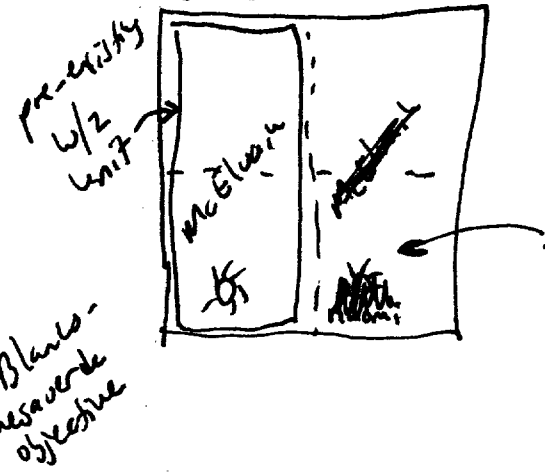
12635

S. Mon - Motion to Stay:
① risk mitigation not a proper rationale for pooling pursuant to 70-2-17
② McElvain will not be prejudiced

McElvain S/2 (lay down)
D.J. Simmons E/2 (stand-up)



Simmons Gallup-Dakota reserves

McElvain Response:
① Simmons testified that no imminent plans to drill

Order - deal w/ Memo. No. 3-85

Simmons

70-2-17(c)

2 or more separately owned tracts
2 or more separately owned royalty interests
owners not agreed to pool interests
separate owner has right to drill -or- proposes to drill a well

avoidance of drilling of unnecessary wells
protect correlative rights
prevent waste

orders:

1. notice + hearing
2. just and reasonable terms and conditions
3. afford opportunity to recover or receive without unnecessary expense his just and fair share of the oil or gas
4. describe lands included in the unit
5. identify the pool or pools
6. designate an operator
7. make provision as to any owner who elects not to pay his proportionate share in advance - for prorata reimbursement solely out of production
8.

McElvain / Simmons
12635 de novo
12705

McElvain - 3 witnesses
Simmons - 3 witnesses

McElvain - Opening
70 - 2 - 17 (c)

Land witness - ex 15
proposed Blanco - Mesa Verde re-entry project

no Simmons proposal - Division hearing made
[seems to argue that Division hearing should
bar consideration of competing pooling
application despite a de novo filing -
when no application filed before Division hearing
calls it a "policy issue"]

"due diligence not required?"

harps on this issue

W/2 well leaves other interest owners
out of a Mesa Verde development
well

Simmons

Mesa Verde + Lewis +

best developed on a stand up basis
pre existing fractures run N to S
20° to the right of N

Naomi well will not drain SE

Misapplication of compulsory pooling statute

McElvain has pre-existing Stand-up w/2 – McElvain's witness said that wanted to minimize risk all place on others ——
[no basis in statute]

risk has no basis in Oil + Gas Act
[but what about Vikings?]

"Due diligence" as a predicate to pooling – in brief
McElvain's "proposal" perfunctory

Commission should set parameters of good faith –

=

McElvain

Mona Bivion – proposes to re-enter ~~Ed~~ Naomi #1 (prev. approved NSL) Pt A'ed 12-98

Vyanna to test Dakota oil well
pursuant to test Mesa-verde formation

Minerals released after Pt A in 12-98
re-acquired w/2
proposed recently 1 mo. later ex. 2

Simmons rec'd letter

proposed S/2 because:
ownership - McElvain has interest
risk - what parties benefit & who should bear risk
benefit - potential for future development
test - could be done at low cost & risk could be shared by more than one party & all parties who benefit - looking out for other parties - geology unknown until test complete

risk sharing a common & reasonable consideration — (normally the predominant reason for land dept.)

W. of Lindrith
Prevailing spacing - mile
some N/2 some E-W

[Special Rules for Blanco-Mesaverde R-10987-A]

Division approved unorthodox location on Dec. 29, 2000 [effect]

objection: hearsay - Ex. 8

I would admit Exhibit 8 but point out that [redacted] it is hearsay and that the legal residuum rule might present problems if Ex. 8 is the only admissible evidence on a proposition.

