For article, "State Conservation Regulation and the Proposed R-199," see 6 Nat. Resources J. 223 (1966).

For comment on geothermal energy and water law, see 19 Nat. Resources J. 445 (1979).

**Am. Jur. 2d, A.L.R. and C.J.S. references.** — 38 Am. Jur. 2d Gas and Oil §§ 161, 164.

Rights and obligations, with respect to adjoining landowners, arising out of secondary recovery of gas, oil, and other fluid minerals, 19 A.L.R.4th 1182.

58 C.J.S. Mines and Minerals § 240.

## 70-2-17. Equitable allocation of allowable production; pooling; spacing.

A. The rules, regulations or orders of the division shall, so far as it is practicable to do so, afford to the owner of each property in a pool the opportunity to produce his just and equitable share of the oil or gas, or both, in the pool, being an amount, so far as can be practically determined, and so far as such can be practicably obtained without waste, substantially in the proportion that the quantity of the recoverable oil or gas, or both, under such property bears to the total recoverable oil or gas, or both, in the pool, and for this purpose to use his just and equitable share of the reservoir energy.

B. The division may establish a proration unit for each pool, such being the area that can be efficiently and economically drained and developed by one well, and in so doing the division shall consider the economic loss caused by the drilling of unnecessary wells, the protection of correlative rights, including those of royalty owners, the prevention of waste, the avoidance of the augmentation of risks arising from the drilling of an excessive number of wells, and the prevention of reduced recovery which might result from the drilling of too few wells.

C. When two or more separately owned tracts of land are embraced within a spacing or proration unit, or where there are owners of royalty interests or undivided interests in oil and gas minerals which are separately owned or any combination thereof, embraced within such spacing or proration unit, the owner or owners thereof may validly pool their interests and develop their lands as a unit. Where, however, such owner or owners have not agreed to pool their interests, and where one such separate owner, or owners, who has the right to drill has drilled or proposes to drill a well on said unit to a common source of supply, the division, to avoid the drilling of unnecessary wells or to protect correlative rights, or to prevent waste, shall pool all or any part of such lands or interests or both in the spacing or proration unit as a unit.

All orders effecting such pooling shall be made after notice and hearing, and shall be upon such terms and conditions as are just and reasonable and will afford to the owner or owners of each tract or interest in the unit the opportunity to recover or receive without unnecessary expense his just and fair share of the oil or gas, or both. Each order shall describe the lands included in the unit designated thereby, identify the pool or pools to which it applies and designate an operator for the unit. All operations for the pooled oil or gas, or both, which are conducted on any portion of the unit shall be deemed for all purposes to have been conducted upon each tract within the unit by the owner or owners of such tract. For the purpose of determining the portions of production owned by the persons owning interests in the pooled oil or gas, or both, such production shall be allocated to the respective tracts within the unit in the proportion that the number of surface acres included within each tract bears to the number of surface acres included in the entire unit. The portion of the production allocated to the owner or owners of each tract or interest included in a well spacing or proration unit formed by a pooling order shall, when produced, be considered as if produced from the separately owned tract or interest by a well drilled thereon. Such pooling order of the division shall make definite provision as to any owner, or owners, who elects not to pay his proportionate share in advance for the prorata reimbursement solely out of production to the parties advancing the costs of the development and operation, which shall be limited to the actual expenditures required for such purpose not in excess of what are reasonable, but which shall include a reasonable charge for supervision and may include a charge for the risk involved in the drilling of such well, which charge for risk shall not exceed two hundred percent of the nonconsenting working interest owner's or owners' prorata share of the cost of drilling and completing the well.

In the event of any dispute relative to such costs, the division shall determine the proper costs after due notice to interested parties and a hearing thereon. The division is specifically authorized to provide that the owner or owners drilling, or paying for the drilling, or for the operation of a well for the benefit of all shall be entitled to all production from such well which would be received by the owner, or owners, for whose benefit the well was drilled or operated, after payment of royalty as provided in the lease, if any, applicable to each tract or interest, and obligations payable out of production, until the owner or owners drilling or operating the well or both have been paid the amount due under the terms of the pooling order or order settling such dispute. No part of the production or proceeds accruing to any owner or owners of a separate interest in such unit shall be applied toward the payment of any cost properly chargeable to any other interest in said unit.

If the interest of any owner or owners of any unleased mineral interest is pooled by virtue of this act, seven-eighths of such interest shall be considered as a working interest and one-eighth shall be considered a royalty interest, and he shall in all events be paid one-eighth of all production from the unit and creditable to his interest.

D. Minimum allowable for some wells may be advisable from time to time, especially with respect to wells already drilled when this act takes effect, to the end that the production will repay reasonable lifting cost and thus prevent premature abandonment and resulting waste.

E. Whenever it appears that the owners in any pool have agreed upon a plan for the spacing of wells, or upon a plan or method of distribution of any allowable fixed by the division for the pool, or upon any other plan for the development or operation of such pool, which plan, in the judgment of the division, has the effect of preventing waste as prohibited by this act and is fair to the royalty owners in such pool, then such plan shall be adopted by the division with respect to such pool; however, the division, upon hearing and after notice, may subsequently modify any such plan to the extent necessary to prevent waste as prohibited by this act.

F. After the effective date of any rule, regulation or order fixing the allowable production, no person shall produce more than the allowable production applicable to him, his wells, leases or properties determined as in this act provided, and the allowable production shall be produced in accordance with the applicable rules, regulations or orders.

