17 that well, it could tell you whether you ought to
18 drill in the north half or the south half. My guess
19 is just as good a location could be made in the south
20 half as the north half as far as the information we
21 have here.

22 Q. Mr. Scott, I'd ask you to look at the -- I
23 believe that was the structure map -- the isopach map
24 prepared by Mitchell and tell the examiner if you have
25 any further critique or comment on that map.

1 A. I've already covered that, I believe, in
2 some of the remarks.

3 Q. Is there anything you'd like to add with
4 respect to Strata Exhibit 6 that you've provided?

5 MR. STOVALL: I'll take that as a no, Mr.
6 Scott.

7 MR. CAVIN: I'm sorry.

8 Q. Just one further question. Mr. Scott, is
9 it your opinion as an expert in petroleum geology that
10 a west half spacing unit is not warranted in this case
11 in light of the location of the well?

12 A. Say it again.

13 Q. A west half spacing unit in Section 28, in
14 light of the location of the well, is it your opinion
15 that that should be warranted in this case?

16 A. Well, my opinion is that it would probably
17 be better to drill in the north half and the south
18 half. You know, I think I've already addressed that
19 in discussing the trends of these sandstones.

20 I would like to make one more remark here,
21 if I might, about this area.

22 MR. KELLAHIN: I'm going to object to the
23 narrative answer to a question that's not asked.

24 EXAMINER STOGNER: I'm going to agree with
25 Mr. Kellahin, Mr. Cavin.

1 Q. (BY MR. CAVIN) Mr. Scott, do you have any
2 closing remarks that you'd like to make regarding the
3 Morrow in this area, the area of Section 28?

4 A. No, I have none regarding the Morrow.

5 MR. CAVIN: I have no further questions.

6 EXAMINER STOGNER: Thank you, Mr. Cavin.

7 Mr. Kellahin, do you have any?

8 MR. KELLAHIN: Just a few, Mr. Examiner.

9 EXAMINATION

10 BY MR. KELLAHIN:

11 Q. Mr. Scott, when were you asked to be an
12 expert in this case?

13 A. Oh, several days ago, I guess.

14 Q. How many hours would you estimate that you
15 devoted to studying what would be the appropriate way
16 to maximize development in Section 28?

17 A. I've looked at the seismic map that you all
18 furnished or Mitchell furnished to Strata, looked at
19 it and had one of my geologists who is responsible for
20 the Lea County District review the Morrow wells in the
21 area, and I discussed this with him sometime back, I
22 guess about the time we got your seismic map.

23 Q. Approximately when did you get that map?

24 A. Oh, let me think. When -- I believe that
25 was -- you brought that downstairs to our office the

1 day it was received up there.

2 MR. MURPHY: I think so.

3 THE WITNESS: I'm referring to this exhibit
4 right here.

5 MR. STOVALL: Mr. Scott, the question is
6 being asked of you, so just to the best of your
7 recollection; okay?

8 THE WITNESS: Oh, okay. Heck, three or
9 four weeks ago, I suppose.

10 MR. KELLAHIN: Let me see what was provided
11 to you, sir.

12 THE WITNESS: Okay.

13 Q. (BY MR. KELLAHIN) You were provided a
14 portion of Mr. Gawloski's structure map?

15 A. Yes.

16 Q. And it is an area that's approximately two
17 sections on each side north and south, east and west,
18 of Section 28?

19 A. It's four sections wide.

20 Q. Yes, sir. My question for you, sir, is,
21 once you were asked to be involved as an expert, how
22 many hours did you personally devote to studying what
23 to do with Section 28?

24 A. I spent all day yesterday and until about
25 eleven o'clock last night reviewing data. And this

1 doesn't -- okay, your question was after I was asked
2 to be a witness.

3 Q. Yes, sir.

4 A. That doesn't take into account the many
5 hours I've been involved in this area before.

6 Q. Let's look at Mr. Gawloski's structure map,
7 this area. Identify for me any of the Morrow wells in
8 which you were the exploration geologist that proposed
9 that Morrow well.

10 A. This is just a small segment of Lea
11 County. I have not been involved in any Morrow wells
12 in this area right here, to the best of my knowledge.
13 Let me think for just a minute, because this is -- let
14 me think. I have to go back about 25 years here in
15 this area, and I may well have been, but to tell you
16 the truth, I would have to go back and check my
17 facts.

18 I have generated Morrow prospects in this
19 area, put it this way -- that I have tried to get
20 clients to move on them, yes, over the years.

21 Q. My question was that as an exploration
22 geologist, there's none of these Morrow wells on that
23 display that you were the primary geologist that
24 proposed that well and got it drilled?

25 A. I don't believe so.

1 Q. Let me look at the structure map that
2 you've introduced as Exhibit No. 6.

3 A. Yes.

4 Q. If I can orient myself as to where you are,
5 I think your map ends, the north end of your map ends
6 --

7 A. It does.

8 Q. -- just about where Mr. Gawloski's south
9 end of his map stops?

10 A. That is correct, yes. I just wanted to
11 show that south of here but still in the general area,
12 what it looked like there.

