Correspondence

Renovo

Case No. 12635

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AND
CAMPBELL & CARR
ATTORNEYS AT LAW

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November 14, 2001

Stephen C. Ross
Assistant General Counsel
New Mexico Energy, Minerals &
Natural Resources Department
1220 South St. Francis Drive
Santa Fe, New Mexico 87505

Re: Case No. 12635, Application of McElvain Oil & Gas Properties, *de novo*
Case No. 12705, Application of D. J. Simmons, Inc.

Dear Mr. Ross:

Pursuant to your letter dated October 30, 2001 for the above-referenced matters, please be advised that I have no objection to the proposed tender of Exhibit 34.

Please feel free to give me a call should you have any questions.

Very truly yours,

Michael H. Feldewert

MHF/js
cc: Florene Davidson, Commission Secretary
J. Scott Hall

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

IN THE MATTER OF THE APPLICATION OF McELVAIN OIL & GAS PROPERTIES, INC. FOR COMPULSORY POOLING RIO ARRIBA COUNTY, NEW MEXICO **CASE NO. 12635, *de novo***

IN THE MATTER OF THE APPLICATION OF D. J. SIMMONS, INC. FOR COMPULSORY POOLING, RIO ARRIBA COUNTY, NEW MEXICO **CASE NO. 12705**

McELVAIN'S POST-HEARING STATEMENT

This Post-hearing Statement is submitted by McElvain Oil & Gas Properties, Inc. pursuant to the request of the Commissioners at the November 17, 2001, hearing.

At the May 17, 2001, Examiner hearing, D.J. Simmons presented the same arguments and evidence it has presented to the Commission. After considering this evidence, the Division's Examiner concluded "the cumulative evidence presented in this matter serves to support McElvain's position..."[1] D.J. Simmons has presented nothing to the Commission to overturn that conclusion.

I. No Competing Mesaverde Well Proposal Is Before the Commission.

Compulsory pooling is limited to situations where an interest owner with a right to drill "has drilled or proposes to drill a well on said unit to a common source of supply..." NMSA 1978, Section 70-2-17.C. D.J. Simmons has not met the statutory preconditions for invoking the Division's compulsory pooling power. It has not proposed to drill and complete a well in the

[1] *See* Division Order R-11663 at p. 2, para. 10.

Mesaverde formation in Section 25.[2] Instead, D.J. Simmons merely plans to drill a Gallup Dakota oil well in the NE/4 of Section 25 (which is spaced on 160-acres owned entirely by D.J. Simmons) with the "possibility" of a Mesaverde completion in this wellbore at some unknown time in the future. As a result, the only proposal before the Commission to drill a well to source of supply common to all of the interest owners in Section 25, and the only proposal that allows Dugan and Forcenergy to produce their just and equitable share of Mesaverde reserves under their property, is McElvain's re-entry project approved by Division Order R-11663 and Administrative Order NSL-4538.

II. Division Order R-11663 Protects Correlative Rights And Affords the Interest Owners In The SE/4 of Section 25 The Opportunity To Recover Without Unnecessary Expense Their Just And Fair Share of Mesaverde Reserves.

When the statutory preconditions are met, the Division "shall" pool properties to "avoid the drilling of unnecessary wells or to protect correlative rights or to prevent waste." *See* NMSA 1978, Section 70-2-17.C. The Division is further compelled to enter pooling orders that are "just and reasonable and will afford to the owners 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 oil or gas, or both." *Id.* McElvain has met all of the statutory preconditions for pooling, and Division Order R-11663 protects the correlative rights of the interest owners in the SE/4 by providing them the opportunity to recover their fair share of Mesaverde reserves without unnecessary expense.

The evidence establishes that D.J. Simmons intends to drill Gallup Dakota oil wells in both

---

[2] *See, e.g.*, McElvain exhibits 11-13, the testimony of Mona Binion, and the cross-examination of D.J. Simmons' witnesses (in particular Ed Dunn and Tom Mullins).

the NE/4 and SE/4 of Section 25. Nothing in Order R-11663 prevents that development plan. Indeed, D.J. Simmons' proposed oil wells are eligible for re-completion, if necessary, as in-fill Mesaverde gas wells for N/2 and S/2 spacing units. D.J. Simmons cries of "waste" are nothing more than a desire to "keep in its back pocket" the ability to operate at some unknown time a Mesaverde gas well. That desire does not constitute "waste" (*see* NMSA 1978, Section 70-2-3) and compulsory pooling authority does not exist to keep in an operator's "back pocket" a formation the interest owners in Section 25 wish to develop now.

D.J. Simmons also fails to establish that Division Order R-11663 is contrary to the known geology and prevailing drainage patterns in the area. D.J. Simmons presented no direct evidence of fracturing in the Mesaverde formation or north-south drainage trends. Indeed, the only direct evidence presented by the parties shows that the sand orientations in Section 25 support east-west drainage trends.[3]

D.J. Simmons' main objection to Order R-11663 is that it spreads the risk of a Mesaverde test well among the parties who will share in the production from that well. However, the testimony of Mona Binion and Ed Dunn establish that this sharing of benefits and risk is a common consideration operators take into account in developing properties. Moreover, McElvain not only owns Mesaverde rights in the W/2 of Section 25, but also the SE/4. The correlative rights of the interest owners in the SE/4 are protected, and they are afforded an opportunity to share in the recovery of Mesaverde reserves without unnecessary expense, by

[3]*See* McElvain Exhibits 16 and 17; D.J. Simmons Exhibit 25.

participating in the re-entry of a well in the SW/4 under the terms of Division Order R-11663.

III. McElvain Is The Only Party That Made Diligent and Good Faith Efforts to Reach a Voluntary Agreement With the Interest Owners In Section 25.

D.J. Simmons' has observed: "The Division and the Commission require operators to show that they have made a 'diligent' and 'good faith' effort to negotiate a voluntary agreement before a compulsory pooling application may be filed."[4] Looking at the same facts as the Commission, the Division's Examiner concluded D.J. Simmons was not diligent in this matter. *See* Tr. of May 17th Hearing at p. 129, line 20. Ed Dunn further testified that D.J. Simmons never attempted to reach an agreement with Dugan. *See also* D.J. Simmons Exhibit 3.

With respect to McElvain, D.J. Simmons' arguments consist of attempting to establish who initiated the numerous discussions and exchange of information that took place between the parties since McElvain proposed its re-completion project in November of 2000. *See, e.g,* D.J. Simmons Exhibit 3. However, D.J. Simmons' landman (Ed Dunn) candidly admitted that by the end of November of 2000, McElvain had provided all the documentation D.J. Simmons considered necessary to meet the "good faith" obligation, and that McElvain had indeed made good faith efforts to reach an agreement with D.J. Simmons.[5]

---

[4] D.J. Simmons, Inc.'s Hearing Memorandum at p. 7.

[5] Indeed, McElvain accepted farmout terms for D.J. Simmons' Mesaverde interests in the SE/4 of Section 25. The only matter holding up the settlement is D.J. Simmons' insistence that McElvain support the creation of two non-standard 160-acre Mesaverde spacing units in the N/2 of Section 25. *See* McElvain's Exhibit B-1 (11/1/01 McElvain settlement letter to John A. Byrom). At the May 17th hearing, Examiner Stogner noted the absence of precedent for non-standard spacing units for the Mesaverde formation. *See* Transcript of May 17th hearing at p. 123-126. Certainly it does not constitute bad faith for McElvain to refuse to support a proposal that is contrary to the Division's rules and regulations.

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Respectfully submitted,

Michael H. Feldewert
Attorney for McElvain Oil & Gas Properties, Inc.

CERTIFICATE OF SERVICE

I certify that on November 9, 2001 I served a copy of the foregoing document to the following by

☒ U.S. Mail, postage prepaid
☐ Hand Delivery
☐ Fax

J. Scott Hall, Esq.
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Santa Fe, NM 87504-1986

Michael H. Feldewert

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

IN THE MATTER OF THE APPLICATION OF
McELVAIN OIL & GAS PROPERTIES, INC.
FOR COMPULSORY POOLING
RIO ARRIBA COUNTY, NEW MEXICO — CASE NO. 12635, *de novo*

IN THE MATTER OF THE APPLICATION OF
D. J. SIMMONS, INC. FOR COMPULSORY POOLING,
RIO ARRIBA COUNTY, NEW MEXICO — CASE NO. 12705

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Respectfully submitted,

Michael H. Feldewert
Attorney for McElvain Oil & Gas Properties, Inc.

CERTIFICATE OF SERVICE

I certify that on November 9, 2001 I served a copy of the foregoing document to the following by

☒ U.S. Mail, postage prepaid
☐ Hand Delivery
☐ Fax

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Michael H. Feldewert

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PLEASE REPLY TO SANTA FE

* NEW MEXICO BOARD OF SPECIALIZATION RECOGNIZED SPECIALIST IN NATURAL RESOURCES - OIL & GAS LAW
** NEW MEXICO BOARD OF SPECIALIZATION RECOGNIZED SPECIALIST IN REAL ESTATE LAW

November 7, 2001

Lori Wrotenbery, Director
New Mexico Oil Conservation Division
1220 St. Francis Drive
Santa Fe, New Mexico 87505

Re: NMOCC Case No. 12635 *de novo*; Application of McElvain Oil and Gas Properties, Inc. for Compulsory Pooling, Rio Arriba County, New Mexico
Consolidated with
NMOCC Case No. 12705; Application of D. J. Simmons, Inc. for Compulsory Pooling, Rio Arriba County, New Mexico

Dear Ms. Wrotenbery:

At the November 6, 2001 hearing on the above consolidated cases, I neglected to tender into evidence our Rule 1207 Notice Affidavit. A copy of the Notice Affidavit, marked as D. J. Simmons Exhibit No. 34 is enclosed. The original and one copy of the Affidavit were left with Mr. Brenner immediately following the hearing.

On behalf of D. J. Simmons, Inc., I request that our Notice Affidavit be made a part of the record in the above consolidated matters.

Thank you.

Very truly yours,

J. Scott Hall

JSH/kam
enclosures a/s

Cc: Mike Feldewert, Esq. W/enclos

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

IN THE MATTER OF THE APPLICATION OF
McELVAIN OIL & GAS PROPERTIES, INC.
FOR COMPULSORY POOLING,
RIO ARRIBA COUNTY, NEW MEXICO — CASE NO. 12,635 *De Novo*

Consolidated with:

IN THE MATTER OF THE APPLICATION OF
D. J. SIMMONS, INC. FOR COMPULSORY POOLING,
RIO ARRIBA COUNTY, NEW MEXICO — CASE NO. 12705

AFFIDAVIT

STATE OF NEW MEXICO)
) ss.
COUNTY OF SANTA FE)

J. SCOTT HALL, attorney in fact and authorized representative of D.J. Simmons, Inc., the Applicant herein, being first duly sworn, upon oath, states that the notice provisions of Rule 1207 of the New Mexico Oil Conservation Division have been complied with, that Applicant has caused to be conducted a good faith diligent effort to find the correct addresses of all interested persons entitled to receive notice, as shown by Exhibit "A" attached hereto, and that pursuant to Rule 1207, notice has been given at the correct addresses provided by such rule.

J. SCOTT HALL

NMOCC Case No. 12635
and Case No. 12705
November 6, 2001
D.J. Simmons, Inc. Exhibit No. 34

SUBCRIBED AND SWORN to before me this 5th day of November, 2001.

Rachael K. Martin
Notary Public

My Commission Expires:

11/14/01

MILLER, STRATVERT & TORGERSON, P.A.

LAW OFFICES

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PLEASE REPLY TO SANTA FE

* NEW MEXICO BOARD OF SPECIALIZATION RECOGNIZED SPECIALIST IN NATURAL RESOURCES - OIL & GAS LAW
** NEW MEXICO BOARD OF SPECIALIZATION RECOGNIZED SPECIALIST IN REAL ESTATE LAW

July 13, 2001

CERTIFIED MAIL
RETURN RECEIPT REQUIRED

T. H. McElvain Oil & Gas Limited Partnership
1050 17th Street, Suite 1800
Denver, Colorado 80265

Re: NMOCD Case No. _____; Application of D.J. Simmons, Inc. for Compulsory Pooling, Rio Arriba County, New Mexico (E/2 Sec. 25, T-25-N, R-3-W, NMPM; Bishop Federal 25 No. 1 well)

Dear Sir or Madam:

Please be advised that D. J. Simmons, Inc. has filed an Application with the New Mexico Oil Conservation Division (NMOCD) seeking the issuance of an order pooling all mineral interests from the surface to the base of the Mesaverde formation in the E/2 of Section 25, Township 25 North, Range 3 West, NMPM, for all formations and or pools developed on 320-acre spacing, including, but not necessarily limited to, the Mesaverde formation, Blanco-Mesaverde Gas Pool. Said units are to be dedicated to Applicant's Bishop Federal 25-1 well to be drilled at a standard location in the NE/4 of said Section 25 to a depth sufficient to test all formations in the pooled intervals, as well as the Chacra formation and the Gallup-Dakota formation, West Lindrith Gallup-Dakota Oil pool. Also to be considered will be the cost of drilling and completing said well and the allocation of the cost thereof, as well as actual operating costs and charges for supervision, designation of Applicant as operator and a charge for the risk involved in drilling said well.

EXHIBIT
A

D. J. Simmon's Application is set for hearing before a Division Examiner at 8:15 a.m. on Thursday, August 9, 2001 at the NMOCD's offices located at 1220 South St. Francis Drive in Santa Fe, New Mexico. You have the right to appear at the hearing and participate in the case. Failure to appear at the hearing will preclude you from contesting this matter at a later date.

Very truly yours,

MILLER, STRATVERT & TORGERSON, P.A.

J. Scott Hall
ATTORNEY FOR D. J. SIMMONS, INC.

JSH/ao
Enclosure(s) – as stated

2187/Notice ltr.doc

SENDER: COMPLETE THIS SECTION

- Complete items 1, 2, and 3. Also complete item 4 if Restricted Delivery is desired.
- Print your name and address on the reverse so that we can return the card to you.
- Attach this card to the back of the mailpiece, or on the front if space permits.

1. Article Addressed to:

T.H. McElvain Oil &
Gas Limited Partnership
1050 17th Street, Suite 1800
Denver, CO 80265

COMPLETE THIS SECTION ON DELIVERY

A. Received by *(Please Print Clearly)* DENISE DIANA — B. Date of Delivery 7/17/01

C. Signature — X [signature] — ☐ Agent ☐ Addressee

D. Is delivery address different from item 1? ☐ Yes
If YES, enter delivery address below: ☐ No

3. Service Type
☒ Certified Mail ☐ Express Mail
☐ Registered ☒ Return Receipt for Merchandise
☐ Insured Mail ☐ C.O.D.

4. Restricted Delivery? *(Extra Fee)* ☐ Yes

2. Article Number *(Copy from service label)* 7000 0600 0025 0308 6867

PS Form 3811, July 1999 — Domestic Return Receipt — 102595-00-M-0952

MILLER, STRATVERT & TORGERSON, P.A.
LAW OFFICES

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July 13, 2001

CERTIFIED MAIL
RETURN RECEIPT REQUIRED

Forcenergy Onshore, Inc.
c/o Forest Oil Corporation
1600 Broadway, Suite 2200
Denver, Colorado 80202

Re: NMOCD Case No. _____; Application of D.J. Simmons, Inc. for Compulsory Pooling, Rio Arriba County, New Mexico (E/2 Sec. 25, T-25-N, R-3-W, NMPM; Bishop Federal 25 No. 1 well)

Dear Sir or Madam:

Please be advised that D. J. Simmons, Inc. has filed an Application with the New Mexico Oil Conservation Division (NMOCD) seeking the issuance of an order pooling all mineral interests from the surface to the base of the Mesaverde formation in the E/2 of Section 25, Township 25 North, Range 3 West, NMPM, for all formations and or pools developed on 320-acre spacing, including, but not necessarily limited to, the Mesaverde formation, Blanco-Mesaverde Gas Pool. Said units are to be dedicated to Applicant's Bishop Federal 25-1 well to be drilled at a standard location in the NE/4 of said Section 25 to a depth sufficient to test all formations in the pooled intervals, as well as the Chacra formation and the Gallup-Dakota formation, West Lindrith Gallup-Dakota Oil pool. Also to be considered will be the cost of drilling and completing said well and the allocation of the cost thereof, as well as actual operating costs and charges for supervision, designation of Applicant as operator and a charge for the risk involved in drilling said well.