**History: Laws 1935, ch. 72, § 12; 1941 Comp., § 69-213½; Laws 1949, ch. 168, § 13; 1953, ch. 76, § 1; 1953 Comp., § 65-3-14; Laws 1961, ch. 65, § 1; 1973, ch. 250, § 1; 1977, ch. 255, § 51.**

**Meaning of "this act".** — The term "this act," referred to in this section, means Laws 1935, ch. 72, §§ 1 to 24, which appear as 70-2-2 to 70-2-4, 70-2-6 to 70-2-11, 70-2-15, 70-2-16, 70-2-21 to 70-2-25, 70-2-27 to 70-2-30, and 70-2-33 NMSA 1978.

**The terms "spacing unit" and "proration unit" are not synonymous** and the commission has power to fix spacing units without first creating proration units. Rutter & Wilbanks Corp. v. Oil Conservation Comm'n, 87 N.M. 286, 532 P.2d 582 (1975).

**Proration formula required to be based on recoverable gas.** — Lacking a finding that new gas proration formula is based on amounts of recoverable gas in pool and under tracts, insofar as these amounts can be practically determined and obtained without waste, a supposedly valid order in current use cannot be replaced. Such findings are necessary requisites to validity of the order, for it is upon them that the very power of the commission to act depends. Continental Oil Co. v. Oil Conservation Comm'n, 70 N.M. 310, 373 P.2d 809 (1962).

**Findings required before correlative rights ascertained.** — In order to protect correlative rights, it is incumbent upon commission to determine, "so far as it is practical to do so," certain foundationary matters, without which the correlative rights of various owners cannot be ascertained. Therefore, the commission, by "basic conclusions of fact" (or what might be termed "findings"), must determine, insofar as practicable: (1) amount of recoverable gas under each producer's tract; (2) the total amount of recoverable gas in pool; (3) proportion that (1) bears to (2); and (4) what portion of arrived at proportion can be recovered without waste. That the extent of the correlative rights must first be determined before commission can act to protect them is manifest. Continental Oil Co. v. Oil Conservation Comm'n, 70 N.M. 310, 373 P.2d 809 (1962).

In addition to making such findings the commission, "insofar as is practicable, shall prevent drainage between producing tracts in a pool which is not equalized by counter-drainage," under the provisions of 70-2-16 NMSA 1978. Continental Oil Co. v. Oil Conservation Comm'n, 70 N.M. 310, 373 P.2d 809 (1962).

Four basic findings required to adopt a production formula under this section can be made in language equivalent to that required in previous decision construing this section. El Paso Natural Gas Co. v. Oil Conservation Comm'n, 76 N.M. 268, 414 P.2d 496 (1966) (explaining Continental Oil Co. v. Oil Conservation Comm'n, 70 N.M. 310, 373 P.2d 809 (1962)).

Although subservient to prevention of waste and perhaps to practicalities of the situation, protection of correlative rights must depend upon commission's (now division's) findings as to extent and limitations of the right. This the commission is required to do



illegal oil or illegal gas or product thereof. Notice of the action in rem shall be given in conformity with the law or rule applicable to such proceeding. Any person or party in interest who may show himself to be adversely affected by any such seizure and sale shall have the right to intervene in the suit to protect his rights.

B. Whenever the pleading with respect to the forfeiture of illegal oil or illegal gas or product thereof shows ground for seizure and sale, and the pleading is verified or is supported by affidavit or affidavits, or by testimony under oath, the court shall order such commodity to be impounded or placed under the control, actual or constructive, of the court through an agent appointed by the court.

C. The judgment affecting the forfeiture shall provide that the commodity be seized, if not already under the control of the court, and that a sale be had in similar manner and with similar notice as provided by law or rule with respect to the sale of personal property under execution; provided, however, the court may order that the commodity be sold in specified lots or portions, and at specified intervals, instead of being sold at one time. Title to the amount sold shall pass as of the date of the seizure. The judgment shall provide for payment of the proceeds of the sale into the common school fund, after first deducting the costs in connection with the proceedings and the sale. The amount sold shall be treated as legal oil or legal gas or product thereof, as the case may be, in the hands of the purchaser, but the

proceeding provided in this section that the owner of such illegal oil or illegal gas or product thereof is liable, or in some proceeding authorized by Sections 70-2-1 through 70-2-34 NMSA 1978, such owner has already been held to be liable, for penalty for having produced the illegal oil or illegal gas, or for having purchased or acquired the illegal oil or illegal gas or product thereof. Whenever the division believes that illegal oil or illegal gas or product thereof is subject to seizure and sale, as provided herein, it shall, through the attorney general, bring a civil action in rem for that purpose in the district court of the county where the commodity is found, or the action may be maintained in connection with any suit or cross-action for injunction or for penalty relating to any prohibited transaction involving the illegal oil or illegal gas or product thereof. Notice of the action in rem shall be given in conformity with the law or rule applicable to such proceeding. Any person or party in interest who may show himself to be adversely affected by any such seizure and sale shall have the right to intervene in the suit to protect his rights.

B. Whenever the pleading with respect to the forfeiture of illegal oil or illegal gas or product thereof shows ground for seizure and sale, and the pleading is verified or is supported by affidavit or affidavits, or by testimony under oath, the court shall order such commodity to be impounded or placed under the control, actual or constructive, of the court through an agent appointed by the court.

C. The judgment affecting the forfeiture shall provide that the commodity be seized, if not already under the control of the court, and that a sale be had in similar manner and with similar notice as provided by law or rule with respect to the sale of personal property under execution; provided, however, the court may order that the commodity be sold in specified lots or portions, and at specified intervals, instead of being sold at one time. Title to the amount sold shall pass as of the date of the seizure. The judgment shall provide for payment of the proceeds of the sale into the common school fund, after first deducting the costs in connection with the proceedings and the sale. The amount sold shall be treated as legal oil or legal gas or product thereof, as the case may be, in the hands of the purchaser, but the purchaser and the commodity shall be subject to all applicable laws and rules, regulations and orders with respect to further sale or purchase or acquisition, and with respect to the transportation, refining, processing or handling in any other way, of the commodity purchased.