13 Q. You have circled a portion of your display
14 with an orange elliptical shape?

15 A. Yes.

16 Q. Just north of that shape, Hat Mesa?

17 A. Yes.

18 Q. Does that not show you as a geologist that
19 there is a significant structural component to the
20 success of Morrow wells when they're drilled on
21 structure?

22 A. No, not at all because there's some wells
23 right on top of there that have nearly no sand at all.

24 Q. The best wells in that Hat Mesa are on the
25 best structural position in that pool, are they not,

1 sir?

2 A. No, I can't deny that. Where these sand
3 channels cross that big structure, yes, that is true
4 of some wells but not all. Where there are no sands,
5 your production is very poor, or poorly developed
6 sands, your production is poor.

7 Q. On your Exhibit No. 6 prepared in December
8 of '92, did you prepare a structure map that would
9 take into Section 28 just to the north?

10 A. We have other maps. This one particular
11 map is one that -- let me say, this is a work map, a
12 map that we keep up, we keep current, try to keep up
13 with the activity on, and we have other mapping
14 segments up there. Now, I don't --

15 Q. But you chose not to bring any of those and
16 utilize them today to utilize your points about
17 Section 28?

18 A. It was not up-to-date. No, I did not
19 choose to bring it because we do not keep up with
20 current Morrow activity in those two townships up
21 north.

22 Q. How about an isopach, did you prepare an
23 isopach that involves Section 28 so we can see what
24 your opinion is with regards to thickness?

25 A. I really didn't think that was necessary

1 because I have no objection to the values that Mr.
2 Gawloski puts on his map here.

3 Q. You didn't see his isopach until today, did
4 you?

5 A. No, that is correct but --

6 Q. How did you independently verify the
7 accuracy of that exhibit if you've just seen it?

8 A. I have to go by the reputation of Mr.
9 Gawloski.

10 Q. And it's pretty good, isn't it?

11 A. In my opinion, as I said when I started, I
12 have a high regard for him. I also said that the way
13 he contoured the map in here, his isopach map, is
14 subject to question.

15 Q. Mr. Gawloski's conclusion was that any well
16 drilled in Section 28 because of the inherent risk in
17 drilling Morrow gas wells was going to justify the
18 maximum risk factor penalty of 200 percent. Do you
19 concur in that opinion?

20 A. I would have to give that some serious
21 thought.

22 Q. Let's talk about some of your comments.
23 You said there was very little well control, very,
24 very sparse information, and you said it was high
25 risk.

1 A. If I used the word "high" risk, I'd like to
2 modify that. There is risk, certainly. There's
3 considerable risk there because you don't have any
4 close-by wells. You're projecting sand trends across
5 a map with very little control; so there has to be
6 risk. We're in a game of risk, obviously.

7 MR. KELLAHIN: No further questions, Mr.
8 Examiner.

9 EXAMINER STOGNER: Any other questions of
10 of this witness? He may be excused.

11 Do you have anything further, Mr. Cavin.

12 MR. CAVIN: Yeah, I'd like to ask -- first
13 of all, I'd like to ask Mr. Scott a question, if you
14 don't mind, Mr. Examiner.

15 EXAMINER STOGNER: Okay, Redirect?

16 MR. CAVIN: Yes

17 FURTHER EXAMINATION

18 BY MR. CAVIN:

19 Q. Mr. Scott, do you think your experiences in
20 the Morrow, in other areas of Lea County in the
21 Permian Basin, are valid when we're looking at Section
22 28 here?

23 A. I certainly do.

24 Q. So you don't see anything that's unique
25 about this area that would not allow you to pull on

1 your 30-some years' experience in the Permian Basin?

2 A. Certainly, experience helps, you know. I
3 would think yes, that I'm pretty competent. I'm not
4 sure I'm answering your question exactly.

5 MR. CAVIN: I have no further questions for
6 Mr. Scott.

7 I would like to ask -- these are the
8 notices of staking, and I was going to see, if there's
9 no objection, admitting those, or I can have Mr.
10 Murphy admit them, but they're the notices of staking
11 for the wells for the locations that Mr. Murphy has
12 described.

13 MR. STOVALL: Why don't you hand those to
14 Mr. Kellahin and let him look at them so he can refer
15 to them?

16 MR. CAVIN: We can make more copies.

17 THE WITNESS: Am I excused?

18 MR. KELLAHIN: No objection.

19 MR. STOVALL: Mr. Cavin, I'll return these
20 to you, please make copies, two for us and copies for
21 everybody else after the conclusion of the hearing.