D. J. Simmon's Application is set for hearing before a Division Examiner at 8:15 a.m. on Thursday, August 9, 2001 at the NMOCD's offices located at 1220 South St. Francis Drive in Santa Fe, New Mexico. You have the right to appear at the hearing and participate in the case. Failure to appear at the hearing will preclude you from contesting this matter at a later date.

Very truly yours,

MILLER, STRATVERT & TORGERSON, P.A.

J. Scott Hall
ATTORNEY FOR D. J. SIMMONS, INC.

JSH/ao
Enclosure(s) – as stated

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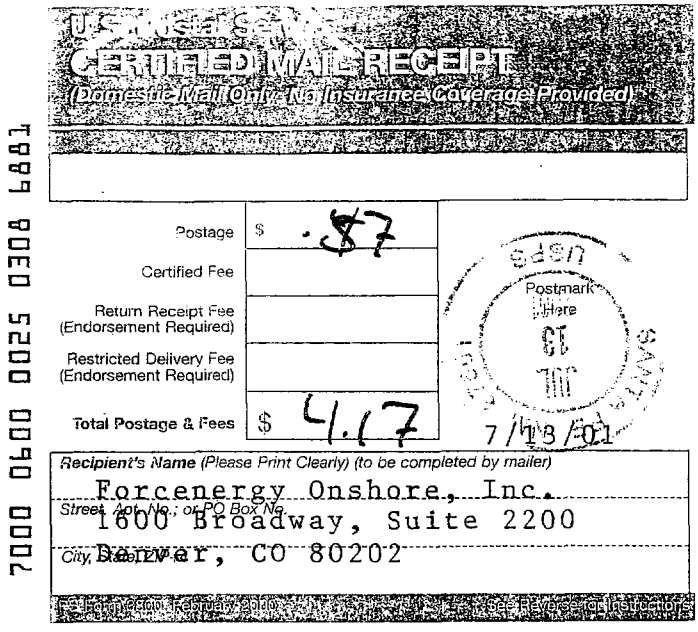

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** NEW MEXICO BOARD OF SPECIALIZATION RECOGNIZED SPECIALIST IN REAL ESTATE LAW

July 13, 2001

CERTIFIED MAIL
RETURN RECEIPT REQUIRED

Dugan Production Corporation
709 East Murray Drive
Farmington, New Mexico 87499

Re: NMOCD Case No. _____; Application of D.J. Simmons, Inc. for Compulsory Pooling, Rio Arriba County, New Mexico (E/2 Sec. 25, T-25-N, R-3-W, NMPM; Bishop Federal 25 No. 1 well)

Dear Sir or Madam:

Please be advised that D. J. Simmons, Inc. has filed an Application with the New Mexico Oil Conservation Division (NMOCD) seeking the issuance of an order pooling all mineral interests from the surface to the base of the Mesaverde formation in the E/2 of Section 25, Township 25 North, Range 3 West, NMPM, for all formations and or pools developed on 320-acre spacing, including, but not necessarily limited to, the Mesaverde formation, Blanco-Mesaverde Gas Pool. Said units are to be dedicated to Applicant's Bishop Federal 25-1 well to be drilled at a standard location in the NE/4 of said Section 25 to a depth sufficient to test all formations in the pooled intervals, as well as the Chacra formation and the Gallup-Dakota formation, West Lindrith Gallup-Dakota Oil pool. Also to be considered will be the cost of drilling and completing said well and the allocation of the cost thereof, as well as actual operating costs and charges for supervision, designation of Applicant as operator and a charge for the risk involved in drilling said well.

D. J. Simmon's Application is set for hearing before a Division Examiner at 8:15 a.m. on Thursday, August 9, 2001 at the NMOCD's offices located at 1220 South St. Francis Drive in Santa Fe, New Mexico. You have the right to appear at the hearing and participate in the case. Failure to appear at the hearing will preclude you from contesting this matter at a later date.

Very truly yours,

MILLER, STRATVERT & TORGERSON, P.A.

J. Scott Hall
ATTORNEY FOR D. J. SIMMONS, INC.

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City, State, ZIP+4
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11-6-01

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

IN THE MATTER OF THE APPLICATION OF
McELVAIN OIL & GAS PROPERTIES, INC.
FOR COMPULSORY POOLING,
RIO ARRIBA COUNTY, NEW MEXICO — CASE NO. 12,635 *De Novo*

Consolidated with:

IN THE MATTER OF THE APPLICATION OF
D. J. SIMMONS, INC. FOR COMPULSORY POOLING,
RIO ARRIBA COUNTY, NEW MEXICO — CASE NO. 12705

D.J. SIMMONS, INC.'S HEARING MEMORANDUM

D.J. Simmons, Inc., ("Simmons"), through its counsel, submits this memorandum of points and authorities for consideration by the Commission in conjunction with the November 6, 2001 hearing on these consolidated applications. This memorandum addresses two points: (1) The use of the Division's powers to force-pool interests for purposes not authorized by the compulsory pooling statute; and (2) the applicable standards of "diligence" and "good faith" that an operator must meet in its efforts to obtain the voluntary participation of other interest owners as a pre-condition to filing a compulsory pooling application.

INTRODUCTION

McElvain Oil and Gas Properties, Inc., ("McElvain"), initiated this force-pooling proceeding on November 10, 2000 when it sent a perfunctory and uninformative well proposal to Simmons, followed by the filing of an Application for Compulsory Pooling on March 15, 2001 seeking to pool the **SE/4** of Section 25, T-25-N, R-3-W to create a

320 acre **S/2** lay-down spacing unit for the re-entry and re-completion of its Naomi Com No. 1 well. McElvain's application is unnecessary because it already owns 100% of the oil and gas leases underlying the **W/2** of Section 25, and is free to dedicate that acreage to its well located at an unorthodox location 450' from the west line in the **SW/4** of the section. McElvain proposes to re-complete its well in the Blanco-Mesaverde pool only; it has no plans to develop the Gallup-Dakota reserves underlying the **SE/4**. McElvain's proposal to ignore its pre-existing **W/2** unit and instead initiate compulsory pooling proceedings to dedicate a **S/2** unit to its well makes little sense and is contra-indicated by the known geology and the prevailing north-south drainage patterns in the area. Moreover, McElvain's proposal would disrupt and likely prevent the further development and recovery of Blanco-Mesaverde and Gallup-Dakota reserves in the remainder of the section.

Simmons opposed McElvain's application for the reasons, among others, that given the availability of a pre-existing **W/2** unit, the compulsory pooling proceedings would result in the unnecessary expenditure of time, effort and legal expense. McElvain's force-pooling effort would also interfere with Simmons's plans to dedicate an **E/2** unit to the drilling of its Bishop 25-1 No. 1 well by which it proposes to evaluate both the Blanco-Mesaverde and Gallup-Dakota formations.

At the May 17, 2001 examiner hearing on its Application, McElvain's motives were made clear: During cross-examination, all of McElvain's witnesses admitted that the reason they weren't dedicating their 100% owned **W/2** unit to the well and were instead asking the Division to force-pool the **SE/4** of the section for a **S/2** unit was to require others to bear the costs of their operation. As was said during the hearing,

McElvain is using the Division's compulsory pooling process as a tool for "mitigating its risk". (See Excerpts from May 17, 2001 Hearing Transcript, Ex. "A", attached.) In other words, by forsaking its pre-existing stand-up spacing unit and forcing the interest owners in the **SE/4** of the section into a lay-down **S/2** unit, McElvain was engaging in a risk-mitigation scheme: same well, same location, but at a fraction of the cost to it. According to McElvain's witnesses, this was the "primary" reason for force-pooling the other interest owners.

1. The Use of the Compulsory Pooling Statute for purposes of "Risk-Mitigation" is Impermissible.

McElvain's invocation of the compulsory pooling statutes[1] for the purpose of mitigating its economic risk is an abusive and impermissible use of the Division's police powers. McElvain can point to no provision in those statutes that authorizes the Division to utilize risk mitigation as a basis for the forced-pooling of a third party's property interests. Indeed, no such provision exists, either express or implied, under even the broadest reading of the law.[2] An examination of the language of the Oil and Gas Act ("the Act") demonstrates that McElvain's application is inappropriate because it requests the Commission to act beyond the scope of its statutory authority. "The starting point in every case involving the construction of a statute is an examination of the language utilized by [the legislature] when it drafts the pertinent statutory provisions. *State v. Johnson*, 2001-NMSC-001, P.6, 15 P.3d 1233 (2001) quoting *State v. Wood*, 117 N.M. 682, 685, 875 P.2d 1113, 1116 (Ct. App. 1994). "When a statute contains language which is clear and ambiguous, we must give effect to that language and refrain from

[1] NMSA, 1978, §§ 70-2-17 and 70-2-18

further statutory interpretation." *Id.* quoting *State v. Jonathan M.*, 109 N.M. 789, 790, 791 P.2d 64, 65 (1990). "The Oil Conservation Commission is a creature of statute, expressly defined, limited and empowered by the laws creating it." *Santa Fe Exploration Co. v. Oil Conservation Comm'n*, 114 N.M. 103, 113, 835 P.2d 819, 829 (1992) quoting *Continental Oil Co. v. Oil Conservation Comm'n*, 70 N.M. 310, 318, 373 P.2d 809, 814 (1962).

The Act gives the Oil Conservation Commission ("the Commission") and the Oil Conservation Division ("the Division") two major duties: the prevention of waste as well as the protection of correlative rights. *Id.* citing NMSA 1972, §70-2-11(A); *Continental Oil Co.*, 70 N.M. at 323, 373 P.2d at 817. Correlative rights are defined as:

> The opportunity afforded . . . to the owner of each property and a pool to produce without waste his just and equitable share of the oil . . . 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 . . . under the property bears to the total recoverable oil . . . in the pool and, for such purpose, to use his just and equitable share of the reservoir energy.

NMSA 1978, §70-2-33(H). In addition to its ordinary meaning, waste is defined as "the locating, spacing, drilling, equipping, operating or producing, of any well or wells in a manner to reduce or tend to reduce the total quantity of crude petroleum oils . . . ultimately recovered from any pool." NMSA 1978 §70-2-3 (A).

Additionally, in NMSA 1978, § Section 70-2-17 (C), the New Mexico Legislature has specified the circumstances where the Division is authorized, not mandated, to exercise its compulsory pooling powers. That authority is limited to the following circumstances:

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[2] The non-consent risk penalty provision of Section 70-2-17(C) is entirely separate and wholly inapplicable to a discussion of the basis and extent of the Division's authority to force pool working interests.

- Where there are two or more separately owned tracts within a spacing unit;
- One of the owners who has a right to drill proposes to drill on the unit to a common source of supply.

If the separate owners have not agreed to pool their interests, the Division or Commission is mandated to pool interests ***only*** in the circumstance where:

- The Division of Commission finds pooling is necessary to:
- - avoid the drilling of unnecessary wells,
- - protect correlative rights, or
- - to prevent waste.

NMSA 1978, ss70-2-17(C).

The mitigation of risk is not included within the enumerated circumstances where the compulsory pooling authority may be invoked. Moreover, the Commission is constrained from reading such a provision into its authority. "The Oil Conservation [Division] is a creature of statute, expressly defined, limited and empowered by the laws creating it." *Continental Oil Co. v. Oil Conservation Commission*, 70 N.M. 310, 318, 373 P.2d 809, 817 (1962). Instead, the Commission is obliged to follow the "plain meaning" of the statute. This plain meaning rule, is a guideline for determining legislative intent. *Johnson, 2001-NMSC-001, P.6,* citing *Junge v. John D. Morgan Constr. Co.*, 118 N.M. 457, 463, 882 P.2d 488, 54 (Ct. App. 1994). It is actually the responsibility of the court or in this case, the Commission, to search for and effectuate the purpose and object of the underlying statutes. *Id.* citing *State ex rel. Helman v. Gallegos*, 117 N.M. 346, 353, 871 P.2d 1352, 1359 (1994). Additionally, statutes should be harmonized and construed together when possible, so that the achievement of their goals is facilitated. *Id.* citing

State ex rel. Quintana v. Schneder, 115 N.M. 573, 575-76, 855 P.2d 562, 564-65 (1993). Further, "statutes must be construed so that no part of the statute is rendered surplusage or superfluous." In *Re Rehabilitation of W. Investor's Life Ins. Co.*, 100 N.M. 370, 373, 671 P.2d 31, 34 (1983).

More importantly the Commission may be in violation of the principal of separation of powers if it grants the McElvain's application because, "an unlawful conflict or infringement occurs when an administrative agency goes beyond the existing New Mexico statutes or case law it is charged with administering and claims the authority to modify this existing law or to create new laws on its own." *State ex rel. Sandel v. New Mexico Public Utility Commission*, 1999-NMSC-19, P.12, 980 P2d 55. When reading the language of a statute and attempting to ascertain and give effect to the intention of the legislature, the language of the statute must be considered as a whole; however, a literal reading must give way to a reasonable construction when the literal reading leads to injustice, absurdity, or contradiction. *State v. Romero*, 2000-NMCA-029, P.27, 999 P.2d 1038.

It would be absurd to think that the Act was enacted in order to mitigate the economic risk of parties like McElvain. It is not the function of the Commission to make it more economically and financially lucrative for McElvain to operate its unit. McElvain's use of the Division's processes and the compulsory pooling statutes as a means to reduce its economic risk is wholly outside the agency's statutory authority. Risk mitigation is a complete misapplication of the law and should not be allowed. Were it to grant McElvain's application, the Commission would be acting in excess of its clearly delineated authority and will be in violation of the separation of powers doctrine.

The Commission should put all operators on notice by way of specific findings in an order stating that the use of the compulsory pooling process for such unauthorized purposes shall not be permitted.

2. The Applicable Standards of Diligence and Good Faith.

McElvain has approached this proceeding as if the granting of a compulsory pooling order were its entitlement. In so doing, it has failed to make a good faith effort to obtain an agreement for the voluntary participation of Simmons.

As McElvain would have it, under the compulsory pooling statute, an operator need do nothing more than appear at a hearing and show (1) it has the right to drill, (2) that there are two or more interest owners in a spacing unit, (3) that the owners have not agreed to pool their interests, and (4) it made a well proposal to the other owners, as perfunctory as that effort might have been.

Under NMSA 1978, §70-2-18(A), an operator proposing to dedicate separately-owned lands to a proration unit has an "obligation" to negotiate a voluntary agreement with the other interest owners to pool their lands. The Division and the Commission require operators to show that they have made a "diligent" and "good faith" effort to negotiate a voluntary agreement before a compulsory pooling application may be filed.[3]

The historic treatment by the agency of its compulsory pooling powers is revealing: The first compulsory pooling orders made by the Commission were made with some reluctance. In many instances, the Commission ordered pooling but further ordered that a continuing effort be made to secure the consent of all the interests involved. Morris, Richard, *Compulsory Pooling of Oil and Gas Interests in New Mexico*, 3 Nat.

[3] Indeed, the "good faith" requirement has been expressly codified in the compulsory unitization procedures of the Statutory Unitization Act at NMSA 1978, §70-7-6-A(5).

Resources J. 316 (1963). (Exhibit B, attached.) After a few cases had been decided, the Commission adopted the attitude toward compulsory pooling that still remains today. In each case there is an inquiry concerning the efforts made by the operator to secure the consent of the interests being pooled. The reasonableness of the offer may also be questioned. Morris, Richard, *Compulsory Pooling of Oil and Gas Interests in New Mexico*, 3 Nat. Resources J. 316, 318 (1963). The Commission continues to recognize the importance of good faith efforts to negotiate before commencing compulsory pooling actions, and uses it as one criterion to determine if the application will be accepted or denied.

While the parameters of what constitutes a "good faith" effort have not been precisely defined in any order of the Commission or the Division, or in any reported court decision, the procedure of compulsorily pooling the interests of landowners in order to drill wells is strikingly analogous to the procedure of eminent domain, where one, who seeks to invoke the state's police power of eminent domain, can condemn or expropriate private lands for public use. Both compulsory and eminent domain dramatically effect the rights landowners have in their land, and both compel the landowner into an action that was not of his/her own desire. One of our most basic liberties is the right to property, and it must be guarded. Actions like eminent domain and compulsory pooling must be carefully scrutinized. Enforcing a good faith effort to negotiate is one way the Commission and the courts can slow the imposition on private citizens' rights to property. While eminent domain dissolves all rights of the property owner, its procedure and effect are very similar to the action of compulsory pooling, and can shed light on the proper procedure of conducting these acts in accordance with the right to property.