D. Nothing in this section shall deny or abridge any cause of action a royalty owner, or any lienholder, or any other claimant, may have, because of the forfeiture of the illegal oil or illegal gas or product thereof, against the person whose act resulted in such forfeiture.

**History: 1953 Comp., § 65-3-28, enacted by Laws 1978, ch. 58, § 1.**

**Cross references.** — For sale on execution, see 39-5-1 NMSA 1978.

**Repeals and reenactments.** — Laws 1978, ch. 58, § 1, repeals 65-3-28, 1953 Comp. (former 70-2-32 NMSA 1978), relating to procedure for seizure and sale of illegal oil or gas or products, and enacts the above section.

## 70-2-33. Definitions.

As used in the Oil and Gas Act [this article]:

A. "person" means:

(1) any individual, estate, trust, receiver, cooperative association, club, corporation, company, firm, partnership, joint venture, syndicate or other entity; or

(2) the United States or any agency or instrumentality thereof or the state or any political subdivision thereof;

B. "pool" means an underground reservoir containing a common accumulation of crude petroleum oil or natural gas or both. Each zone of a general structure, which zone is completely separate from any other zone in the structure, is covered by the word pool as used in the Oil and Gas Act. Pool is synonymous with "common source of supply" and with "common reservoir";

C. "field" means the general area which is underlaid or appears to be underlaid by at least one pool and also includes the underground reservoir or reservoirs containing the crude petroleum oil or natural gas or both. The words field and pool mean the same thing

when only one underground reservoir is involved; however, field, unlike pool, may relate to two or more pools;

D. "product" means any commodity or thing made or manufactured from crude petroleum oil or natural gas and all derivatives of crude petroleum oil or natural gas, including refined crude oil, crude tops, topped crude, processed crude petroleum, residue from crude petroleum, cracking stock, uncracked fuel oil, treated crude oil, fuel oil, residuum, gas oil, naphtha, distillate, gasoline, kerosene, benzine, wash oil, waste oil, lubricating oil and blends or mixtures of crude petroleum oil or natural gas or any derivative thereof;

E. "owner" means the person who has the right to drill into and to produce from any pool and to appropriate the production either for himself or for himself and another;

F. "producer" means the owner of a well capable of producing oil or natural gas or both in paying quantities;

G. "gas transportation facility" means a pipeline in operation serving gas wells for the transportation of natural gas or some other device or equipment in like operation whereby natural gas produced from gas wells connected therewith can be transported or used for consumption;

H. "correlative rights" means the opportunity afforded, so far as it is practicable to do so, to the owner of each property in a pool to produce without waste his just and equitable share of the oil or gas or both in the pool, being an amount, so far as can be practicably determined and so far as can be practicably obtained without waste, substantially in the proportion that the quantity of recoverable oil or gas or both under the property bears to the total recoverable oil or gas or both in the pool and, for such purpose, to use his just and equitable share of the reservoir energy;

I. "potash" means the naturally occurring bedded deposits of the salts of the element potassium; and

J. "casinghead gas" means any gas or vapor or both indigenous to an oil stratum and produced from such stratum with oil including any residue gas remaining after the processing of casinghead gas to remove its liquid components.

**History: Laws 1935, ch. 72, § 24; 1941 Comp., § 69-230; Laws 1949, ch. 168, § 26; 1953 Comp., § 65-3-29; Laws 1965, ch. 58, § 4; 1982, ch. 51, § 1; 1986, ch. 56, § 1.**

**Cross references.** — For definition of "waste," see 70-2-3 NMSA 1978. For definition of "carbon dioxide gas," see 70-2-34 NMSA 1978.

**The 1986 amendment,** effective May 21, 1986, added Subsection J and made stylistic changes throughout the section.

**Relationship between prevention of waste and protection of correlative rights.** — The prevention of waste is of paramount interest to the legislature and protection of correlative rights is interrelated and inseparable from it. The very definition of "correlative rights" emphasizes the term "without waste." However, protection of correlative rights is a necessary adjunct to the prevention of waste. Continental Oil Co. v. Oil Conservation Comm'n, 70 N.M. 310, 373 P.2d 809 (1962).

**Protection of correlative rights.** — Although subservient to prevention of waste and perhaps to the practicalities of the situation, protection of correlative rights must depend upon commission's findings as to extent and limitations of the right. This the commission is required to do under legislative mandate. Continental Oil Co. v. Oil Conservation Comm'n, 70 N.M. 310, 373 P.2d 809 (1962).

**Required findings by commission to protect correlative rights.** — In order to protect correlative rights, it is incumbent upon commission to determine, "so far as it is practical to do so," certain foundationary matters, without which correlative rights of various owners cannot be ascertained. Therefore, the commission, by "basic conclusions of fact" (or what might be termed "findings"), must determine, insofar as practicable: (1) amount of recoverable gas under each producer's tract; (2) total amount of recoverable gas in the pool; (3) proportion that (1) bears to (2); and (4) what portion of the arrived at proportion can be recovered without waste. That extent of the correlative rights must first be determined before commission can act to protect them is manifest. Continental Oil Co. v. Oil Conservation Comm'n, 70 N.M. 310, 373 P.2d 809 (1962).