22 EXAMINER STOGNER: Is there anything
23 further, Mr. Cavin?

24 MR. CAVIN: Do you mean a closing
25 statement?

1 EXAMINER STOGNER: It's up to you if you'd
2 like to make a closing.

3 MR. STOVALL: We'd like to hear the
4 testimony first.

5 MR. CAVIN: We have no further testimony,
6 Mr. Examiner.

7 EXAMINER STOGNER: I guess we're ready for
8 closing statements, if you care to go first, Mr.
9 Cavin.

10 MR. CAVIN: Mr. Examiner, what we have here
11 is a case where Mitchell wants everything its own
12 way. They want a west half proration unit. They want
13 the location they want. They want the operating
14 agreement they want. And they just want to sort of
15 shove it down Strata's throat.

16 Mitchell has stated that the location could
17 be improved by moving it to the north. Certainly if
18 that's the critical consideration, then maybe they
19 should be satisfied with one well in the north half.
20 We believe Mitchell should move the location to the
21 north and dedicate the well to the north half spacing
22 unit.

23 Strata has staked the south half location,
24 the legal location for the Morrow well. Strata
25 intends to seek participation for Mitchell and other

1 owners in the south half of Section 28 or,
2 alternatively, seek force pooling of these interests.

3 In summary, Mitchell's request for an
4 unorthodox well should be denied for the reasons
5 stated.

6 Mr. Examiner, I would also note, while I do
7 not represent any of the partners at this time, Strata
8 is concerned that its partners have not received
9 adequate notice required by both the State and Federal
10 Constitution. We believe these partners should have a
11 chance to address this body either in support or
12 opposition to Mitchell's application. And, frankly,
13 we don't know which they would do. We would note that
14 it's difficult to believe that Mitchell has made a
15 good faith, diligent effort to provide such notice.

16 Thank you, Mr. Examiner.

17 EXAMINER STOGNER: Thank you, Mr. Cavin.
18 Mr. Kellahin.

19 MR. KELLAHIN: Couple of quick points, Mr.
20 Examiner. The efforts that Mr. Smith has extended on
21 behalf of his company to reach a voluntary agreement
22 have been exhaustive. Despite his efforts, the
23 parties admit there is no agreement.

24 The issue of notification to these
25 undisclosed partners is a red herring in this case.

1 It would set an unusual and onerous precedent for the
2 examiner in a situation such as this to allow a party
3 that has required us to go through this exhaustive
4 effort of compulsory pooling to frustrate and escape
5 pooling by, at the last minute, a week before hearing,
6 now telling us for the first time the identity and
7 addresses of some 15 or 16 individuals. Our
8 obligations are to deal with the public record and
9 with representations made to us with regards to that
10 interest, and we have in good faith complied with that
11 obligation.

12 It would be an unusual precedent to allow a
13 party being pooled at the last minute, after all this
14 effort, to then come in and tell you they now have 10,
15 20, 1,500 people that they're assigning their interest
16 to. That's not how we need to do this.

17 I must tell you about Mr. Gawloski's
18 geology that Mr. Scott hasn't already confirmed for
19 us. He admits that Mr. Gawloski is well recognized
20 among his peers as being very good at what he does,
21 and part of what he does is not unusual for Section
22 28. It's a development methodology that Mitchell is
23 utilizing for the Morrow play. It's a high-risk play,
24 and he's looking for two locations in the section, and
25 that's the way you optimize the development of the

1 section. You take your best thickness and your best
2 structural position, and the only way to accomplish
3 that is to stand them up.

4 The notion that Strata is serious now about
5 this well location they have proposed today in Section
6 5 is made ridiculous when you look at the last
7 exhibits that Mr. Cavin submitted to you. On the very
8 face of those exhibits, every one of those three
9 wells, including this one, is specifically identified
10 to be a shallow, Delaware oil well. There is no
11 effort, no intent nor execution on their part to
12 propose a south half orientation. We think we've done
13 all we need to do and more, and we would like to have
14 our forced pooling order.

15 EXAMINER STOGNER: Thank you, Mr.
16 Kellahin.

17 Does anybody else have anything further in
18 Case 10,656? If not, this case will be taken under
19 advisement.

20 Take a five-minute recess.

21
22 I do hereby certify that the foregoing is
23 a complete record of the proceedings in
24 the Examiner hearing of Case No. 10656
25 heard by me on 2/2/93, 1993.


Examiner
Oil Conservation Division

1 CERTIFICATE OF REPORTER
2

3 STATE OF NEW MEXICO)

4) ss.

5 COUNTY OF SANTA FE)

6 I, Deborah O'Bine, Certified Shorthand
7 Reporter and Notary Public, HEREBY CERTIFY that I
8 caused my notes to be transcribed under my personal
9 supervision, and that the foregoing transcript is a
10 true and accurate record of the proceedings of said
11 hearing.

12 I FURTHER CERTIFY that I am not a relative
13 or employee of any of the parties or attorneys
14 involved in this matter and that I have no personal
15 interest in the final disposition of this matter.

16 WITNESS MY HAND AND SEAL, February 1, 1993.

17 *Deborah O'Bine*
18

19 DEBORAH O'BINE
20 CCR No. 63