Eminent domain is the power of a government entity to take private lands and convert them for public use, with just compensation. Eminent domain is liberally interpreted in New Mexico. *Landavazo v. Sanchez*, 111 N.M. 137, 140, 802 P.2d 1283, 1286 (1990). The decision of the grantee of the power of eminent domain as to the necessity, expediency, or propriety of exercising that power is political, legislative, or administrative and its determination is conclusive and not subject to judicial review, absent fraud, bad faith, or clear abuse of discretion. *Id.* at 140, 1286; *North v. Public Service Co. of New Mexico*, 101 NM 222, 680 P.2d 603 (N.M. App. 1983). While eminent domain is not often subject to the judicial review, it is expressly subject to the courts supervision when it has been exercised in bad faith, or when one has exercised the power and has failed to make a good faith effort to negotiate with landowners commencing the action. NMSA 1978 § 42-A-1-4A states, "A condemnor shall make reasonable and diligent efforts to acquire property by negotiation." NMSA 1978 § 42-A-1-6A further states "...an action to condemn property may not be maintained over timely objection by the condemnee unless the condemnor made a good faith effort to acquire the property by purchase before commencing the action." (emphasis added). Just as NMSA 1978 § 70-2-1 et. seq. sets out the requirements before commencing compulsory pooling, the eminent domain statutes stress the importance and lay out the requirement of good faith negotiations with the landowners before any further action is taken.

There are many eminent domain cases that analyze good faith efforts in negotiations. "What constitutes a good faith offer must be determined in light of its own particular circumstances." *Unger v. Indiana & Michigan Electric Co.*, 420 N.E.2d 1250, 1254 (Ind. App. 1981). A good faith offer is one where a reasonable offer is made in

good faith and a reasonable effort is made to induce the owner to accept it. Perfunctory offers are not sufficient. *Id.* at 1254 (emphasis added.) In the *Unger* case, the Indiana & Michigan Electric Company, (I&M) did not make a good faith effort to purchase the property of Unger. In that case, I&M failed to form an opinion on the fair market value of the easement they sought to acquire. Similarly, in the present case, McElvain failed to make any reasonable offer in good faith and failed to make an effort to induce Simmons to accept it. Furthermore, McElvain's uninformative proposal was merely a perfunctory offer. Had McElvain in good faith been attempting to persuade Simmons to agree, it would have included all the relevant information in order to achieve that goal.

Similarly, the city of Detroit's offer to purchase land owned by non-interested parties did not constitute a good faith offer in *Matter of Acquisition of Land for Cent. Indus. Park Project*, 338 N.W.2d 204 (Mich. App. 1983). Their offer did not include either lesser of appraised detach-reattach costs of movable trade fixtures or their value in place. Because the city did not include in its offer all relevant elements, the court found that it was not a good faith effort. An offer must be fair and reasonable, not wholly inadequate. *Chambers v. Public Service Co. of Indiana, Inc.*, 335 N.E.2d 781 (Ind. 1976).

The question to be asked in determining whether the condemnor engaged in good faith is whether the condemnor made a good faith effort to acquire the property or rights by conventional agreement before the expropriation suit was filed. *Transcontinental Gas Pipeline Corp. v. 118 Acres of Land, etc.* 745 F.Supp. 366 (1990). In that case, Transcontinental (Transco) negotiated with the defendants on numerous occasions, made numerous offers in proportion to appraisals, and when the negotiations reached a point

where Transco concluded that any further attempt would be useless, stopped. Transco's efforts were found to be in good faith. In the present case, however, McElvain only contacted Simmons once with an inadequate proposal. It did not make any further contacts with Simmons in order to obtain his participation before filing an application for compulsory pooling. Furthermore, McElvain had no indication from Simmons that further negotiations would prove futile. Rather, it was Simmons who initiated further contacts with McElvain, in order to obtain specific geological, engineering, and cost information. Simmons's action of seeking more information gave the indication that it was considering the proposal, and McElvain's failure to follow up before filing its application for compulsory pooling are all evidence of McElvain's lack of a good faith effort to negotiate.

Here, McElvain made only a token, cursory effort to obtain Simmons's participation in its re-completion proposal. On November 10, 2000, McElvain sent a bare-bones proposal to Simmons, but failed to include either a drilling and completion procedure or an AFE, which is a standard part of any proposal. After its November 10th letter, McElvain initiated no further contacts before filing its compulsory pooling application on March 15, 2001. All other contacts were initiated by D.J. Simmons's staff, primarily for the purposes of obtaining specific geologic, engineering and cost information, as well as some justification for a S/2 unit. It was not until the evening before the hearing on its application that McElvain's landman made any effort to initiate a discussion on her own.

These efforts fall far short of the standards that the industry and the Division expect an operator to meet when negotiating for an interest owner's voluntary participation in a well proposal.

CONCLUSION

McElvain invokes this agency's compulsory pooling powers not for the purposes of preventing waste or protecting correlative rights, but simply to reduce its exposure to risk. The Commission lacks the authority to grant such relief. In addition, McElvain has failed to demonstrate adequate diligence or that it made a reasonable, good faith effort to obtain the voluntary agreement of Simmons. For these reasons, McElvain's Application must be denied.

Respectfully submitted,

MILLER, STRATVERT & TORGERSON, P.A.

By _____

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Certificate of Mailing

I hereby certify that a true and correct copy of the foregoing was hand-delivered to counsel of record on the 6th day of November, 2001, as follows:

Michael Feldewert, Esq.
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_____
J. Scott Hall

STATE OF NEW MEXICO

ENERGY, MINERALS AND NATURAL RESOURCES DEPARTMENT

OIL CONSERVATION DIVISION

IN THE MATTER OF THE HEARING CALLED BY THE OIL CONSERVATION DIVISION FOR THE PURPOSE OF CONSIDERING:	)	CASE NO. 12,635
APPLICATION OF McELVAIN OIL AND GAS PROPERTIES, INC., FOR COMPULSORY POOLING, RIO ARRIBA COUNTY, NEW MEXICO	)	

REPORTER'S TRANSCRIPT OF PROCEEDINGS

EXAMINER HEARING

BEFORE: MICHAEL E. STOGNER, Hearing Examiner

May 17th, 2001

Santa Fe, New Mexico

This matter came on for hearing before the New Mexico Oil Conservation Division, MICHAEL E. STOGNER, Hearing Examiner, on Thursday, May 17th, 2001, at the New Mexico Energy, Minerals and Natural Resources Department, 1220 South Saint Francis Drive, Room 102, Santa Fe, New Mexico, Steven T. Brenner, Certified Court Reporter No. 7 for the State of New Mexico.

* * *

EXHIBIT A

I N D E X

May 17th, 2001
Examiner Hearing
CASE NO. 12,635

(Continued...)

Q. Couldn't McElvain have dedicated a west-half unit to the Naomi?

A. That's certainly a possibility, yes, we could have dedicated the west half.

Q. And why didn't it do so?

A. Its choice was based on the fact that it wanted to share the risk of the test, as well as closely identify a drainage pattern for a geologic position as we could. So for those combination of reasons we chose the south half.

Q. Would you agree that by dedicating a west-half unit to the well, which McElvain owns 100 percent of, McElvain could have avoided the administrative, overhead and legal expense associated with this compulsory pooling proceeding?

A. I assume that would have been the case, yes.

Q. As a landman familiar with compulsory pooling proceedings before the New Mexico Oil Conservation Division, can you point to any provision in the compulsory pooling statute that allows risk as a basis for pooling another interest party? In other words, where is it in the compulsory pooling statute that authorizes an operator to seek to mitigate its risk in drilling a well by pooling another interest owner?

A. I would have to defer to our attorney to give me better advice on that. I couldn't tell you specifically.

Q. So you don't know of any such provision in the compulsory pooling statute?

A. I can't tell you that there is or there isn't. I'm not familiar enough with the actual wording within the provision to be able to tell you that, so no.

Q. So the record is clear, you do agree with me that the primary motivation for dedicating a south-half unit to the Naomi well was risk mitigation?

A. Primary could be, yes. Yes.

Q. What is the prevailing spacing pattern for the Blanco-Mesaverde in the area, if you know?

A. I am not aware that there is a prevailing spacing pattern for the Blanco-Mesaverde. I'm not aware that there's much production right here in this specific area, this general vicinity --

Q. Does -- I'm sorry?

A. -- for this particular zone, for Blanco-Mesaverde, I don't think that there has been a pattern established in this immediate vicinity.

Q. Does McElvain offer another Blanco-Mesaverde well scenario?

A. Yes, we do.

Q. And can you tell us, if you know, how those spacing units are oriented to those --

A. I can tell you that some are north-south and some

are east-west. I can tell you they go both ways --

Q. So -- I'm sorry.

A. -- 320-acre north-south in some cases, and 320-acre east west. So there's laydown and standup both.

Q. All right, so geology wasn't necessarily the prime consideration in orienting --

A. Geology is a consideration in each one of them. Geology, land, ability, surface restrictions. There's a lot of different factors that are taken into account in forming the spacing patterns.

Q. Including mitigation of risk?

A. Certainly.

Q. When did McElvain acquire the Kai interest?

A. Recently, in the last week.

Q. All right.

A. We had been negotiating for the purchase of that interest for several months.

Q. Did McElvain acquire the Kai interest for its Gallup-Dakota potential?

A. No.

Q. Did it evaluate the Gallup-Dakota potential in the southeast quarter?

A. That I'm not qualified to answer. I can tell you that we previously had Gallup-Dakota production in the Wynona Number 1 well and it was uneconomic and it was

A. It could.

Q. Have you undertaken a study of any of the literature done evaluating formational fracturing in the Blanco-Mesaverde formation in this area?

A. Not in the Mesaverde. I've looked at in other formations, but not in the Mesaverde.

Q. All right. Do you know that it exists for --

A. Yes, I do.

Q. The Naomi Number 1 in its unorthodox location, in your view, is it better situated to drain reserves from the south half or the west half of Section 25?

A. In my opinion, I would say the south half.

Q. And what's the basis of your opinion?

A. The trend goes east-west on the isopach.

Q. What other data or information would you evaluate to make a determination whether that well would drill west-half as opposed to south-half reserves?

A. I would think that that would -- I would talk to the engineer about it, because I think that's an engineering issue.

Q. All right. You don't feel that you're qualified to answer?

A. That's correct.

Q. Is it your understanding from your employment as a geologist at McElvain that geology was not the primary

consideration for dedicating a south-half unit to this well?

A. Yes.

MR. HALL: Nothing further.

EXAMINER STOGNER: Any redirect?

MR. FELDEWERT: No.

EXAMINATION

BY EXAMINER STOGNER:

Q. If the Naomi Number 1 turns out to be a commercial producer in the Blanco-Mesaverde, where do you feel would be the best place for the infill well, or for a second well in that section to be placed?

A. In the southeast quarter.

Q. And why is that?

A. Because I think the trend goes east-west, based on the limited subsurface data that we have.

Q. On Exhibit Number 10, how was the information obtained? Was this -- any 3-D seismic involved --

A. No --

Q. -- or was this just the well?

A. -- it's strictly from log data, porosity logs.

Q. Now, is this the only well control you have, is what's shown on the map? Or are there any other wells out there that --

A. The wells that are shown on this map are all

Q. Do you agree with the testimony of the other two McElvain witnesses here that mitigation of risk is a primary consideration in dedicating a south-half unit to the well?

A. I don't think mitigation of risk is the exact term. I like to call it sharing of the risk. But more to the point, proving up your neighbor's reserves, that is a consideration, yes.

Q. Proving up your neighbor's reserves in the southeast quarter?

A. Yes, sir.

Q. And you would be proving up McElvain's reserves in the southeast quarter as well, correct?

A. To some extent, yes.

MR. HALL: I have nothing further, Mr. Examiner.

EXAMINER STOGNER: Any redirect?

MR. FELDEWERT: Just one question.

REDIRECT EXAMINATION

BY MR. FELDEWERT:

Q. Mr. Steuble, looking at McElvain Exhibit Number 11, given the information that you have today, is it your opinion that there are commercially recoverable Gallup-Dakota reserves anywhere in Section 25?

A. In my opinion, no.

MR. FELDEWERT: Okay, that's all I have.

COMPULSORY POOLING OF OIL AND GAS INTERESTS IN NEW MEXICO

RICHARD S. MORRIS*

In 1935, the New Mexico Legislature passed the Oil Conservation Act[1] to require the conservation of oil and generally to provide for the regulation of the oil industry. Although this action followed closely the pattern of legislation then developing in other states, notably Texas[2] and Oklahoma,[3] the New Mexico Oil Conservation Act is distinctive in being the first truly comprehensive conservation law to be adopted in any state. The Act remains substantially unchanged today.[4]

The Act defines and prohibits the waste of oil,[5] requires the proration of oil to market demand,[6] and establishes the Oil Conservation Commission[7] to administer and enforce its provisions. Among the broad powers given the Commission is the authority to establish for each oil pool the size of proration unit which one well can efficiently and economically drain.[8] Also, the Commission is authorized to enforce development on the size proration unit it prescribes as standard in a pool by requiring whatever diverse interests might exist in such a unit to join for the purpose of drilling a well.[9]

The role of the proration unit in the orderly development of oil and gas properties is well established.[10] But the power of compulsory pooling, by which this orderly development may be enforced, is not well established and in many quarters appears to be misunderstood as to both its purpose and the method by which it is effected.

Twenty-four states, including New Mexico, now have some form of com-

* Member of the New Mexico bar.

1. N.M. Laws 1935, ch. 72; now N.M. Stat. Ann. §§ 65-3-1 to -34 (1953).

2. Tex. Acts 4th Called Sess. 1932, ch. 2 at 3; Tex. Acts 1935, ch. 76 at 180.

3. Okla. Laws 1933, ch. 131.

4. For a history of this legislation see Conservation of Oil and Gas: A Legal History, 1958 at 155-57 (Sullivan ed. 1958).

5. N.M. Stat. Ann. § 65-3-3 (1953), defines "waste" to include both surface and subsurface waste, as well as waste in its ordinary meaning. This section also defines waste to be the production of oil or gas in excess of reasonable market demand, or the nonratable taking of oil.

6. N.M. Stat. Ann. §§ 65-3-2 to -3 (1953).

7. N.M. Stat. Ann. § 65-3-4 (1953). The Commission is composed of the Governor, the Land Commissioner, and the State Geologist.

8. N.M. Stat. Ann. § 65-3-14(b) (1953).

9. N.M. Stat. Ann. § 65-3-14(c) (1953) (amended by N.M. Stat. Ann. § 65-3-14(c) (Supp. 1961)).

10. See Legal History of Conservation of Oil and Gas—A Symposium (Published by Mineral Law Section, A.B.A., 1938); Conservation of Oil and Gas: A Legal History, 1948 (Murphy ed. 1949); Conservation of Oil and Gas: A Legal History, 1958 (Sullivan ed. 1958).

EXHIBIT

B

pulsory pooling law.[11] In a few states, notably Oklahoma and Mississippi, the compulsory pooling laws have received considerable attention in the courts.[12] Without exception they have been upheld against attacks of unconstitutionality.[13]

In New Mexico, however, there has been no judicial recognition or interpretation of the compulsory pooling law even though it has been in effect since 1935—the year in which Oklahoma adopted its pooling law.[14] The lack of New Mexico cases involving compulsory pooling is no indication that this provision of the law has not been invoked. Many cases have been considered by the New Mexico Oil Conservation Commission, and they have resulted in orders requiring the pooling of oil and gas interests, and, in many of these cases, novel legal questions have arisen.

I

POOLING PRIOR TO 1961

A Non-Consenting Working and Unleased Interests

New Mexico's original compulsory pooling law[15] remained unchanged until

11. See Myers, The Law of Pooling and Unitization, Voluntary—Compulsory § 8.01(4) (1957, Supp. 1961).

12. See, *e.g.*, Patterson v. Stanolind Oil and Gas Co., 182 Okla. 155, 77 P.2d 83 (1938), *appeal dismissed*, 305 U.S. 376 (1939); Superior Oil Co. v. Foote, 214 Miss. 857, 59 So. 2d 85 (1952).