**Commission's findings upheld.** — When commission exercises its duty to allow each interest owner in a pool his just and equitable share of the oil or gas underlying his property, mandate to determine the extent of those correlative rights is subject to the qualification as far as it is practicable to do so, and where commission established participation formula giving each owner in the unit a share in production in the same ratio as his acreage bore to the acreage of the whole units, the supreme court found that such a formula was reasonable and logical, if perhaps not the most complete or accurate method that may be used when more subsurface information becomes available. Rutter & Wilbanks Corp. v. Oil Conservation Comm'n, 87 N.M. 286, 532 P.2d 582 (1975).

**New proration formula to be based on recoverable gas.** — Lacking a finding that a new gas proration formula is based on the amounts of recoverable gas in the pool and under the tracts, insofar as these amounts can be practically determined and obtained without waste, a supposedly valid order in

**VIKING PETROLEUM, INC., Petitioner-Appellee,**
**vs.**
**OIL CONSERVATION COMMISSION OF THE STATE OF NEW MEXICO and HARVEY E. YATES COMPANY, Respondents-Appellants.**

No. 14632
SUPREME COURT OF NEW MEXICO
100 N.M. 451, 672 P.2d 280
November 17, 1983
Appeal from the District Court of Chaves County, William J. Schnedar, District Judge

**COUNSEL**

W. Perry Pearce, Santa Fe, New Mexico, for Appellant Oil Conservation Commission.
Losee, Carson & Dickerson, A. J. Losee, Artesia, New Mexico, for Appellant Harvey E. Yates Company.
Jones, Gallegos, Snead & Wertheim, Arturo L. Jaramillo, Santa Fe, New Mexico, for Appellee.

**JUDGES**

Federici, J., wrote the opinion. WE CONCUR: WILLIAM RIORDAN Justice, HARRY E. STOWERS, JR., Justice
**AUTHOR:** FEDERICI

**OPINION**

*{*452}* FEDERICI, Justice.

Viking Petroleum, Inc., petitioner-appellee (Viking), is the holder of an oil and gas leasehold estate on the E 1/2, NW 1/4, Section 18, Township 9 South, Range 27 East, NMPM, Chaves County, New Mexico. Harvey E. Yates Company, respondent-appellant (HEYCO), is the operator of the oil and gas leasehold estate on the W 1/2, NW 1/4 and SW 1/4 of Section 18, Township 9 South, Range 27 East, NMPM, Chaves County, New Mexico. Viking controls 25%, and HEYCO controls 75% of the underlying mineral interests. HEYCO applied for a permit to drill to the Ordovician formation. Viking agreed to participate in the drilling costs to the base of the shallower Abo formation, but declined to participate in the drilling of a well to the deeper Ordovician formation.

The Oil Conservation Commission of the State of New Mexico, respondent-appellant (Commission), denied Viking's request for partial participation. After a hearing, the Commission issued Order R-6873 (Order), which required all mineral interests pooled through the Ordovician formation to form a standard 320-acre gas spacing and prorationing unit to be dedicated to a well to be drilled at a standard location on the tract. The Order also provided that there should be withheld from any nonconsenting working interest owner's share of production his share of reasonable well costs plus 200% as a reasonable charge for the risk in drilling the well. The Order authorized HEYCO to withheld a pro rata share of all drilling costs as a means of collecting the penalty from Viking as a nonparticipating working interest owner. Viking's application for rehearing was automatically denied by failure of the Commission to act on the application within ten days.

Viking filed a Petition for Review of the Order and a Motion for Stay or Suspension of Order in the District Court of Chaves County. After a hearing on the motion, the district judge entered a decision suspending the Order. The district court's decision was conditional upon Viking's tender of $90,000 to HEYCO as Viking's estimated share of the cost of drilling and completing the well to the base of the Abo formation.

There was a dispute at the hearing as to whether Viking was willing and able to assume its share of the risk of the proposed well through the Abo by advancing to HEYCO Viking's share of those particular costs. Concerning the share of the risk and drilling costs for the well to formations **below** the Abo, Viking presented the concept of "partial participation," which ultimately became the central issue on appeal to the district court. Viking contended that as a correlative right owner it was entitled to participate partially in the subject well by paying in advance for its share of costs to the Abo. Concerning the drilling and completion costs below the Abo, Viking wished to proceed on a "carried basis." HEYCO, as operator, would be entitled to full reimbursement for Viking's share of the drilling and completion costs carried by HEYCO below the Abo. The payment was to be made out of Viking's share of the production from formation below the Abo until those costs were fully recouped by HEYCO.

Viking further contended that if a risk penalty under NMSA 1978, Section 70-2-17(C) would be appropriate at all in this case, it could **only** be applied to the drilling and completion costs being carried on behalf of Viking **below** the Abo formation. In other words, since HEYCO would not be required to advance any drilling or completion costs on behalf of Viking from the surface through the Abo formation, HEYCO would not be assuming any risk as to Viking's share of those costs and would not *{*453}* be entitled to risk compensation. With regard to the imposition of a risk penalty for the carried costs **below** the Abo, Viking argued that it was within the discretion of the Commission not to permit any risk penalty at all because the lack of production history in the deeper formation rendered the drilling venture below the Abo an extreme and unjustified risk for correlative right owners.

Following submission of briefs and without further hearing or oral arguments the district court held that Viking's application for rehearing preserved its right to object to the Commission's denial of partial participation. The district court also held that **as a matter of law** the Commission must provide partial participation by Viking unless there is substantial evidence in the record that such participation is clearly unreasonable. After reviewing the record of the Commission hearing, the district court concluded that the Order was not supported by substantial evidence, and that the Order was arbitrary, capricious, and contrary to law. We reverse.

We are limited to the same review of administrative actions as the district court. **Reynolds v. Wiggins,** 74 N.M. 670, 397 P.2d 469 (1964). This standard was applied to review of Commission order in **El Paso Natural Gas Company v. Oil Conservation Commission,** 76 N.M. 268, 414 P.2d 496 (1966).

Substantial evidence is such relevant evidence as a reasonable mind might accept as adequate to support a conclusion. **Rinker v. State Corporation Commission,** 84 N.M. 626, 506 P.2d 783

(1973). We must view the evidence and all reasonable inferences in the light most favorable to support the findings, and any evidence unfavorable will not be considered. **Martinez v. Sears, Roebuck and Co.**, 81 N.M. 371, 467 P.2d 37 (Ct. App.), **cert. denied,** 81 N.M. 425, 467 P.2d 997 (1970). Special weight will be given to the experience, technical competence and specialized knowledge of the Commission. **Rutter & Wilbanks Corporation v. Oil Conservation Commission,** 87 N.M. 286, 532 P.2d 582 (1975); **Grace v. Oil Conservation Commission,** 87 N.M. 205, 531 P.2d 939 (1975). Our review is limited to the evidence presented to the Commission, and the administrative findings by the Commission should be sufficiently extensive to show the basis of the order. **Continental Oil Company v. Oil Conservation Commission,** 70 N.M. 310, 373 P.2d 809 (1962). The findings must disclose the reasoning of the Commission in reaching its conclusion. **Fasken v. Oil Conservation Commission,** 87 N.M. 292, 532 P.2d 588 (1975).

**Pooling.**

Forced pooling of multiple zones with an election to participate in less than all zones is a question of first impression in New Mexico.

The Legislature, in an apparent desire to encourage the exploration and development of oil and gas in situations similar to the one before us, adopted NMSA 1978, Section 70-2-17(C), which provides in part as follows:

C. When two or more separately owned tracts of land are embraced within a spacing or proration unit, or where there are owners of royalty interests or undivided interests in oil and gas minerals which are separately owned or any combination thereof, embraced within such spacing or proration unit, the owner or owners thereof may validly pool their interest and develop their lands as a unit. **Where, however, such owner or owners have not agreed to pool their interests, and where one such separate owner, or owners, who has the right to drill has drilled or proposes to drill a well on said unit to a common source of supply, the division, to avoid the drilling of unnecessary wells or to protect correlative rights, or to prevent waste, shall pool all or any part of such lands or interests or both in the spacing or proration unit as a unit.** (Emphasis added.)

We now review the conclusion reached by the Commission determine whether the provisions of the Order are supported by substantial evidence. The first of the key provisions *{*454}* pooled the 320-acre tract from the surface to the Ordovician formation. The Commission found that to prevent waste, to protect correlative rights and to allow each interest owner to recover its fair share of gas, the mineral interests will be pooled to the lower formation. HEYCO's geologist testified that relying on an Abo well would not be economical because the risk involved was so great. Both sides presented expert testimony on quantities of oil and gas from formations below the Abo through the Ordovician which were commercially feasible to recover. The force pooling provision in the order is supported by a finding allowing interest owners to recover their fair share from the Ordovician formation. There is substantial evidence in the record to support the finding of the Commission that oil and gas reserves in the Ordovician were commercially feasible to produce. The Commission found that any nonconsenting working interest owner

should be allowed to pay his share of well costs out of production. In addition, the Commission found that a reasonable charge for the risk taken in drilling the well in 200% and any nonconsenting working interest owner who does not participate should be subject to this risk charge.

Based upon its findings the Commission: (1) pooled the 320-acre tract applied for from the surface to the Ordovician formation; (2) ordered HEYCO to proceed with due diligence to drill a test well to the Ordovician formation; (3) allowed any working interest owner who had not yet agreed to participate the option of paying his share of well costs, enabling such owner to avoid any risk charge; (4) authorized the operator to withhold the pro rata share of well costs plus a risk charge of 200% from production attributable to any nonparticipating working interest owner; (5) ordered that any amounts withheld from production should be withheld only from the working interest portion of production, not from the royalty interest portion.

**Commercial Production Below the Abo.**

In considering the application, the Commission heard evidence presented by HEYCO on the reasons for drilling this well to the Ordovician formation. It was the position of HEYCO's expert witness, Rodney O. Thompson (Thompson), that the most likely production from a well in the proposed location was from the geological formation which he referred to as the pre-Mississippian dolomite.

In discussing all of the prospective zones at the proposed location, Thompson stated that he believed that the pre-Mississippian dolomite and the Basal Penn sand were the most likely prospects. Based on the structure map which he had prepared from information derived from other wells in the area, Thompson testified that the location represented an excellent prospect in these two formations. The testimony and exhibits indicate that in the general area on the proposed location of the well there is commercial production potential from the pre-Mississippian dolomite.

In response to the expert testimony presented by HEYCO, Viking presented expert testimony from Morris Ettinger (Ettinger) which indicated that there was not sufficient evidence to justify the expenditure of funds for a deeper test. Ettinger testified that his review of the proposal indicated that a deeper test was unreasonable for a prudent joint interest owner and operator of a well in that area.

There is substantial evidence in the record to support the finding of the Commission that the most likely production would be from the pre-Mississippian dolomite, and that the well was economically feasible.

**Commercial Production From the Abo.**

An expert witness called by HEYCO testified that in his opinion the San Andres formation, which had a shallower depth than the Abo formation, was a likely secondary prospect, and that he expected to encounter some oil production from the San Andres. He expressed the opinion that although he expected to encounter gas production in the Abo formation at the proposed

location, he believed that there was a high risk of those reserves being noncommercial. In fact, this expert witness expressed his opinion that it would not be a *{*455}* justifiable economic risk to drill a well at the proposed location depending **only** upon Abo production.

Viking presented contradictory evidence through their expert witness, Ettinger, who gave his opinion that there was a good chance of commercial production from the Abo. He stated that Viking was willing to participate in a well drilled to the Abo formation at the proposed location.