13. See Annot., 37 A.L.R.2d 434 (1954).

14. Only two cases involving orders of the Oil Conservation Commission have been appealed to the New Mexico Supreme Court. The first, Continental Oil Co. v. Oil Conservation Comm'n, 70 N.M. 310, 373 P.2d 809 (1962), 3 Natural Resources J. 178 (1963), concerned a change of the proration formula in the Jalmat Gas Pool of Lea County, New Mexico. The second, Sims v. Mechem, 382 P.2d 183 (N.M. 1963), concerned a change in the configuration of a proration unit, and incidentally involved the compulsory powers of the Commission. In *Sims* the court stated that the Commission has unquestionable power to require pooling of properties where the owners have failed to agree. But the court held the pooling order invalid since the Commission had made no finding of waste.

15.

> The pooling of properties or parts thereof shall be permitted, and, if not agreed upon, may be required in any case when and to the extent that the smallness or shape of a separately owned tract would, under the enforcement of a uniform spacing plan or proration unit, otherwise deprive or tend to deprive the owner of such tract of the opportunity to recover his just and equitable share of the crude petroleum or natural gas, or both, in the pool; Provided, that the owner of any tract that is smaller than the drilling unit that is established for the field, shall not be deprived of the right to drill on and produce from such tract, if same can be done without waste; but in such case, the allowable production from such tract, as compared with the allowable production therefrom if such tract were a full unit, shall be in ratio of the area of such tract to the area of the full unit. All orders requiring such pooling shall be upon terms and conditions that are just and reasonable, and will afford to the owner of each tract in

1961.[16] It contained a provision authorizing the Commission to require pooling "when and to the extent that the smallness or shape of a separately owned tract would, under the enforcement of a uniform spacing plan or proration unit, otherwise deprive or tend to deprive the owner of such tract of the opportunity to recover his just and equitable share of the crude petroleum or natural gas, or both, in the pool . . . ." The law further provided "that the owner of any tract that is smaller than the drilling unit established for the field, shall not be deprived of the right to drill on and produce from such tract, if same can be done without waste . . . ." The Commission was authorized to adjust allowables proportionately to the size of the tract when a small tract owner insisted on his right to develop his own property and, further, to determine costs between interests pooled by Commission orders.

The first compulsory pooling orders entered by the Commission showed a reluctance to use the full authority of the law. In several instances the Commission required pooling but further ordered that a continuing effort be made to secure the consent of all interests to a communitization agreement.[17] In one case,[18] the Commission ordered pooling but required that all interests be signed to a communitization agreement as a condition to the effectiveness of the order.

After the first few cases had been considered, the Commission adopted a basic attitude toward pooling which, in most aspects, remains unchanged. In each case inquiry is made by the Commission concerning the efforts of the applicant for compulsory pooling to secure the consent of the interests being pooled.[19] Where unleased interests are to be pooled, the reasonableness of the offer to lease may be questioned.[20] Whether active protest to pooling is voiced[21] and whether the protestant appears at the Commission hearing[22] are

the pool the opportunity to recover or receive his just and equitable share of the oil or gas, or both, in the pool as above provided, so far as may be practicably recovered without waste. In the event such pooling is required, the costs of development and operation of the pooled unit shall be limited to the lowest actual expenditures required for such purpose including a reasonable charge for supervision; and in case of any dispute as to such costs, the commission shall determine the proper costs.

N.M. Stat. Ann. § 65-3-14(c) (1953) (amended by N.M. Stat. Ann. § 65-3-14(c) (Supp. 1961).

16. N.M. Stat. Ann. § 65-3-14(c) (Supp. 1961). See note 41 *infra*.

17. See, *e.g.*, Texas Co., Case No. 117, Order No. R-739 (N.M. Oil Conservation Comm'n 1948).

18. C. H. Sweet, Case No. 427, Order No. R-234 (N.M. Oil Conservation Comm'n 1952).

19. See, *e.g.*, El Paso Natural Gas Co., Case No. 595, Order No. R-396 (N.M. Oil Conservation Comm'n 1953).

20. *Ibid.*

21. See, *e.g.*, Blackwood and Nichols Co., Case No. 566, Order No. R-357 (N.M. Oil Conservation Comm'n 1953).

22. *Ibid.*

strongly considered factors. Also, the economic feasibility of a second well on a proration unit is considered a factor in ordering pooling,[23] and in many cases orders have been entered based on a finding that waste would be caused by the drilling of a second well on the acreage to be pooled.[24]

An examination of these cases reveals that "waste" as used in this context meant *economic* waste rather than the *physical* waste of oil and gas. The protection of correlative rights and the prevention of economic waste caused by the drilling of unnecessary wells were the chief considerations in ordering pooling, and physical waste became a factor only where it appeared that without pooling no well would be drilled to develop the proration unit.

One of the major problems of compulsory pooling in New Mexico is the determination of costs between the operator on the one hand and the non-consenting working interest owner or unleased interest owner on the other. Where a working interest or an unleased interest has not agreed to voluntary pooling and an operator seeks compulsory pooling of that interest with interests of his own, usually amounting to most of the acreage in the proposed unit, that operator will seek to have the interest being pooled charged with its share of the costs of unit development and operation. The non-consenting interest may not object to being pooled but may object to the operator's proposal for the apportionment of costs. This dispute has occurred in numerous pooling cases[25] and is probably the reason for most cases being brought before the Commission.

In early cases involving disputes of this nature the Commission again was reluctant to use the full authority of the pooling law. Many orders merely required pooling and left to the operator and the non-consenting interest owner the problem of working out costs between them the best they could.[26] In later cases the Commission, in its pooling orders, began providing alternative courses of action for the non-consenter to follow. In the first case providing such alternatives,[27] an owner of an unleased interest involuntarily pooled was allowed to share in the production from the unit from such time as he had (a) paid his proportionate share of the well costs, or (b) made other arrangements satisfactory to the operator. The Commission retained jurisdiction to determine well costs in the event of a dispute. It seems apparent now, with the experience of more recent cases, that this order was inadequate to protect a non-

23. See note 37 *infra*.

24. See, *e.g.*, Phillips Petroleum Co., Case No. 978, Order No. R-747 (N.M. Oil Conservation Comm'n 1956).

25. See, *e.g.*, Saul A. Yager and El Paso Natural Gas Co., Case Nos. 1000-1001 Consol., Order No. R-795 (N.M. Oil Conservation Comm'n 1956).

26. See, *e.g.*, Blackwood and Nichols Co., Case No. 566, Order No. R-357 (N.M. Oil Conservation Comm'n 1953).

27. Phillips Petroleum Co., Case No. 978, Order No. R-747 (N.M. Oil Conservation Comm'n 1956).

consenting interest owner who might have been unable to pay his share of well costs.

Following closely on this case the Commission considered another pooling application involving a non-consenting unleased interest.[28] At the hearing the operator proposed that the pooling order should provide the non-consenter with the alternative of paying his share of well costs in cash or allowing recovery out of production to the extent of 150 per cent of his share. The non-consenting interest opposed this method of allocating costs, contending that no penalty should be assessed against him as a "carried" interest due to the statutory requirement that the costs be "limited to the lowest actual expenditures required . . . ."[29] for drilling the well. The non-consenting interest further contended that his unleased interest should be considered seven-eighths working interest and one-eighth royalty interest and, accordingly, that costs should be withheld only from seven-eighths of the proceeds attributable to his interest. The Commission's order[30] provided that the non-consenter pay his share of well costs in cash within fifteen days from the date of the order or, as an alternative, that the operator be allowed to withhold from production attributable to the full eight-eighths of his interest 125 per cent of his share of well costs.

The recovery of 125 per cent allowed in this order set the pattern for future orders which pooled non-consenting working or unleased interests. Since by statute costs were limited to "lowest actual expenditures . . . including a reasonable charge for supervision . . . ."[31] the additional twenty-five per cent must be justified as a charge for supervision. Charges for interest or for risk, although not disallowed, were not expressly authorized by the terms of the statute.[32]

So far in this discussion the cases mentioned have been those where the party bringing the pooling case before the Commission was an operator who owned most of the working interest in the proposed unit and who had been unsuccessful in leasing or communitizing the remainder. This is the typical case for which the pooling law was created. Some cases, however, have not fit neatly into this category; consider, for example, the following situation.[33]

Upon a showing that a small unleased interest not only refused to lease or

28. Saul A. Yager and El Paso Natural Gas Co., Case Nos. 1000-1001 Consol., Order No. R-795 (N.M. Oil Conservation Comm'n 1956).

29. N.M. Stat. Ann. § 65-3-14(c) (1953) (amended by N.M. Stat. Ann. § 65-3-14(c) (Supp. 1961)). See note 15 *supra*.

30. Saul A. Yager and El Paso Natural Gas Co., Case Nos. 1000-1001 Consol., Order No. R-795 (N.M. Oil Conservation Comm'n 1956).

31. N.M. Stat. Ann. § 65-3-14(c) (1953) (amended by N.M. Stat. Ann. § 65-3-14(c) (Supp. 1961)). See note 15 *supra*.

32. See note 48 *infra*.

33. W. H. Swearingen, Case No. 2080, Order No. R-1748-A (N.M. Oil Conservation Comm'n 1960).

join an operator's proposed unit but actively opposed being pooled into the unit on any terms, the Commission created a non-standard proration unit which excluded the unleased interest.[34] After the order was entered, but before the unit well was drilled, the owner of the unleased interest reconsidered and applied to the Commission for an order requiring the pooling of his acreage with the acreage previously included in the non-standard unit.

This type of an application raised several important questions: Inasmuch as the owner of the unleased interest did not protest, but rather endorsed the order establishing the non-standard unit which excluded his acreage, was his pooling application a collateral attack upon the prior order? May the compulsory pooling law be invoked by an interest other than the operator who proposes to drill the unit well? Should a pooling order enforce the assumption of dry hole risk upon the owner of a small unleased interest solely because he is the applicant for compulsory pooling?

Little consideration was given the first two questions. The application was heard and the dispute was narrowed to the question of how the costs and risk of drilling the unit well should be allocated. The Commission's order allowed the owner of the unleased interest the alternative of either paying his share of well costs in cash by a certain date, subject to a subsequent adjustment to actual cost, or allowing his share of well costs, plus twenty-five per cent thereof as a charge for supervision, to be paid out of the production attributable to his entire interest. No effective separation of the unleased interest into working and royalty interests was recognized. A proviso was attached to the latter alternative that in the event the well was a dry hole the unleased interest should bear its share of well costs.

The Commission evidently required the unleased interest to take the risk of paying dry hole costs due to the absence of statutory authority to provide for an increased percentage to be withheld from production for risk. It should be noted that in this case there was little dry hole risk.

The practice of allowing the operator to withhold from eight-eighths of the proceeds attributable to an unleased interest was not continued beyond this case; in all subsequent cases involving the involuntary pooling of unleased interests, the interests were treated as being separated into working and royalty interests—the royalty interests were paid free of costs.

In most cases where the owner of some interest in a proposed proration unit has opposed the pooling of his interest, such as in the last-mentioned case, the Commission has excluded it, if practicable, and formed a non-standard unit. Most cases of this sort have involved small, unleased interests which have opposed pooling on any terms due to their own ignorance or stubbornness, or both.

34. Charles Loveless, Case No. 2036, Order No. R-1748 (N.M. Oil Conservation Comm'n 1960).

Nevertheless, where opposition to pooling has amounted to something more than passive non-consent, interests have been excluded from the unit even though the correlative rights of the owners of those interests were impaired by their own position.[35] In some cases where it appeared that upon reconsideration the non-consenting interest would wish to join the unit, a non-standard unit was established subject to the condition that the non-consenting interest could join at a later time.[36]

In some cases, however, substantial interests have been involuntarily pooled over their vehement protestations. In one case,[37] the working interest owner in an eighty-acre tract sought the compulsory pooling of the unleased interest in an adjoining eighty-acre tract to form a standard 160-acre gas proration unit. The pooling application was brought after all of the owners of the undivided, unleased interest had been offered, and had refused, the opportunity to lease or to join the unit voluntarily. At the hearing of the pooling application, the owner of an undivided 17/30ths interest in the unleased eighty acres appeared and actively protested the inclusion of his interest in the proposed unit. The protest may have been due to the protestant's misconception of the effect of pooling, which was fancied as some form of uncompensated confiscation, but may have had some reasonable basis in as much as the eighty-acre tract being involuntarily pooled had better productive potential than the tract owned by the applicant. The applicant proposed to locate the unit well on the protestant's land after a pooling order had been entered, but there was evidence showing that the entire 160 acres was productive of gas. There was also evidence that a well drilled on either eighty-acre tract as a non-standard unit would be uneconomical due to the proportionately decreased allowable it would receive, and no proposal was made by the applicant or the protestant to form two eighty-acre units.

This situation presented the problem of how to protect the correlative rights of everyone concerned and, at the same time, prevent the waste that might occur if the lands involved were not developed. The correlative rights of both the applicant and the protestant dictated that a well be drilled to prevent drainage by other wells in the reservoir, yet the rights of the protestant, as voiced by him, included the right to refuse to commit his acreage to the proposed unit.

Since there were other owners of unleased interests in the tract owned partially by the protestant, who had not voiced active non-consent to pooling, and since a well could not economically be drilled on an eighty-acre tract, the

35. See note 33 *supra*.

36. See, *e.g.*, El Paso Natural Gas Co., Case No. 986, Order No. R-737 (N.M. Oil Conservation Comm'n 1955).

37. Southern Union Prod. Co., Case No. 2249, Order No. R-1960 (N.M. Oil Conservation Comm'n 1961).

Commission ordered pooling as the solution best designed to protect the correlative rights of all affected parties.

The pooling order allowed the operator to withhold 110 per cent of the proceeds attributable to seven-eighths of the non-concerning interest until the pro rata share of well costs were paid, and required the operator to submit an itemized schedule of well costs to the Commission. The well was drilled and completed at a location on the protestant's eighty-acre tract with the full 160-acre unit dedicated to the well.

B. Non-consenting Royalty Interests

No discussion has been offered, so far, of the problems involved in pooling non-consenting royalty interests as such, considered apart from their recognition as a portion of an unleased interest. Many pooling cases considered by the Commission have been occasioned by non-consenting royalty interests. But few of these cases have presented any problem because in most of them, even though the royalty owner would not consent to voluntary pooling, no objection was made to compulsory pooling. There have been a few notable exceptions, however.

In one case,[38] the application for compulsory pooling was opposed by royalty owners on the grounds that (1) the Commission had no statutory authority to require the pooling of royalty interests, (2) pooling, whether voluntary or involuntary, was merely a lease-holding and contractual-avoidance device, and (3) since the oil pool involved was governed merely by temporary rules providing for eighty-acre proration units, and since the royalty owners intended to object to the establishment of permanent rules to that effect, the pooling of an eighty-acre unit would be prejudicial to their cause.

The Commission ordered pooling based on its standard finding that "denial of the subject application would deprive, or tend to deprive the mineral interest owners in the said eighty-acre tract of the opportunity to recover their just and equitable share of the crude petroleum oil or natural gas, or both, in the . . . Pool."[39]

The contention made in this case concerning the lack of statutory authority requiring the pooling of royalty interests had been anticipated but never raised directly in a previous case. Its basis lay in the use of the word "owner" in the pooling statute which is defined in another section of the conservation law in terms relating only to a working interest.[40]

The Commission managed to operate successfully under the original form of the pooling law, and in spite of the inadequacies that appeared no litigation

38. Cities Serv. Oil Co., Case No. 2101, Order No. R-1801 (N.M. Oil Conservation Comm'n 1960).

39. *Id.*, Finding No. 6.

40. N.M. Stat. Ann. § 65-3-29(e) (1953).

resulted. In 1961, however, the law was revised to clarify the power of the Commission and to remedy some of the problems which threatened its effectiveness.[41]

41.

When two [2] 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 commission, 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 [affecting] 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 commission shall make definite provision as to any owner, or owners, who elects not to pay his proportionate share in advance for the pro rata 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 fifty per cent [50%] of the nonconsenting working interest owner or owners' pro rata share of the cost of drilling and completing the well.

In the event of any dispute relative to such costs, the commission shall determine the proper costs after due notice to interested parties and a hearing thereon. The commission 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

II

THE 1961 AMENDMENT

A. Problems Solved by the Amendment

Under the new law the pooling of royalty interests and undivided working or unleased interests may be required. Also, when an unleased interest is pooled, seven-eighths of the interest is considered working interest and one-eighth is considered royalty interest to be paid free of costs. The proviso in favor of the small tract owner was written out of law, thereby eliminating an ever present threat to the effectiveness of the pooling law.