The record contains substantial evidence to support the finding of the Commission that production from the Abo formation alone would not be to the advantage of the mineral interest and royalty owners, and that drilling to a deeper zone would prevent waste and protect correlative rights.

**Risk Involved.**

Witness for both parties at the proceeding before the Commission testified that there is a substantial risk involved in drilling a well to the Abo or the Ordovician, or in drilling any well. The finding that risk was involved and the finding of the proportionate share to be assumed by the owners is supported by substantial evidence.

**Reimbursement to HEYCO for Costs and Risk Charges.**

The application before the Commission not only requested that the designated mineral interests be pooled, but also that HEYCO be named operator and be entitled to recover the pro rata share of well costs and compensation for risk out of production from any nonconsenting working interest owner. Reimbursement of costs and risk charges is authorized by NMSA 1978, Section 70-2-17, which mandates that provision by made for payment from production of well costs for "any owner or owners who elects not to pay his proportionate share in advance." This section further allows the inclusion of a charge for the risk involved in the drilling of such well, which charge shall not exceed 200% of the nonconsenting working interest owner's or owners' pro rata share of the cost of drilling and completing the well. The granting or refusal to grant forced pooling of multiple zones with an election to participate in less than all zones, the amount of costs to be reimbursed to the operator, and the percentage risk charge to be assessed, if any, are determinations to be made by the Commission on a case-to-case basis and upon the particular facts in each case.

Based upon the record in this case, we find that there was substantial evidence to support the findings made and conclusions reached by the Commission, and that the Commission's Order is not arbitrary, capricious, or contrary to law.

The judgment of the district court is reversed. The order of the Commission is affirmed.

IT IS SO ORDERED.

WE CONCUR: WILLIAM RIORDAN Justice, HARRY E. STOWERS, JR., Justice

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

**IN THE MATTER OF THE HEARING CALLED BY THE OIL CONSERVATION DIVISION FOR THE PURPOSE OF CONSIDERING:**

**CASE NO. 12698**
**ORDER NO. R-11636-A**

**THE APPLICATION OF MEWBOURNE OIL COMPANY FOR COMPULSORY POOLING, EDDY COUNTY, NEW MEXICO.**

## ORDER OF THE OIL CONSERVATION COMMISSION

**BY THE COMMISSION:**

This case came on for an evidentiary hearing before the Oil Conservation Commission (hereinafter referred to as "the Commission") on October 12, 2001, at Santa Fe, New Mexico, and the Commission, having carefully considered the evidence presented, the pleadings and other materials submitted by the parties hereto, now, on this 6th day of November, 2001,

**FINDS,**

1. Notice has been given of the application and the hearing on this matter, and the Commission has jurisdiction of the parties and the subject matter herein.

2. The Applicant Mewbourne Oil Company (hereinafter referred to as "the Applicant") seeks an order pooling all uncommitted mineral interests from the base of the Yates formation to the base of the Morrow formation underlying the E/2 of Section 15, Township 21 South, Range 27 East, N.M.P.M, Eddy County, New Mexico, in the following manner:

> The E/2 to form standard 320-acre gas spacing and proration units for all formations or pools spaced on 320 acres within this vertical extent which presently include, but are not necessarily limited to, the Burton Flat-Morrow Gas Pool, Burton Flat-Strawn Gas Pool, Undesignated Cedar Hills-Upper Pennsylvanian Gas Pool, and Undesignated East Carlsbad-Wolfcamp Gas Pool.
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> The SE/4 to form standard 160-acre gas spacing and proration units for all formations or pools spaced on 160 acres within this vertical extent which presently include, but are not necessarily limited to, the Undesignated East Avalon-Bone Spring Gas Pool.

The NW/4 SE/4 to form standard 40-acre oil spacing and proration units for all formations or pools spaced on 40 acres within this vertical extent which presently include, but are not necessarily limited to, the Undesignated La Huerta-Delaware Pool, the Undesignated East Avalon-Bone Spring Pool, and the Undesignated East Carlsbad-Bone Spring Pool.

3. The Applicant seeks to dedicate these units to its proposed Esperanza "15" State Com. Well No. 1 (the "proposed well") to be drilled 2232 feet from the south line and 1980 feet from the east line, within the NW/4 SE/4 (Unit J) of Section 15.

4. The Application is opposed in-part by Harvey E. Yates Company and Jalapeno Corporation (hereinafter referred to as "Yates and Jalapeno") who filed an application for *de novo* review by this body.

5. Yates and Jalapeno do not oppose pooling from the base of the Wolfcamp formation to the base of the Morrow formation. However, Yates and Jalapeno oppose pooling formations above the Morrow on the grounds that pooling would prevent them from developing those formations and thereby impair correlative rights. Yates and Jalapeno argue that Mewbourne has no intention of actually producing from formations above the Morrow or, in the alternative, that Mewbourne's basis for development is to improve the economics of the proposed well which Yates and Jalapeno contend is an improper basis for compulsory pooling under the Oil and Gas Act. Yates and Jalapeno contend that pooling above the Morrow formation in this case would affect their correlative rights and effect a regulatory taking of their interests.

6. Mewbourne claims it is entitled to compulsory pooling of formations above the Morrow because it has the statutory right to do so, that it intends to develop all the formations pooled, that pooling above the Wolfcamp formation is essential for an economic well, that failure to compulsory pooling will result in the drilling of unnecessary wells, and that piecemeal pooling as proposed by Yates and Jalapeno would be wasteful of the Commission's and the parties' resources.

7. The evidence presented to this body establishes that the application for compulsory pooling from the base of the Yates formation to the base of the Morrow formation should be granted.