The Commission is specifically authorized to require pooling to prevent economic waste caused by the drilling of unnecessary wells—a basis for pooling previously recognized by the Commission but without clear statutory foundation.

The Commission is expressly required to provide for the withholding of proceeds from production attributable to a working interest which has not paid its share of well costs. Such costs are limited to actual costs including costs of supervision, as under the previous law, but costs may now be assessed for the risk involved in drilling up to an additional fifty per cent of the non-consenting working interest's share. A provision for interest charges was proposed, but not included in the revision.

B. Problems Created by the Amendment

The revised law eliminated many threats to the effectiveness of compulsory pooling, but it has not proved to be a panacea for all pooling problems. New problems have been created in the area of assessing charges for risk. The proper determination of supervisory costs continues to be a problem, and new questions have been posed concerning the nature of compulsory pooling which would have been applicable to the law before as well as after its revision.

Some confusion presently exists concerning the risk for which a charge may be made and added to a non-consenting interest's share of the development costs. The risk for which a charge properly may be made is, in the words of the statute, "the risk involved in the drilling of such well."[42] There are,

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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.

N.M. Stat. Ann. § 65-3-14(c) (Supp. 1961).

42. *Ibid.*

however, at least three forms of risk inherent in every oil or gas prospect: (1) the risk of encountering unusual and expensive mechanical problems in the drilling of the well, (2) the risk of a dry hole, and (3) the risk of obtaining an uneconomical well—a risk which may not be resolved for years and which depends on such factors as market demand and the ability of the operator of the well to make a successful technical evaluation of the reservoir.

It has been argued[43] that all three forms of risk should be considered in fixing costs. But it cannot be ascertained from Commission orders to date upon what basis risk is to be charged, because the specific issue has not been presented for determination. The standard Commission order finds merely, without amplification, that risk should be assessed at a certain percentage of well costs.[44]

One difficulty in assessing costs for risk as a percentage of well costs is that there is no actual relationship between the two items. Few would argue that risk should not be compensated for in some manner, however, and the assessment of such costs has found general acceptance in the industry as a percentage of drilling costs. It has been shown to the Commission by those seeking fifty per cent as a risk factor that in "arms-length" transactions, *i.e.*, communitization agreements, it is customary to provide a risk charge on "carried" interests of 100 per cent.[45] And such charges are occasionally 200[46] and even 300,[47] per cent of drilling costs.

It should be borne in mind that risk charges are made only against "carried" interests, *i.e.*, those working interests which elect to pay their proportionate share of costs out of the proceeds from production rather than in advance of the drilling of the well. Where a working interest owner refuses to pay his share of costs in advance of drilling, his share of costs must be paid by the remaining working interests participating in the well. This situation, which may result either from compulsory pooling or from agreement, causes the remaining working interests to assume the burden of having their capital tied up for years until well costs can be recovered as well as the burden of all of the risk involved in the drilling of the well. Without any provision in communitization agreements or in compulsory pooling orders which allows the participating working interests to charge the non-participating owners for interest on their

43. Southwest Prod. Co., Case Nos. 2415, 2416, 2446 and 2453 (N.M. Oil Conservation Comm'n 1962) (heard *de novo*).

44. See, *e.g.*, S. P. Yates, Case No. 2655, Order No. R-2339 (N.M. Oil Conservation Comm'n 1962), in which order the maximum factor of fifty per cent was allowed.

45. See Southwest Prod. Co., Case Nos. 2415, 2416, 2446 and 2453 (N.M. Oil Conservation Comm'n 1962).

46. Pan American Petroleum Corp., Case No. 2500, Order No. R-2226 (N.M. Oil Conservation Comm'n 1962).

47. *Ibid.*

proportionate share of drilling costs, it is apparent that some portion of the so-called risk charge should actually be considered a charge for interest. The exact amount of this charge cannot be fixed either before or after drilling since it must depend upon the length of time required for well costs to be recovered which, in turn, depends on many variable factors such as well reserves and market demand.

Therefore, much of the clamor for an adequate risk factor is due, at least in part, to a desire to be compensated for interest.[48] Viewed in this light, the fixing of risk charges by the Commission would amount to an adjustment of equities between participating and non-participating interests. If this is the aim of the Commission, independent consideration should be given to the two factors, risk and interest, and each must be assessed as realistically as possible.[49]

Practical difficulties encountered in assessing risk and interest as separate costs may justify the Commission's current practice, and it may be that additional legislation would be necessary to permit the assessment of interest charges as such. In any event, charges should be assessed in such a manner as to treat the non-consenting interest owner who must be pooled by compulsion the same, but no better, than his counterpart who voluntarily pooled his interest but elected to be "carried." Certainly, no incentive should be provided for an interest owner to refuse to join voluntarily in an agreement offering fair and equitable terms because he may obtain an advantage by being pooled by order of the Commission.

Another problem is that of assessing costs of supervision. The law provides that charges shall be made for supervision,[50] a term which, like "risk," may assume several forms. There are costs of supervision incurred in the drilling of a well, and, also, there are costs involved in supervising the well throughout its productive life.

Until recently, costs of supervision have been assessed by the Commission as an additional percentage of well costs.[51] No attempt to fix actual costs has been made in the Commission's orders.

If costs of supervision are to be considered as only those incidental to the drilling of the well, they might be reasonably related to well costs and assessed

48. In Oklahoma, interest may be recovered as an item of well costs, but only if the operator has actually paid the interest. See Wood Oil Co. v. Corporation Comm'n, 268 P.2d 878 (Okla. 1953).

49. There is no specific provision in the pooling law allowing a charge to be made for interest; there is, however, the general expression: "All orders effecting [affecting] such pooling . . . shall be upon such terms and conditions as are just and reasonable . . . ." N.M. Stat. Ann. § 65-3-14(c) (Supp. 1961).

50. *Ibid.*

51. See, *e.g.*, Order No. R-1883 (N.M. Oil Conservation Comm'n 1961), allowing ten per cent of well costs as an additional charge for supervision.

as a percentage. However, if costs of supervision are considered also to include operating costs over the life of the well, then they do not appear to be reasonably related to well costs.

The orders entered by the Commission in recent pooling cases indicate a change in its interpretation of the term "supervision." Costs now are fixed at a certain monthly figure,[52] and each non-consenting working interest is assessed with its proportionate share to be paid out of production. Thus it now appears that no consideration is being given to supervisory costs incurred in the drilling of the well, unless the Commission is recognizing that such costs may properly be included as well costs without being specifically recognized and authorized as such in the pooling order.[53]

Aside from those questions involving the allocation of costs, others have arisen concerning the compulsory pooling process. In a series of cases[54] arising after the 1961 revision of the pooling law, the nature and operation of compulsory pooling were considered anew with questions concerning the Commission's power and discretion in such matters.

Following hearings before an Examiner where it was shown that certain specified interests refused to join in a proration unit, the Commission entered its orders pooling those specific interests with the remainder of the working interest in the proposed unit owned by the applicant.[55] By specifying each interest to be pooled as to identity and amount of ownership, the Commission departed from its previous practice of pooling "all mineral interests" within the unit.[56]

These cases were taken before the full Commission on hearings *de novo* where legal, equitable and practical arguments were made for both methods of effecting compulsory pooling. In support of specifying the interests to be pooled, the argument was advanced that only in that way could the Commission be reasonably sure all interests being pooled had been given the opportunity to join, lease or sell upon fair terms. In support of pooling all interests, whatever they might be, it was argued that only in that way could the Commission be absolutely sure that its order would be effective to form the unit, since the possibility of error in identifying the ownership or the extent of an interest would always be inherent in the other manner. Further, it was argued, the nature of

52. See, *e.g.*, Order No. R-2068-B (N.M. Oil Conservation Comm'n 1962), fixing $75.00 per month as the cost of supervision.

53. May interest (the cost of money) also be considered a proper item of well cost and included as such by the operator without the express approval of the Commission? See note 49 *supra*.

54. Southwest Prod. Co., Case Nos. 2415, 2416, 2446 and 2453 (N.M. Oil Conservation Comm'n 1962).

55. Order Nos. R-2150, R-2151, R-2068-A and R-2152 (N.M. Oil Conservation Comm'n 1961).

56. See, *e.g.*, Order No. R-2027 (N.M. Oil Conservation Comm'n 1961).

the proceeding, being *in rem* rather than *in personam*, would dictate the method of effecting pooling.

As the result of the hearings *de novo*, the Commission entered its orders[57] which pooled "all mineral interests, whatever they may be"[58] in each unit, thereby recognizing the *in rem* nature of the proceeding. The orders were based, however, on findings that the applicant had made "diligent effort to identify and to locate all owners of interest in the proposed proration unit . . . ,"[59] that the applicant had made "fair and reasonable offers to lease, to obtain quit claim deeds, or to communitize with respect to each non-consenting interest owner whose identity and address [were] known . . . ,"[60] and that, in spite of these efforts, there remained non-consenting interests.[61]

By the inclusion of these findings in the pooling orders, it is apparent that the diligence of the applicant was a factor considered by the Commission in ordering pooling. To what extent an applicant might relax his leasing practices, his title search and his curative procedures and still obtain a compulsory pooling order has not been determined. The Commission has indicated, however, that it will demand at least "good faith" efforts in this regard, and that it will not allow compulsory pooling to be used as a substitute for prudent leasing practices.

The proposition has been urged that the Commission has no discretion in a pooling case—where there are non-consenting interests, they obviously "have not agreed,"[62] and the Commission must order pooling.[63] This view would deny the Commission the prerogative of refusing to order pooling if it found evidence of imprudent leasing practices; indeed, it would deny the Commission the right to inquire into the diligence of the applicant's efforts to form a unit by negotiated means. It would deny to the pooling procedure any equitable qualities, even though such procedure necessarily involves adjusting the rights and equities of the various interests.

Such arguments notwithstanding, the Commission considers itself endowed with equitable powers in pooling matters and continues to require a showing of diligent effort by the applicant before ordering pooling. It should be noted,

57. Order Nos. R-2150-A, R-2151-A, R-2068-B and R-2152-A (N.M. Oil Conservation Comm'n 1962).

58. *Id.*, para. 1.

59. *Id.*, Finding No. 3.

60. *Id.*, Finding No. 4.

61. *Id.*, Finding No. 5.

62. The pooling law provides: "Where, however, such owner or owners have not agreed to pool their interests . . . the commission . . . shall pool all or any part of such lands or interests or both in the spacing or proration unit as a unit." N.M. Stat. Ann. § 65-3-14(c) (Supp. 1961).

63. In accordance with this view, see Superior Oil Co. v. Foote, 214 Miss. 857, 59 So. 2d 85 (1952).

however, that in every case brought before the Commission upon an application for compulsory pooling, pooling eventually has been ordered.[64]

SUMMARY

From the foregoing discussion the reader may have become aware of the basic nature of compulsory pooling in New Mexico. He may also have become aware of certain inadequacies in the pooling law and its administration. Some of these inadequacies might be remedied by new approaches to the administration of the law, and others might be cured only by new legislation. One thing is certain: new problems will continue to arise and old problems will assume new forms. The solutions to these problems will continue to come from the petroleum industry and those charged with the administration of the law. If these problems are resolved by the application of equitable principles and by the determination, in each case, of the reasonableness of the compulsory pooling order toward all concerned, the compulsory pooling law, with its avowed purposes of avoiding the drilling of unnecessary wells, of protecting correlative rights and of preventing waste, should continue to serve the cause of petroleum conservation in New Mexico.

64. In some instances, applications for pooling were denied folowing an examiner hearing. But they were granted following hearing *de novo* before the Commission where it appeared that additional efforts to lease or communitize had been made in the interim. See, *e.g.*, Southwest Prod. Co., Case Nos. 2415, 2416, 2446 and 2453 (N.M. Oil Conservation Comm'n 1962).

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See Also Orders No. R-11663
R-11663-A
R-11663-C

11-2-01

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

IN THE MATTER OF THE APPLICATION OF
McELVAIN OIL & GAS PROPERTIES, INC.
FOR COMPULSORY POOLING,
RIO ARRIBA COUNTY, NEW MEXICO **CASE NO. 12635, *de novo***

Consolidated with:

IN THE MATTER OF THE APPLICATION OF
D.J. SIMMONS INC. FOR COMPULSORY POOLING,
RIO ARRIBA COUNTY, NEW MEXICO

CASE NO. 12705

ORDER NO. R-11663-B

ORDER OF THE DIVISION
DENYING MOTION TO DISMISS

BY THE DIVISION DIRECTOR:

THIS MATTER has come before the Division Director of the New Mexico Oil Conservation Division (hereinafter referred to as "the Director") on Motion to Dismiss filed herein by McElvain Oil & Gas Properties Inc. (hereinafter referred to as "McElvain"), opposed by D.J. Simmons Inc. (hereinafter referred to as "Simmons"), and the Director, being fully advised in the premises,

FINDS:

1. On March 13, 2001 McElvain filed an application for compulsory pooling of all interests from the base of the Pictured Cliffs formation to the base of the Mesaverde formation under the under S/2 of Section 25, Township 25 North, Range 3 West, NMPM, Rio Arriba County, New Mexico to form standard spacing and proration units for formations and/or pools spaced on 320 acres. The application was assigned case number 12635 by the Oil Conservation Division (hereinafter referred to as "the Division").

2. On July 12, 2001, Simmons filed an application for compulsory pooling all interests from the surface to the base of the Mesaverde formation under the E/2 of Section 25, to form standard spacing and proration units for formations and/or pools spaced on 320 acres. The application was assigned case number 12705 by the Division.

3. On September 24, 2001, the Division entered Order No. R-11663 in Case No. 12635 which, in pertinent part, ordered compulsory pooling of all uncommitted mineral interests from the base of the Pictured Cliffs formation to the base of the Mesaverde formation underlying the S/2 of Section 25, Township 25 North, Range 3 West, NMPM, Rio Arriba County, New Mexico, to form a standard 320-acre spacing unit.

4. On October 3, 2001 Simmons filed an application to have Case No. 12635 heard *de novo* by the New Mexico Oil Conservation Commission (hereinafter referred to as "the Commission"), and on October 16, 2001, because the applications sought compulsory pooling in the same section, the Director issued an order consolidating Case No. 12635 with Case No. 12705.

5. Both matters are scheduled for hearing before the Oil Conservation Commission on November 6, 2001.

6. On October 1, 2001, before the cases were consolidated, McElvain filed a Motion to Dismiss the application of Simmons, now before the Director as a preliminary matter to be addressed before commencement of the hearing.

7. As grounds for its Motion, McElvain seems to argue that Simmons' failure to develop definitive plans to drill a well, to propose the drilling of a well to working interest owners, to file an Application to Drill with the Division, to file an application to pool or otherwise act with due diligence to drill a well, requires the application be dismissed.

8. Simmons filed a response opposing the motion. Simmons argued that McElvain's Motion fails to present proper grounds for dismissal and that McElvain's motion urges prejudgment of the outcome of the *de novo* hearing. Simmons characterizes McElvain's arguments as based on principles of "first-come, first-served" rather than on more appropriate factors.

9. The Motion to Dismiss of McElvain is not well taken and should not be granted.

10. As noted, the principal grounds cited for dismissal appear to be the delay of Simmons to develop plans to drill, the failure to propose the well to working interest owners, the failure to file an APD with the Division, the failure to file a pooling application, and the failure to proceed with due diligence to drill a well.

11. The Oil and Gas Act provides, in pertinent part, that the Division may pool interests in favor of an interest owner where "... such separate owner, or owners ... has the right to drill has drilled or proposes to drill a well ..." NMSA 1978, § 70-2-17(C) (Repl. 1995). Thus, the Division may pool in favor of an interest owner in two distinct circumstances: (a) where an owner who has the right to drill has already drilled a well; or (b) where an owner who has the right proposes to drill a well.

12. It seems to be undisputed that Simmons has the right to drill in Section 25. *See e.g.* McElvain Exhibits 2, 3 and Simmons Exhibits 1, 2, 5, 8, hearing of May 17, 2001 (Case No. 12,635). Certainly no party has to date raised this as an issue and it does not appear to be raised in the Motion and Response.

13. Although testimony from the examiner's hearing of May 17, 2001, cited by McElvain in support of the Motion, may establish that as of May 17, 2001 Simmons had no immediate plans to drill, had not filed an application to drill and had not proposed the drilling of a well, the application of Simmons in Case No. 12705 demonstrates that the situation may have changed and a well may now in fact be proposed by Simmons. As Simmons points out in the response to the motion, Simmons has apparently only recently acquired its property in Section 15 and it may be unreasonable to expect Simmons to have taken these steps during a brief period of ownership.

14. Thus, the issue of proposal of a well is, at the very least, a fact issue and inappropriate for summary disposition.

15. McElvain's apparent argument that its earlier application and the Division's pooling order establish McElvain's position as a matter of law is defective. By virtue of the timely *de novo* filing, the application in Case No. 12635 is before the Commission. Such an argument might have credence if an order were entered by the Division and the time to apply for *de novo* review had expired, making the order permanent. Moreover, a decision by the Division or the Commission on a pooling application must be governed by the factors set forth in the Oil and Gas Act, including the avoidance of the drilling of unnecessary wells, the protection of correlative rights and the prevention of waste. NMSA 1978, § 70-2-17(C). Normally, a pooling decision cannot be made strictly on the basis of which party filed the first application. Any suggestion by McElvain that the case be decided on this basis should be rejected.

16. As a result of the foregoing, the Motion to Dismiss of McElvain should be denied.

IT IS THEREFORE ORDERED that the Motion to Dismiss Case No. 12705 is denied.

DONE at Santa Fe, New Mexico, on the 2nd day of November 2001.

STATE OF NEW MEXICO
OIL CONSERVATION DIVISION

LORI WROTENBERY
Director

MILLER, STRATVERT & TORGERSON, P.A.

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PLEASE REPLY TO SANTA FE

* NEW MEXICO BOARD OF SPECIALIZATION RECOGNIZED SPECIALIST IN NATURAL RESOURCES - OIL & GAS LAW
** NEW MEXICO BOARD OF SPECIALIZATION RECOGNIZED SPECIALIST IN REAL ESTATE LAW

November 1, 2001

HAND-DELIVERED

Ms. Florene Davidson
New Mexico Oil Conservation Division
1220 St. Francis Drive
Santa Fe, New Mexico 87505

Re: Case No. 12635 *De Novo*; Application of McElvain Oil and Gas Properties, Inc. For Compulsory Pooling, Rio Arriba County, New Mexico; and

Case No. 12705; Application of D. J. Simmons, Inc. for Compulsory Pooling, Rio Arriba County, New Mexico

Dear Ms. Davidson:

With this letter are three sets of the exhibits that will be presented by D. J. Simmons, Inc. at the Commission hearing on the above-referenced consolidated cases.

Very truly yours,

J. Scott Hall

JSH/kam
enclosures a/s

cc: Steve Ross, Esq.
Michael Feldewert

NEW MEXICO ENERGY, MINERALS and
NATURAL RESOURCES DEPARTMENT

GARY E. JOHNSON
Governor
Jennifer A. Salisbury
Cabinet Secretary

Lori Wrotenbery
Director
Oil Conservation Division

October 30, 2001

Via Facsimile

Michael Feldewert, Esq.
Holland & Hart and Campbell & Carr
P.O. Box 2208
Santa Fe, New Mexico 87504

J. Scott Hall
Miller, Stratvert & Torgerson, P.A.
P.O. Box 1986
Santa Fe, New Mexico 87504-1986

Re: Case No. 12635, Application of McElvain Oil and Gas Properties Inc., *de novo*
Case No. 12705, Application of D.J. Simmons Inc.

Counsel,

Mr. Hall brought to my attention that my previous letter required that exhibits and Pre-hearing statements be delivered to Ms. Davidson no later than "Thursday, October 30." That reference was intended to refer to "Thursday, November 1." My sincere apologies for the confusion.

As always, if you have any questions, please do not hesitate to give me a call at 476-3451.

Sincerely,

Stephen C. Ross
Assistant General Counsel

Cc: Florene Davidson, Commission Secretary

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GARY E. JOHNSON
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Director
Oil Conservation Division

October 23, 2001

Via Facsimile and First Class Mail

Michael Feldewert, Esq.
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P.O. Box 2208
Santa Fe, New Mexico 87504

J. Scott Hall
Miller, Stratvert & Torgerson, P.A.
P.O. Box 1986
Santa Fe, New Mexico 87504-1986

Re: Case No. 12635, Application of McElvain Oil and Gas Properties Inc., *de novo*
Case No. 12705, Application of D.J. Simmons Inc.

Dear Counsel,

The Commission members have requested that copies of each exhibit which is to be offered during the hearing of this matter be provided to the Commission Secretary no later than one week prior to the date set for hearing in this matter. As the matter is now set for hearing on November 6, exhibits should be submitted to Florene Davidson no later than Wednesday, November 1. If an agreed continuance results in the matter being set in a subsequent month, exhibits should be submitted no later than one week prior to the re-scheduled hearing.

It would also helpful if you could provide a more detailed statement of your positions in the pre-hearing statement than is customary.

The Commission members believe that review of detailed pre-hearing statements and the documentary evidence to be offered will help them to be better prepared for the issues and testimony. As always, if you have any questions, please do not hesitate to give me a call at 476-3451.

Sincerely,

Stephen C. Ross
Assistant General Counsel

Cc: Florene Davidson, Commission Secretary

R-11663
R-11663-B
R-11663-C
10-23-01

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

IN THE MATTER OF THE APPLICATION OF McELVAIN OIL & GAS PROPERTIES, INC. FOR COMPULSORY POOLING, RIO ARRIBA COUNTY, NEW MEXICO **CASE NO. 12635, *de novo***

Consolidated with:

IN THE MATTER OF THE APPLICATION OF D.J. SIMMONS INC. FOR COMPULSORY POOLING, RIO ARRIBA COUNTY, NEW MEXICO

CASE NO. 12705
ORDER NO. R-11663-A

ORDER OF THE DIVISION DENYING MOTION FOR STAY OF DIVISION ORDER R-11663

BY THE DIVISION DIRECTOR:

THIS MATTER, having come before the Division Director of the New Mexico Oil Conservation Division (hereinafter referred to as "the Director") pursuant to Rule 1220(B) of the Rules and Regulations of the Oil Conservation Division, 19 NMAC 15.N.1220(B) (7-15-99), on motion of D.J. Simmons Inc. (hereinafter referred to as "Simmons") for stay of Division Order No. R-11663, which motion was opposed by McElvain Oil & Gas Properties Inc. (hereinafter referred to as "McElvain"), and the Director, being fully advised in the premises,

FINDS:

1. On September 24, 2001 the Oil Conservation Division (hereinafter referred to as "the Division") entered Order No. R-11663 in Case No. 12635 which, in pertinent part, ordered pooling of all uncommitted mineral interests from the base of the Pictured Cliffs formation to the base of the Mesaverde formation underlying the S/2 of Section 25, Township 25 North, Range 3 West, NMPM, Rio Arriba County, New Mexico, to form a standard 320-acre spacing unit within that vertical extent, which at present includes only the Undesignated Blanco-Mesaverde Pool.

2. On October 3, 2001 Simmons filed an application to have the matter heard *de novo* by the New Mexico Oil Conservation Commission (hereinafter referred to as "the Commission").

3. On October 16, 2001, the Director issued an order consolidating Case No. 12635 with Case No. 12705, a competing application for compulsory pooling filed by Simmons before the Division.

4. On October 5, 2001, Simmons, citing "Memorandum No. 3-85" of the Division, filed a motion to stay Order No. R-11663. As grounds for the motion, Simmons argued that McElvain's argument that risk mitigation was a proper rationale for compulsory pooling pursuant to NMSA 1978, § 70-2-17 (Repl. 1995) was erroneous. Simmons also argued that harm would result from denial of a stay, that McElvain would not be prejudiced by entry of a stay because exploration is not imminent, that rig scheduling is not an issue for McElvain, that McElvain retains the right to re-complete the well in question and dedicate the W/2 to it, and, citing McElvain's two requests for continuances, that McElvain was in no hurry to develop the acreage.

5. McElvain filed a response opposing the motion. McElvain, citing the transcript of the proceedings before the Division Examiner, argued that waste is not threatened and no party would be impaired were the motion denied.

6. Rule 1220(B) of the Rules and Regulations of the Oil Conservation Division, 19 NMAC 15.N.1220(B) (7-15-99), permits the Director to enter a stay of a Division order "... if a stay is necessary to prevent waste, protect correlative rights, protect public health and the environment or prevent gross negative consequences to any affected party ..." Simmons' citation to Memorandum No. 3-85 is erroneous; that memorandum is of no force and effect, having been superceded by Rule 1220.

7. Simmons failed to establish that waste is threatened, that correlative rights are in jeopardy, or that gross negative consequences to any party would result from the Division's order.

8. Simmons alluded to the possibility of "harm" if the Motion for Stay is not granted, but did not develop the argument and a review of the record of the proceedings does not support the assertion. Generalized concerns or suspicions are insufficient to establish entitlement to a stay under Rule 1220(B).

9. Simmons' argument that risk mitigation is not a proper rationale for compulsory pooling pursuant to § 70-2-17 is really an argument on the merits of this matter, which will be presented to the Commission during the hearing. This argument has little relevance to the present inquiry, which is limited to factors set out in Rule 1220(B). Similarly, Simmons' argument that McElvain is free to re-complete the well in question and dedicate the W/2 to that well is an argument that goes to the ultimate issue

in this matter, of little relevance to the present inquiry. If these arguments are intended to establish justification for a stay pursuant to Rule 1220(B), the Motion fails to make any discernable connection to the prevention of waste, the protection of correlative rights or the prevention of gross negative consequences to any affected party.

10. The argument presented by Simmons that McElvain *would not* be prejudiced by entry of a stay seems to argue against a stay rather than in favor of one. See Rule 1220(B)(" ... if a stay is necessary to ... to prevent gross negative consequences to *any* affected party ..."). Likewise, Simmons' argument that McElvain's use of continuances demonstrated it was in no hurry to develop the acreage also suggests that no party is likely to be affected by Order No. R-11663 until the Commission has an opportunity to hear this matter.

11. As a result of the foregoing, the Motion to Stay of Simmons should be denied.

IT IS THEREFORE ORDERED that the Motion to Stay Division Order No. R-11663 filed herein by D.J. Simmons Inc. is denied. Order No. R-11663 shall remain in force until the Commission has had occasion to issue an Order in this matter.

DONE at Santa Fe, New Mexico, on the 23rd day of October 2001.

SEAL

STATE OF NEW MEXICO
OIL CONSERVATION DIVISION

Lori Wrotenbery

LORI WROTENBERY
Director

NEW MEXICO ENERGY, MINERALS and NATURAL RESOURCES DEPARTMENT

GARY E. JOHNSON
Governor
Jennifer A. Salisbury
Cabinet Secretary

Lori Wrotenbery
Director
Oil Conservation Division

October 16, 2001

Via Facsimile and First Class Mail

J. Scott Hall
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Michael Feldewert
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P.O. Box 2208
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Re: Case No. 12635, Order No. R-11663; In the matter of the Application of McElvain Oil & Gas Properties, Inc. for compulsory pooling, Rio Arriba County, New Mexico

Case No. 12705; In the matter of the Application of D.J. Simmons Inc. for compulsory pooling, Rio Arriba County, New Mexico

Counsel,

Case No. 12635 is before the New Mexico Oil Conservation Commission *de novo* on request of D.J. Simmons. In addition, Case No. 12705 is before the Division on application of D.J. Simmons. The cases involve competing applications in the same section. Hearing the cases separately would be wasteful of the resources of the Division and the parties, not to mention raising the possibility of inconsistent results and procedural confusion.

Therefore, Case No. 12705 is hereby referred to the New Mexico Oil Conservation Commission and consolidated for hearing pursuant to N.M.S.A. 1978, § 70-2-6(B). Case No. 12605 will be heard along with Case No. 12705.

A Motion to Dismiss and a Motion to Stay have been filed. Orders disposing of those motions will be issued in due course.

Sincerely,

Lori Wrotenbery

Lori Wrotenbery, Director
Oil Conservation Division

Cc: Stephen C. Ross, Commission Counsel
David Brooks, Division Counsel
Richard Ezeanyim, Chief Engineer
Florene Davidson, Commission Secretary

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

IN THE MATTER OF THE APPLICATION OF
D. J. SIMMONS, INC. FOR COMPULSORY POOLING,
RIO ARRIBA COUNTY, NEW MEXICO CASE NO. 12705

D. J. SIMMONS'S RESPONSE TO McELVAIN'S MOTION TO DISMISS

McElvain Oil and Gas Properties, Inc. Motion to Dismiss the Application of D. J. Simmons, Inc. is inappropriate for two separate but equally compelling reasons: (1) It seeks to prevent D.J. Simmons from having a full and fair hearing on its Application, and (2) does not present adequate grounds to support the relief requested. McElvain's motion should be denied. In addition, in order to avoid a duplicative Division hearing, Case No. 12705 and Case No. 12635 should be simultaneously heard by the Commission at the November 9, 2001 hearing docket. Alternatively, this case should be continued until the *de novo* proceedings in Case No. 12635 are completed.

BACKGROUND

In this case, the Applicant, D. J. Simmons, Inc., seeks the compulsory pooling of the Blanco-Mesaverde formation underlying the E/2 of Section 25, T-25-N, R-3-W, NMPM, in Rio Arriba County. D. J. Simmons proposes to dedicate the E/2 of Section 25 to its Bishop Federal 25 No. 1 well to be drilled at a standard location in the NE/4 of the section. In addition to testing the Blanco-Mesaverde formation, D. J. Simmons also plans test the Chacra/Lewis and the Gallup-Dakota formations.

There is also presently pending before the New Mexico Oil Conservation Commission D. J. Simmons's Application for Hearing De Novo in the matter of

McElvain's application for the compulsory pooling of the S/2 of Section 25, T-25-N. R-3-W. (Case No. 12635; Order No. R-11663, *de novo*). As the two cases involve competing applications affecting the SE/4 of the same section, D. J. Simmons filed a request for a temporary stay of the pooling order in Case No. 12635 pending the completion of the *de novo* proceedings. Simmons has also requested that the hearing on its Application in this case be continued until the *de novo* proceedings in Case No. 12635 are completed. To date, McElvain has presented no evidence that it would be prejudiced by a stay.

POINTS AND AUTHORITIES

McElvain's Motion to Dismiss Case No. 12705 is premature. Moreover, it presents no adequate grounds to support an outright dismissal.

McElvain seeks to short-circuit these proceedings by pre-supposing the outcome the *de novo* appeal in Case No. 12635. Until the Commission has resolved the issues in the *de novo* proceeding, McElvain can neither presume that its pooling order will stand, nor that Simmons is precluded from pursuing its own Application. By circumventing the regular processes of the Division and the Commission, McElvain would prevent Simmons from having a full and fair hearing on its legitimately filed application. Yet, it is understandable why McElvain would seek to pre-empt any further exposure of the numerous issues involved in these two cases. McElvain would rather avoid having the Division hear evidence on such issues as (1) McElvain's delays in developing its acreage, (2) waste, and (3) the propriety of developing an E/2 unit.

McElvain's Delays. In its motion, McElvain argues that it is entitled to a compulsory pooling order under the theory of "first-come, first served". McElvain

derides the fact that Simmons's compulsory pooling application was filed some four months after its own. Yet, McElvain fails to mention the fact that the record in Case No. 12635 established that Simmons acquired its acreage interest only last year while McElvain has held its W/2 acreage since at least 1987. McElvain avoids explaining why, on the one-hand, it has put-off its simple re-completion operation and delayed any development of the Blanco-Mesaverde reserves for over fourteen years while, on the other hand, Simmons is ready to proceed with a new-drill in only a few months time.

Waste. In Case No. 12635, McElvain seeks to pool only the Blanco-Mesaverde formation in the SE/4 of Section 5. It has eschewed any plans to develop either the Chacra/Lewis or the Gallup-Dakota reserves underlying the acreage it seeks to pool. Simmons, on the other hand, plans to develop the Chacra/Lewis and the Gallup-Dakota in conjunction with the Blanco-Mesaverde. Notably, in its Motion to Dismiss, McElvain represents that it "tested" the Gallup-Dakota in the SW/4 of Section 25 (by its former Wynona No. 1 well, now named the Naomi Com No. 1) and found it to be "non-productive".[1] This is not true. The record in Case No. 12635 established that the Wynona No. 1 produced 144 million cubic feet of gas and 8,893 barrels of oil. In Case No. 12705, Simmons will present evidence consistent with that presented in Case No. 12635, that the potential for economically recoverable Gallup-Dakota reserves underlying the SE/4 exists; potential which McElvain plans to ignore, thus making the development and production of those reserves problematic. Simmons's proposal, unlike McElvain's, would avoid the waste of the Gallup-Dakota reserves underlying the SE/4.