8. It is proper to order compulsory pooling of multiple formations so long as the evidence presented to the Commission justifies it. Viking Petroleum v. Oil Conservation Commission, 100 N.M. 451, 672 P.2d 280 (1983). The Viking case shows that the Commission may base, in part, a decision to pool multiple formations upon evidence that drilling of a well would not be economic if produced from a single formation. Thus, evidence presented by Mewbourne that its proposed well would not be economic if compulsory pooling were extended only to a single formation may be considered.

9. Mewbourne presented evidence that demonstrates that although the Morrow formation is its primary objective, it intends to produce from the Wolfcamp formation and possibly the Strawn formation, if either are capable of producing oil or natural gas. Mewbourne testified that it could multiple complete or downhole commingle the two formations if appropriate and feasible, and that it was interested in producing from any formation that will produce oil and natural gas.

10. Mewbourne presented evidence that established that reserves of crude oil and natural gas exist in the Morrow and the Wolfcamp formations and that data from nearby wells shows the proposed well to be a good prospect. Mewbourne presented evidence that drilling to the Morrow only, as Yates and Jalapeno request, would, under some assumptions, result in a well that produces less than it cost to drill. Mewbourne further presented evidence that including production from the Wolfcamp formation makes an economic well.

11. A well drilled to the Wolfcamp formation must of necessity pass through the producing formations which are at issue in this case, and production from these formations through a single wellbore avoids the possibility that an additional well or wells will be drilled. *See* NMSA 1978, § 70-2-17(C).

12. The evidence presented demonstrates that two or more separately-owned tracts are located within the units proposed for pooling, there are owners of royalty interests and/or undivided interests in oil and gas minerals in one or more tracts within the units which are separately owned.

13. The evidence presented demonstrates that the Applicant is an owner of an oil and gas working interest within the units. The Applicant has the right to drill and proposes to drill the proposed well to a common source of supply at the unorthodox location described above.

14. The evidence presented demonstrates that a considerable risk is entailed in drilling the well as many of the formations are partially depleted or previous attempts to develop certain formations have been unsuccessful.

15. The evidence presented demonstrates that interest owners in the proposed unit that have not agreed to pool their interests.

16. The evidence demonstrates that granting the application will avoid drilling of unnecessary wells, protect correlative rights, prevent waste and afford the owner of each interest in the units the opportunity to recover or receive without unnecessary expense a just and fair share of hydrocarbons.

17. The Applicant should be designated the operator of the proposed well and of the units described.

18. After pooling, each uncommitted working interest owner should be referred to as a "non-consenting working interest owner." An uncommitted working interest

owner is an owner of a working interest in the units, including every unleased mineral interest who is not a party to an operating agreement governing the units. Each non-consenting working interest owner should be afforded the opportunity to pay its share of estimated well costs to the operator in lieu of paying its share of reasonable well costs out of production.

19. Each non-consenting working interest owner who does not pay its share of estimated well costs should have withheld from production its share of reasonable well costs plus an additional 200% thereof as a reasonable charge for the risk involved in drilling the well.

20. Each non-consenting interest owner should be afforded the opportunity to object to the actual well costs, but actual well costs should be adopted as the reasonable well costs in the absence of such objection.

21. Following determination of reasonable well costs, any non-consenting working interest owner who has paid its share of estimated costs should pay to the operator any amount that reasonable well costs exceed estimated well costs and should receive from the operator any amount that paid estimated well costs exceed reasonable well costs.

22. The evidence shows that reasonable charges for supervision (combined fixed rates) should be fixed at $5,400 per month while drilling and $540 per month while producing, provided that these rates should be adjusted annually pursuant to Section III.1.A.3. of the COPAS form titled "*Accounting Procedure-Joint Operations.*" The operator should be authorized to withhold from production the proportionate share of both the supervision charges and the actual expenditures required for operating the well, not in excess of what are reasonable, attributable to each non-consenting working interest.

23. Except as noted in Findings ____ and ____ above, all proceeds from production from the well that are not disbursed for any reason should be placed in escrow to be paid to the true owner thereof upon demand and proof of ownership.

24. If the operator fails to commence drilling the well to which the units are dedicated on or before January 1, 2002, this order should become of no effect.

25. The operator should notify the Oil Conservation Commission in writing of the subsequent voluntary agreement of all parties subject to the compulsory pooling provisions of this order.

26. The location of the proposed well is unorthodox in the Undesignated East Avalone-Bone Spring Gas Pool and the Undesignated East Carlsbad-Wolfcamp Gas Pool.

27. Approval of the unorthodox well location in the Burton Flat-Morrow Gas Pool was obtained in Division Order NSL-4606, but approval of the unorthodox well

location in the Undesignated East Avalone-Bone Spring Gas Pool and the Undesignated East Carlsbad-Wolfcamp Gas Pool had not been sought as of the date of the hearing in this matter.

28. Because the Applicant proposes to drill at an unorthodox location and because the Applicant has only obtained approval of the location in the Burton Flat-Morrow Gas Pool, this Order should be conditioned upon subsequent approval of the unorthodox location in the Undesignated East Avalone-Bone Spring Gas Pool and the Undesignated East Carlsbad-Wolfcamp Gas Pool pursuant to the applicable Rules and Regulations.

29. No basis exists for the claims of Yates and Jalapeno that compulsory pooling under the circumstances described herein constitutes a regulatory taking.

**IT IS THEREFORE ORDERED, AS FOLLOWS:**

1. All uncommitted mineral interests from the base of the Yates formation to the base of the Morrow formation underlying the E/2 of Section 15, Township 21 South, Range 27 East, N.M.P.M., Eddy County, New Mexico, are hereby pooled, as follows:

> The E/2 to form standard 320-acre gas spacing and proration units for all formations or pools spaced on 320 acres within this vertical extent which presently include, but are not necessarily limited to, the Burton Flat-Morrow Gas Pool, Burton Flat-Strawn Gas Pool, Undesignated Cedar Hills-Upper Pennsylvanian Gas Pool, and Undesignated East Carlsbad-Wolfcamp Gas Pool.
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> The SE/4 to form standard 160-acre gas spacing and proration units for all formations or pools spaced on 160 acres within this vertical extent which presently include, but are not necessarily limited to, the Undesignated East Avalon-Bone Spring Gas Pool.
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> The NW/4 SE/4 to form standard 40-acre oil spacing and proration units for all formations or pools spaced on 40 acres within this vertical extent which presently include, but are not necessarily limited to, the Undesignated La Huerta-Delaware Pool, the Undesignated East Avalon-Bone Spring Pool, and the Undesignated East Carlsbad-Bone Spring Pool.

2. The units referred to in the previous paragraph shall be dedicated to Applicant's Esperanza "15" State Com. Well No. 1 to be drilled at a location 2232 feet from the south line and 1980 feet from the east line, within the NW/4 SE/4 (Unit J) of Section 15.

3. The Applicant shall be designated the operator of the well referred to in the previous paragraph and the units created in decretal paragraph 1.

4. The Applicant (hereinafter referred to as "the Operator") shall commence drilling the proposed well on or before January 1, 2002, and shall thereafter continue drilling the well with due diligence to test the Morrow formation.

5. In the event the Operator does not commence drilling the proposed well on or before January 1, 2002, decretal paragraphs 1, 2 and 3 shall be of no effect unless the operator obtains an extension from the Director of the Oil Conservation Division for good cause shown.

6. Should the proposed well not be drilled to completion or is abandoned within 120 days after commencement thereof, the Operator shall appear before the Director of the Oil Conservation Division and show cause why Ordering Paragraphs 1, 2 and 3 should not be rescinded.

7. Uncommitted working interest owners shall be referred to henceforth as "non-consenting working interest owners." Upon the effective date of this order, the Operator shall furnish the Oil Conservation Division and each known non-consenting working interest owner in the units an itemized schedule of estimated well costs.

8. Within thirty (30) days from the date the schedule of estimated well costs is furnished, any non-consenting working interest owner shall have the right to pay its share of estimated well costs to the operator in lieu of paying its share of reasonable well costs out of production as hereinafter provided, and any such owner who pays its share of estimated well costs as provided above shall remain liable for operating costs but shall not be liable for risk charges.

9. The Operator shall also furnish the Oil Conservation Division and each known non-consenting working interest owner an itemized schedule of actual well costs within ninety (90) days following completion of the well. If no objection to the actual well costs is received by the Oil Conservation Division, and the Division has not objected within 45 days following receipt of the schedule, the actual well costs shall be deemed to be the reasonable well costs; provided, however, that if there is an objection to actual well costs within the 45-day period, the Oil Conservation Division will determine reasonable well costs after public notice and hearing.

10. Within 60 days following determination of reasonable well costs, any non-consenting working interest owner who has paid its share of estimated costs in advance as provided above shall pay to the operator its share of the amount that reasonable well costs exceed estimated well costs and shall receive from the Operator its share of the amount that estimated well costs exceed reasonable well costs.

11. The Operator is hereby authorized to withhold the following costs and charges from production:

(a) the proportionate share of reasonable well costs attributable to each non-consenting working interest owner who has not paid its share of estimated well costs within 30 days from the date the schedule of estimated well costs is furnished; and

(b) as a charge for the risk involved in drilling the well, 200% of the above costs.

12. The Operator shall distribute the costs and charges withheld from production, proportionately, to the parties who advanced the well costs.

13. Reasonable charges for supervision (combined fixed rates) are hereby fixed at $5,400 per month while drilling and $540 per month while producing, provided that these rates shall be adjusted annually pursuant to Section III.1.A.3. of the COPAS form titled "*Accounting Procedure-Joint Operations.*" The Operator is authorized to withhold from production the proportionate share of both the supervision charges and the actual expenditures required for operating the well, not in excess of what are reasonable, attributable to each non-consenting working interest.

14. Except as provided in decretal paragraphs ____ and _____ above, all proceeds from production from the well that are not disbursed for any reason shall be placed in escrow in Eddy County, New Mexico, to be paid to the true owner thereof upon demand and proof of ownership. The Operator shall notify the Oil Conservation Division of the name and address of the escrow agent within 30 days from the date of first deposit with the escrow agent.

15. Any unleased mineral interest shall be considered a seven-eighths (7/8) working interest and a one-eighth (1/8) royalty interest for the purpose of allocating costs and charges under this Order. Any well costs or charges that are to be paid out of production shall be withheld only from the working interests' share of production, and no costs or charges shall be withheld from production attributable to royalty interests.

16. Should all the parties to this Order reach voluntary agreement subsequent to its entry, this Order shall thereafter be of no further effect. The Operator shall notify the Commission in writing of the subsequent voluntary agreement of all parties subject to the compulsory pooling provisions of this order.

17. This Order is conditioned upon subsequent approval of the unorthodox location in the Undesignated East Avalone-Bone Spring Gas Pool and the Undesignated East Carlsbad-Wolfcamp Gas Pool pursuant to the applicable Rules and Regulations.

18. Jurisdiction is retained for the entry of such further orders as the Commission deems necessary.

**DONE** at Santa Fe, New Mexico, on the day and year hereinabove designated.

**STATE OF NEW MEXICO**
**OIL CONSERVATION COMMISSION**

**By**_____
**LORI WROTENBERY, Director**

**S E A L**