[1] McElvain Motion to Dismiss, Pg. 2, footnote 2

E/2 Development. Simmons intends to present evidence establishing how the development of the 160 acre Lewis/Chacra and Gallup-Dakota reservoirs in conjunction with the 320 acre Blanco-Mesaverde reservoir on an E/2 stand-up proration unit basis is justified by, among other reasons, (1) the geology, (2) prevailing drainage patterns, and (3) the established equities in the affected acreage. McElvain, on the other hand, would be hard-put to overcome such a showing given, among other things, (1) the inability of the Naomi Com No.1 recompletion, to adequately drain Blanco-Mesaverde reserves from the SE/4 from its present unorthodox location 450 feet from the west line of the section in Unit L, or (2) why it would be inequitable to create an E/2 proration unit when it already owns 100% of the W/2.

These issues, to the extent they specifically concern the lands located in the E/2 of Section 25, were not directly at issue in Case No. 12635. All of these issues have merit and they deserve to be heard. None of them are moot.

Correspondingly, McElvain's motion for outright dismissal is inappropriate and should be denied. Instead, it makes more sense to combine Case No. 12705 with Case No. 12635 for the simultaneous presentation of full evidence in both cases at the Commission's November 9, 2001 hearing docket. Such a course of action is authorized by the Division's Rule 1216(b) and would result in a quicker, and ultimately more efficient resolution of the dispute.

Respectfully submitted,

MILLER, STRATVERT & TORGERSON, P.A.

By _____

J. Scott Hall
Attorneys for D. J. Simmons, Inc.
Post Office Box 1986
Santa Fe, New Mexico 87504-1986
(505) 989-9614

Certificate of Mailing

I hereby certify that a true and correct copy of the foregoing was mailed to counsel of record on the 16th day of October, 2001, as follows:

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_____

J. Scott Hall

10-16-01

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

IN THE MATTER OF THE APPLICATION
OF McELVAIN OIL & GAS PROPERTIES, INC.
FOR COMPULSORY POOLING,
RIO ARRIBA COUNTY, NEW MEXICO **CASE NO. 12635**

McELVAIN'S RESPONSE IN OPPOSITION
TO REQUEST FOR STAY OF ORDER NO. R-11663

McElvain Oil and Gas Properties, Inc. ("McElvain") files this response in opposition to the request by D. J. Simmons to stay Order R-11663.

1. On March 13, 2001, McElvain filed its compulsory pooling application. After requests for continuances by both parties, McElvain's pooling application was heard by Division Examiner Michael Stogner on May 17, 2001.

2. D. J. Simmons appeared at the May 17th hearing in opposition to McElvain's pooling application and presented testimony from a landman, a geologist and an engineer. D. J. Simmons asserted that an E/2 spacing unit should be preserved in Section 25 for up-hole gas completions in the Blanco-Mesaverde Pool in the event D. J. Simmons drilled Gallup-Dakota oil wells in the NE/4 and the SE/4 of Section 25.[1]

3. At the May 17th hearing, Edward B. Dunn (a landman for D. J. Simmons) testified that while D. J. Simmons had discussed plans to drill two Gallup-Dakota oil wells in the E/2 of Section 25, D. J. Simmons had no definitive plans for drilling the wells, had not sent any drilling proposals to the working interest owners in the E/2 of Section 25, and had filed no APDs with the Division for any

[1] The West Lindrith Gallup-Dakota Oil Pool is developed on 160-acres under the special pool rules issued by the Division.

well in the E/2 of Section 25. Tr. at 68-70, 77.[2] Mr. Dunn also testified that the special pool rules for the Blanco-Mesaverde Gas Pool would allow a Gallup-Dakota oil well in the NE/4 or the SE/4 of Section 25 to be re-completed, if necessary, as an in-fill gas well in the Mesaverde formation. Tr. at 70-71. Mr. Dunn also observed that D. J. Simmons' acreage position in the SE/4 is similar to that held by Dugan Production Corporation, that Dugan supported McElvain's application, and that it was reasonable for the parties in the S/2 "to have the financial risk [of a Mesaverde completion] reduced by the use of an existing wellbore and to share the risk among several parties." Tr. at 72-73.

4. At the end of the 3.5 hour hearing, Examiner Stogner made the following observations about D. J. Simmons' absence of due diligence:

> I've been involved in those instances where you have had dual applications for compulsory pooling in which the orientation was questioned and one was taken over the other or they were reoriented because one necessarily -- *but I don't have that in this instance*.....You're wanting them [McElvain] to form a standard standup proration unit, but *there hasn't been any like application file by D. J. Simmons or, for that matter, due diligence to drill a well.* They say they have, but there hasn't been anything written. They haven't talked to---or put anything in writing. So yeah, I understand that downhole commingling would have made it easier. Yes, there could be some precedent set on that. *But given where we are now, why should I reorient or deny this and force them [McElvain] to form a standard standup 320-acre proration unit simply because D. J. Simmons decided to drag their feet on something?*

Tr. at p. 129-30. Examiner Stogner took McElvain's application under advisement and allowed the attorney for D. J. Simmons to submit a post-hearing brief on the matter.

5. On July 12, 2001, almost <u>two months</u> after the hearing on McElvain's application, <u>four months</u> after McElvain filed its pooling application for a S/2 spacing unit, and <u>eight months</u> after McElvain first proposed its re-entry project to the working interest owners, D. J. Simmons filed an

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[2] Indeed, the West Lindrith Gallup-Dakota Oil Pool was tested in the SW/4 of Section 25 and found to be non-productive. *See* Order R-11663 at p. 1, paragraph 4.

application with the Division seeking to establish an E/2 orientation for a Mesaverde well. *See* Case No. 12705. However, McElvain has moved to dismiss the application in Case No. 12705 as untimely and D. J. Simmons has asked that its application be stayed pending its *de novo* appeal of Order R-11663.

6. On September 24, 2001, the Division issued Order R-11663 granting McElvain's pooling application and forming a S/2 spacing unit in Section 25. The Division found that "the cumulative evidence presented in this matter serves to support McElvain's position." *See* Order R-11663 at p. 2, paragraph 10. The Division thus rejected D. J. Simmons' claims at the hearing that the drainage patterns in Section 25 supported stand-up units, or that McElvain's pooling order would prevent development of the Gallup-Dakota formation. *Id.*

7. After all of the delay, testimony, briefing and consideration that finally resulted in Order R-11663, D. J. Simmons now asks the Division to stay that Order and further delay McElvain's re-entry project.

8. Rule 1220(B) of the Rules and Regulations of the Oil Conservation Division, 19 NMAC 15.N.1220(B) (7-15-99), permits the Director to enter a stay of a Division order "...if necessary to prevent waste, to protect correlative rights, to protect fresh water, or to prevent gross negative consequences to any affected party." None of these circumstances exist here. The other working interest owners in the SE/4 of Section 25 support McElvain's proposal to re-enter an existing well in the SW/4 of Section 25 and test the Mesaverde formation with a S/2 spacing unit. Order R-11663 does not prevent D. J. Simmons from drilling a Gallup-Dakota oil well in the NE/4 or the SE/4 of Section 25, nor does it prevent any such oil well from being recompleted as an in-fill gas well in the Mesaverde formation, if necessary. As a result, there is no threat of waste, no impairment

of correlative rights and no gross negative consequences to any affected party.

WHEREFORE McElvain requests that the Division deny D. J. Simmons' request to stay Order No. R-11663.

Respectfully submitted,

HOLLAND & HART LLP
AND
CAMPBELL & CARR

By: _____
Michael H. Feldewert
Post Office Box 2088
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(505) 988-4412

ATTORNEYS FOR McELVAIN OIL AND GAS PROPERTIES, INC.

Certificate of Service

The undersigned hereby certifies that on October 16, 2001 a true copy of the foregoing document was hand-delivered to the following:

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_____
Michael H. Feldewert

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

IN THE MATTER OF THE APPLICATION
OF McELVAIN OIL & GAS PROPERTIES, INC.
FOR COMPULSORY POOLING,
RIO ARRIBA COUNTY, NEW MEXICO CASE NO. 12635

REQUEST FOR STAY OF ORDER NO. R-11663

D. J. Simmons, Inc., ("Simmons"), through its counsel and pursuant to Division Memorandum No. 3-85, requests the Division enter its order temporarily staying Order No. R-11663. The grounds for staying the Division's compulsory pooling order are as follow:

1. Presently pending before the agency are two conflicting applications that both seek the compulsory pooling of working interests in the **SE/4** of Section 25, T-25-N, R-3-W, NMPM, one for the creation of a **S/2** unit in this case, and the other for the creation of an **E/2** unit in Case No. 12705 (Application of D. J. Simmons, Inc. for Compulsory Pooling, Rio Arriba County, New Mexico.) The Division entered Order No. R-11663 in this case on September 24, 2001, and the matter is currently pending a hearing *de novo* pursuant to Simmons's application.

2. The Applicant in this proceeding, McElvain Oil and Gas Properties, Inc., ("McElvain"), owns 100% of the oil and gas leasehold working interests underlying the **W/2** of Section 25, T-25-N, R-3-W, NMPM, upon which its Naomi Com No. 1 well was drilled at a previously approved unorthodox well location 1650' FSL and 450' FWL. McElvain proposes to re-enter and re-complete its P&A'd well in the Blanco-Mesaverde pool. However, rather than logically dedicate its pre-existing 320 acre **W/2** stand-up unit to the well, McElvain instead applied to the Division to force pool working interests in

the **SE/4** of the section in order to create a new **S/2** lay-down unit. McElvain does not plan to develop the Gallup-Dakota reserves underlying the **SE/4.**

3. Simmons opposed McElvain's application for the reasons, among others, that given the availability of a pre-existing **W/2** unit, the compulsory pooling proceeding would result in the unnecessary expenditure of time, effort and legal expense and would impair Simmons's ability to develop the Gallup-Dakota reserves it owns in the **SE/4** of Section 25 in conjunction with a Blanco-Mesaverde production unit consisting of the **E/2** of the same section.

4. Simmons also opposed McElvain's application for the reasons that (1) the prevailing north-south fracture drainage patterns in the area supports the creation of a **W/2** unit, (2) the Naomi Com No. 1 well, at its unorthodox location encroaching on the southwest corner of the Section is not situated to economically or efficiently drain any of the Blanco-Mesaverde reserves from the **SE/4**, and (3) because McElvain failed to meet the applicable legal standards of "good faith" in negotiating for the voluntary participation of the non-joined working interests.

5. At the May 17, 2001 examiner hearing on its Application, McElvain's witnesses were asked to explain why it was necessary to force pool the interests of the other owners in the **SE/4** when the company already controlled 100% of the working interest in the **W/2** of the section. Significantly, McElvain's witnesses represented that they sought the pooling of the **SE/4** in order to force the other working interest owners there to bear a portion of the economic risk associated with the proposed re-entry and re-completion operation. At the hearing, McElvain's witnesses acknowledged that the economic "risk mitigation" scheme was the "primary" motivation behind their pooling

application. By so doing, McElvain avoids having to assume one-hundred percent of the costs and risk of its recompletion were it to dedicate its more logical **W/2** unit to the well.

6. The invocation of the State's considerable police powers to force pool another owner's working interests for the purpose of mitigating an operator's risk is not among the specific circumstances authorized in the Division's compulsory pooling statute, NMSA 1978 §70-2-17. As such, the use by operators of the Division's compulsory pooling authority in such a manner presents a significant policy question for consideration by the Commission. If it is eventually determined that the use of the compulsory pooling for such a purpose is wrong, then the harm caused by a denial of a stay will significantly outweigh any that would result if an interim stay is granted.

7. McElvain will not be prejudiced by the stay of Order No. R-11663: (1) None of the lease acreage underlying the **W/2** or the **SE/4** of Section 25 is subject to imminent expiration. (2) As the re-entry and re-completion of the Naomi Com No. 1 well involves only the use of a readily available work-over rig, McElvain will not have any drilling rig scheduling problems. (3) McElvain will not lose the opportunity to drill (or, more accurately, re-complete) as it will continue to have the ability to dedicate the **W/2** of the section to its well. It should also be noted that McElvain originally asked that its Application be set for the April 5th examiner docket, but then immediately sought its continuance on two subsequent occasions.

8. A proposed form of Order of Stay is enclosed with this Request.

WHEREFORE, D. J. Simmons, Inc. requests the Division enter its order temporarily staying Order No. R-11663 pending the conclusion of the *de novo* proceedings before the New Mexico Oil Conservation Commission in this matter.

Respectfully submitted,

MILLER, STRATVERT & TORGERSON, P.A.

By _____

J. Scott Hall
Attorneys for D. J. Simmons, Inc.
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Certificate of Mailing

I hereby certify that a true and correct copy of the foregoing was mailed to counsel of record on the 4th day of October, 2001, as follows:

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_____

J. Scott Hall

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

IN THE MATTER OF THE APPLICATION
OF McELVAIN OIL & GAS PROPERTIES, INC.
FOR COMPULSORY POOLING,
RIO ARRIBA COUNTY, NEW MEXICO CASE NO. 12635

TEMPORARY STAY OF ORDER

BY THE DIVISION:

This matter came before the Division pursuant to the Request For Stay Of Order No. R-11663 filed on behalf of D. J. Simmons, Inc. on October 4, 2001.

NOW, on this ___ day of October, 2001, the Division Director, being duly advised,

FINDS THAT:

The Request For Stay is well-taken and should be granted.

IT IS THEREFORE ORDERED THAT:

Order No. R-11663 is stayed pending the conclusion of the *de novo* proceedings before the New Mexico Oil Conservation Commission in this matter.

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

STATE OF NEW MEXICO
OIL CONSERVATION DIVISION

LORI WROTENBERY
Director

SEAL

MILLER, STRATVERT & TORGERSON, P.A.
LAW OFFICES

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* NEW MEXICO BOARD OF SPECIALIZATION RECOGNIZED SPECIALIST IN NATURAL RESOURCES - OIL & GAS LAW
** NEW MEXICO BOARD OF SPECIALIZATION RECOGNIZED SPECIALIST IN REAL ESTATE LAW

October 15, 2001

VIA FACSIMILE & U.S. MAIL

Lori Wrotenbery, Director
New Mexico Oil Conservation Division
1220 St. Francis Drive
Santa Fe, New Mexico 87505

Re: NMOCD Case No. 12705; Application of D. J. Simmons, Inc. for Compulsory Pooling, Rio Arriba County, New Mexico

Dear Ms. Wrotenbery:

By the above-referenced Application, D. J. Simmons, Inc. seeks the compulsory pooling of the Blanco-Mesaverde formation underlying the E/2 of Section 25, T-25-N, R-3-W, NMPM, in Rio Arriba County. In addition, presently pending before the New Mexico Oil Conservation Commission is the Application of McElvain Oil and Gas Properties, Inc. for the compulsory pooling of the Blanco-Mesaverde formation underlying the S/2 of Section 25 (Case No. 12635; Order No. R-11663 *de novo*). As the two cases involve competing applications affecting the SE/4 of the same section, on October 4, 2001, D. J. Simmons filed a request for a temporary stay of the pooling order in Case No. 12635 pending the completion of the *de novo* proceedings. McElvain has not responded to the Request for Stay.

On behalf of D. J. Simmons, Inc. and pursuant to Division Rule 1216(2), we respectfully request that the Commission set Case No. 12705 for hearing by the Commission on November 9, 2001, simultaneously with the hearing *de novo* on Case No. 12635. Hearing both cases simultaneously will avoid unnecessarily duplicative proceedings and will be in the interests of efficiency and economy, not only for the parties, but for the Division and Commission as well.

Very truly yours,

J. Scott Hall

JSH/kam

Cc: John Byrom – D. J. Simmons, Inc.
David Brooks, Esq. - NMOCD
Steve Ross, Esq. - NMOCC
Michael Feldewert, Esq. - Counsel for McElvain Oil and Gas Properties

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

IN THE MATTER OF THE APPLICATION OF
D. J. SIMMONS, INC. FOR COMPULSORY POOLING,
RIO ARRIBA COUNTY, NEW MEXICO

Case No. 12705

McELVAIN'S MOTION TO DISMISS POOLING APPLICATION

McElvain Oil and Gas Properties, Inc. ("McElvain") hereby moves the Examiner for an order dismissing applicant's compulsory pooling application that seeks to pool interests in the **E/2** of Section 25, Township 25 North, Range 3 West to form a 320-acre spacing unit for a well in the Mesaverde formation (Undesignated Blanco Mesaverde Gas Pool). The SE/4 of said Section 25 not available for pooling since the **S/2** of Section 25 is already dedicated to McElvain's Naomi Well No. 1 to be recompleted in the Mesaverde formation in the SW/4 of Section 25 (Unit L). *See* Administrative Order NSL-4538 and Division Order No. R-11663 (Attachments 1 and 2). In support of this motion, McElvain states:

1. On November 10, 2000, McElvain proposed by letter to re-enter an existing plugged and abandoned well in the SW/4 of Section 25 and attempt a completion in the Mesaverde formation at an unorthodox location for the Undesignated Blanco-Mesaverde Pool. McElvain proposed to dedicate the S/2 of Section 25 to this proposed re-entry and completion effort. D.J. Simmons did not propose any alternative development plan for Section 25 in response to McElvain's letter.

2. On December 29, 2000, the Division approved McElvain's unorthodox gas well location in the SW/4 of Section 25 for "a proposed 320-acre standard lay-down gas spacing and proration unit comprising the S/2 of Section 25." *See* Attachment 1.

3. On March 13, 2001, McElvain filed a compulsory pooling application to form a S/2 spacing unit for its proposed Naomi Well No. 1. *See* Case No. 12635. D.J. Simmons did not file a competing pooling application.

4. On May 17, 2001, Division Examiner Michael Stogner heard McElvain's compulsory pooling application. D.J. Simmons appeared at the hearing in opposition to McElvain's pooling application and presented testimony that stand-up spacing units should be formed for the Mesaverde formation in Section 25. D.J. Simmons asserted that an E/2 spacing unit should be preserved for up-hole gas completions in the Blanco-Mesaverde Pool in the event D.J. Simmons drilled Gallup-Dakota oil wells in the NE/4 and the SE/4 of Section 25.[1]

5. At the May 17th hearing, Edward B. Dunn (a landman for D.J. Simmons) testified that while D.J. Simmons had discussed plans to drill two Gallup-Dakota oil wells in the E/2 of Section 25, D.J. Simmons had no definitive plans for drilling the wells, had not sent out any drilling proposals to the working interest owners in the E/2 of Section 25, and had filed no APDs with the Division for any well in the E/2 of Section 25. Tr. at 68-70, 77.[2] Mr. Dunn also testified that the special pool rules for the Blanco-Mesaverde Gas Pool would allow any Gallup-Dakota oil well in the NE/4 or the SE/4 of Section 25 to be re-completed, if necessary, as an in-fill gas well in the Mesaverde formation. Tr. at 70-71. Mr. Dunn also observed that D.J. Simmons' acreage position in the SE/4 is similar to that held by Dugan Production Corporation, that Dugan supported McElvain's application, and that it was reasonable for the parties in the S/2 "to have the financial risk [of a Mesaverde completion] reduced

[1] The West Lindrith Gallup-Dakota Oil Pool is developed on 160-acres under the special pool rules issued by the Division.

[2] Indeed, the West Lindrith Gallup-Dakota Oil Pool was tested in the SW/4 of Section 25 and found to be non-productive. *See* Attachment 2 (Order R-11663) at p. 1, paragraph 4.

by the use of an existing wellbore and to share the risk among several parties." Tr. at 72-73.

6. At the end of the 3.5 hour hearing, Examiner Stogner made the following observations about D. J. Simmons' lack of due diligence:

> I've been involved in those instances where you have had dual applications for compulsory pooling in which the orientation was questioned and one was taken over the other or they were reoriented because one necessarily -- *but I don't have that in this instance*.....You're wanting them [McElvain] to form a standard standup proration unit, but *there hasn't been any like application file by D.J. Simmons or, for that matter, due diligence to drill a well.* They say they have, but there hasn't been anything written. They haven't talked to---or put anything in writing. So yeah, I understand that downhole commingling would have made it easier. Yes, there could be some precedent set on that. *But given where we are now, why should I reorient or deny this and force them [McElvain] to form a standard standup 320-acre proration unit simply because D.J. Simmons decided to drag their feet on something?*

Tr. at p. 129-30. Examiner Stogner took McElvain's application under advisement and allowed the attorney for D.J. Simmons to submit a post-hearing brief on the matter.

7. On July 12, 2001, almost two months after the hearing on McElvain's application and four months after McElvain filed its pooling application for a S/2 spacing unit, D. J. Simmons filed the application in this case seeking an E/2 orientation for any Mesaverde well.

8. On September 24, 2001, the Division issued Order R-11663 granting McElvain's pooling application and forming a S/2 spacing unit in Section 25. *See* Attachment 2. The Division found that "the cumulative evidence presented in this matter serves to support McElvain's position." *Id.* at p. 2, paragraph 10. The Division thus rejected D.J. Simmons' claims at the hearing that the drainage patterns in Section 25 supported stand-up units, that McElvain's pooling order would prevent development of the Gallup-Dakota formation and thereby result in waste, and that McElvain had failed to engage in good faith efforts to obtain D.J. Simmons' voluntary participation in the well. *Id.*

WHEREFORE McElvain requests that the Examiner dismiss the application of D.J. Simmons for an order pooling the E/2 of Section 25, Township 25 North, Range 3 West, NMPM, on the grounds that the SE/4 of this section is dedicated to McElvain's Naomi Well No. 1 and may not now be dedicated to D.J. Simmons' proposed spacing unit in the E/2 of this section.

Respectfully submitted,

HOLLAND & HART LLP
AND
CAMPBELL & CARR

By: _____
Michael H. Feldewert
Post Office Box 2088
Santa Fe, New Mexico 87501
(505) 988-4412

ATTORNEYS FOR McELVAIN OIL AND GAS PROPERTIES, INC.

Certificate of Service

The undersigned hereby certifies that on October 1, 2001 a true copy of the foregoing document was mailed to the following:

J. Scott Hall
Miller, Stratvert & Torgerson, P.A.
Post Office Box 1986
Santa Fe, NM 87504-1986

_____
Michael H. Feldewert

NEW MEXICO ENERGY, MINERALS and NATURAL RESOURCES DEPARTMENT

GARY E. JOHNSON
Governor
Jennifer A. Salisbury
Cabinet Secretary

December 29, 2000

Lori Wrotenbery
Director
Oil Conservation Division

McElvain Oil & Gas Properties, Inc.
1050 17th Street - Suite 1800
Denver, Colorado 80265
Attention: John D. Steuble

Telefax No. (303) 893-0914

Administrative Order NSL-4538

Dear Mr. Steuble:

Reference is made to the following: (i) your application dated November 28, 2000; and (ii) the records of the New Mexico Oil Conservation Division ("Division") in Santa Fe and Aztec: all concerning McElvain Oil & Gas Properties, Inc.'s ("McElvain") request for an unorthodox Blanco-Mesaverde gas well location within a proposed 320-acre standard lay-down gas spacing and proration unit comprising the S/2 of Section 25, Township 25 North, Range 3 West, NMPM, Undesignated Blanco-Mesaverde Pool, Rio Arriba County, New Mexico, for the existing Naomi Com Well No. 1 (**API No. 30-039-24222**), located 1650 feet from the South line and 450 feet from the West line (Unit L) of Section 25.

It is our understanding that the Naomi Com Well No. 1 is currently completed in the West Lindrith-Gallup Dakota Oil Pool at a standard oil well location within a standard 160-acre oil spacing and proration unit comprising the SW/4 of section 25; however, this well is to be plugged back and recompleted up-hole into the Mesaverde formation upon issuance of this order. This location however is considered to be unorthodox pursuant to the "*Special Rules for the Blanco-Mesaverde Pool*," as promulgated by Division Order No. R-10987-A.

The application has been duly filed under the provisions of Division Rules 104.F and 605.B and the applicable rules governing both pools.

By the authority granted me under the provisions of Division Rule 104.F (2) the above-described unorthodox gas well location for the Naomi Com Well No. 1 is hereby approved.

Further, the aforementioned well and spacing unit will be subject to all existing rules, regulations, policies, and procedures applicable to prorated gas pools in Northwest, New Mexico.

Sincerely,

Lori Wrotenbery
Director

LW/MES/kv

cc: New Mexico Oil Conservation Division - Aztec
U. S. Bureau of Land Management - Farmington

ATTACHMENT 1

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

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

CASE NO. 12635
ORDER NO. R-11663

APPLICATION OF McELVAIN OIL & GAS PROPERTIES, INC. FOR COMPULSORY POOLING, RIO ARRIBA COUNTY, NEW MEXICO.

ORDER OF THE DIVISION

BY THE DIVISION:

This case came on for hearing at 8:15 a.m. on May 17, 2001, at Santa Fe, New Mexico before Examiner Michael E. Stogner.

NOW, on this 24th day of September, 2001, the Division Director, having considered the testimony, the record and the recommendations of the Examiner,

FINDS THAT:

(1) Due public notice has been given, and the Division has jurisdiction of this case and its subject matter.

(2) The applicant, McElvain Oil & Gas Properties, Inc. ("McElvain"), seeks an order pooling all uncommitted mineral interests from the base of the Pictured Cliffs formation to the base of the Mesaverde formation underlying the S/2 of Section 25, Township 25 North, Range 3 West, NMPM, Rio Arriba County, New Mexico, to form a standard 320-acre lay-down gas spacing and proration unit ("unit") for any pool developed on 320-acre spacing within that vertical extent, which presently includes only the Undesignated Blanco-Mesaverde Pool.

(3) The applicant proposes to re-enter its plugged and abandoned Wynona Well No. 1 (**API No. 30-039-24222**) (the "subject well"), which is to be redesignated the Naomi Well No. 1, and is located at an unorthodox gas well location (approved by Division Administrative Order NSL-4538, dated December 29, 2000) 1650 feet from the South line and 450 feet from the West line (Unit L) of Section 25.

(4) Division records indicate that the subject well was originally drilled in 1988 by McElvain to a depth of 8,113 feet and completed in the West Lindrith Gallup-Dakota Oil

Pool at a standard oil well location within a standard 160-acre oil spacing and proration unit for this oil pool comprising the SW/4 of Section 25.

(5) It is McElvain's intent to re-enter this well by removing the dry hole marker, drilling out six cement plugs, and completing it in the Mesaverde formation at an approximate depth of 5,970 feet as an initial gas well within the proposed 320-acre unit.

(6) Two or more separately owned tracts are embraced within this unit, and/or there are owners of royalty interests and/or undivided interests in oil and gas minerals in one or more tracts included in the unit which are separately owned.

(7) Applicant is an owner of an oil and gas working interest within the unit and therefore has the right to develop this acreage and recover gas underlying the same.

(8) There are interest owners in the proposed unit that have not agreed to pool their interests.

(9) D. J. Simmons, Inc., which owns 100% of the working interest that comprises a portion of a Federal lease (U. S. Government Lease No. NM-10589) consisting of 80 acres, being the N/2 SE/4 of Section 25, or 25% of the proposed 320-acre unit, appeared at the hearing in opposition to McElvain's application and presented evidence to support its position.

(10) However, the cumulative evidence presented in this matter serves to support McElvain's position; therefore, in order to avoid the drilling of unnecessary wells, protect correlative rights, prevent waste and afford to the owner of each interest in the unit the opportunity to recover or receive without unnecessary expense its just and fair share of hydrocarbons, this application should be approved by pooling all uncommitted mineral interests, whatever they may be, within this 320-acre unit.

(11) Applicant should be designated the operator of the Naomi Well No. 1 and of the proposed 320-acre unit.

(12) After pooling, uncommitted working interest owners are referred to as non-consenting working interest owners. ("Uncommitted working interest owners" are owners of working interests in the unit, including unleased mineral interests, who are not parties to an operating agreement governing the unit.) Any non-consenting working interest owner should be afforded the opportunity to pay its share of estimated well costs of the proposed well to the operator in lieu of paying its share of reasonable well costs out of production.

(13) The applicant requested that a risk penalty of 200 percent be assessed against all uncommitted mineral interest owners.

(14) Inasmuch as the subject well has already been drilled, the remaining risk should apply only to re-entry and recompletion operations to be conducted on the well. Further, based on precedent established in a number of other previous compulsory pooling cases involving the re-entry of existing wellbores, the risk penalty should be reduced to 100 percent.

(15) Any 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 100 percent thereof as a reasonable charge for the risk involved in re-entry and recompletion operations.

(16) Any 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.

(17) 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.

(18) Reasonable charges for supervision (combined fixed rates) should be fixed at $5,455.67 per month while re-entering and $545.55 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.

(19) Except as noted in Finding Paragraphs No. (15) and (18) 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.

(20) If the operator fails to commence re-entry and recompletion operations on the well to which the unit is dedicated on or before December 31, 2001, or if all the parties to this forced pooling reach voluntary agreement subsequent to the entry of this order, this order should become of no effect.

(21) The operator may request from the Division Director an extension of the December 31, 2001 deadline for good cause.

(22) The operator should notify the Division in writing of the subsequent voluntary agreement of all parties subject to the forced pooling provisions of this order.

IT IS THEREFORE ORDERED THAT:

(1) Pursuant to the application of McElvain Oil & Gas Properties, Inc. ("McElvain"), all uncommitted mineral interests from the base of the Pictured Cliffs formation to the base of the Mesaverde formation underlying the S/2 of Section 25, Township 25 North, Range 3 West, NMPM, Rio Arriba County, New Mexico, are hereby pooled to form a standard 320-acre lay-down gas spacing and proration unit ("unit") for any pool developed on 320-acre spacing within that vertical extent, which presently includes only the Undesignated Blanco-Mesaverde Pool.

(2) This unit shall be dedicated to the previously plugged and abandoned Wynona Well No. 1 **(API No. 30-039-24222)** (the "subject well"), which is to be redesignated the Naomi Well No. 1 and is located at an unorthodox gas well location (approved by Division Administrative Order NSL-4538, issued December 29, 2000) 1650 feet from the South line and 450 feet from the West line (Unit L) of Section 25.

(3) The operator of the 320-acre unit shall commence re-entry and recompletion operations on the aforementioned well on or before December 31, 2001, and shall thereafter continue the re-entry and recompletion operations on the well with due diligence in order to test the Mesaverde formation.

(4) In the event the operator does not commence re-entry and recompletion on the proposed well on or before December 31, 2001, Ordering Paragraph No. (1) shall be of no effect, unless the operator obtains a time extension from the Division Director for good cause.

(5) McElvain is hereby designated the operator of the subject well and unit.

(6) After pooling, uncommitted working interest owners are referred to as non-consenting working interest owners. After the effective date of this order, the operator shall furnish the Division and each known non-consenting working interest owner in the unit an itemized schedule of estimated costs of the re-entry and recompletion operations ("the well costs").

(7) Within 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.

(8) The operator shall furnish the Division and each known non-consenting working interest owner an itemized schedule of actual well costs within 90 days following completion of the well. If no objection to the actual well costs is received by the 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 Division will determine reasonable well costs after public notice and hearing.

(9) 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.

(10) 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 re-entering and recompleting the well, 100% of the above costs.

(11) The operator shall distribute the costs and charges withheld from production, proportionately, to the parties who advanced the well costs.

(12) Reasonable charges for supervision (combined fixed rates) are hereby fixed at $5,455.67 per month while re-entering and recompleting and $545.55 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.

(13) Except as provided in Ordering Paragraphs No. (10) and (12) above, all proceeds from production from the well that are not disbursed for any reason shall be placed in escrow in Rio Arriba County, New Mexico, to be paid to the true owner thereof upon demand and proof of ownership. The operator shall notify the Division of the name and address of the escrow agent within 30 days from the date of first deposit with the escrow agent.

(14) 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.

(15) Should all the parties to this compulsory pooling order reach voluntary agreement subsequent to entry of this order, this order shall thereafter be of no further effect.

(16) The operator of the well and unit shall notify the Division in writing of the subsequent voluntary agreement of all parties subject to the forced pooling provisions of this order.

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

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

SEAL

STATE OF NEW MEXICO
OIL CONSERVATION DIVISION

Lori Wrotenbery

LORI WROTENBERY
Director