I would admit Ex. 8 but point

Bixler dismisses Simmons' 6-7-01 proposal at well as inadequate
doesn't address clearly Mesa-verde or Dakota

Simmons:
surface to base of Dakota
(letter doesn't address how to deal w/ Fruitland)

(Ex. 12 doesn't agree to complete in Mesaverde - traditionally wells completed from bottom up at shortest drilling costs not requested until completion is done)

Dakota - 160's

McElvain & Simmons — S/2 Mesaverde (only?)
— E/2 Mesaverde
objective: Gallup Dakota oil well (NE/4 well)

McElvain
1-7
9-14

Cross (Hall) → *not creating w/ 2 unit because maximum # of parties should share the risk all have the potential to benefit - exploration benefits the entire section - by exploring the formation [attorney?]

*risk mitigation of S/2 the primary motivation - also orderly development

☆ do we need title opinion? "owners"

"good faith effort" = could vary from owner to owner, assuring other party has adequate information, proposal clear and concise, states intent of proposal cost estimates, terms, plan for development, alternatives to participation, adequate time to consider, ~~other~~ sharing info. on request,

McElvain evaluates proposals rec'd – not geology (not given), not engineering info./ ≠ economics,

min. info – terms, timing,

☆ only 1 contact initiated w/ Simmons before filing compulsory pooling app.

didn't call Simmons because their position seemed clear —

McElvain pools a lot in Ludlow area because of difficult wi owners in the area

Bailey - could propose well in E/2 if an E-W unit were created - would have to propose to operator (Simmons) would not be able to develop the entire section as it sees fit —

//

Jane E Jackson -

Geologist

mesa verde formation
Blanco-mesa verde pool

papers not applicable
ex 23 - not applicable

14 wells drilled in mesa verde (completed)

used well data from active wells

Mr Elvain
16, 17
admitted

PJ Simmons
25
admitted

Simmons 25 shows east-west sand trend? used resistivity cut off rather than porosity cut off?

Menefee at Pt. Lookout of Mesa Verde (specific objective)

general correlation between sand thickness at production yet good producers in #17 have less sand

[RL - thickness large & irrelevant - need to know where fractures are]

[She alludes to #s of wells but then offers a sand thickness map?]

no evidence of fracture in #25

log has NO evidence of fracturing

RL ⇒ Mesa Verde produces through matrix rather than natural fracture system

John Steuble

Naomi: 1 had problems
volumes too low to justify
workovers

AFE: prepared himself 10-20% low
Procedure:

agrees w/ Ext. { $5455/mo drilling
$545[illegible] mo. Operating

does not agree w/ 150%

{ believes 200% should apply
wildcat well
no mesaverde production in area
only one mesaverde
well in area - and it
only made 6013 mcf (Ex. 18)
a good well in § 15, 3 mi.
to the NW (Ex. 19)
(Ex. 20)
total lack of mesaverde
production justified high
risk factor

criticizes papers

- '98 - 12 wells in Lindrith area, 14 in Mesa Verde
- 35 frac jobs w/in formation
- 5 re-entrys
- No evidence of N/S trends in wells

Economic Summary -
Simmons exhibits show no intention of completing in Mesa Verde

Rate Return should justify well under Simmon's ex. 32

Their recompletion Charges

December completion window
hunting season/landowner a prob.

McElvain
18-22
Admitted

cross →
Could have recompleted as a w/2 well w/out delay -

expects Naomi well to drain a relatively small area -
this area probably a bit tighter & less fractured than remainder of the basin

can't drain SE corner (but could do an infill) (other areas downspacing to 80's - area of drainage small)

McElvain opposes 160's ~~but~~ because 320's is the std. spacing -

wants people who will benefit to also share the risk

no fracture link studies - expects fractures less than 300' - can't say what the orientation would be

reserves est. at .5 to 1 bcf

Simmons

Ed Dunn

E/2

efforts to obtain

Summary
1-18
D-1
Admitted

Wants to pool:

pool surface to base of Mesaverde less Fruitland coal

target: Dakota (main objective)

want Mesaverde in case Dakota does not turn out well

Gusek
Lisa [redacted] - geologist

6 wells drilled w/ Simmons
12 wells operating
12 Lewis shale
6 well Chacra Lewis

=

Blanco - Mesaverde pool limits set out

750' below Huerfanito Bentonite marker

shouldn't be included? Chacra unit
Otero sands

Mancos directly underlies Dakota (studies done) - Burlington work - eliptical drainage pattern (opposite
most fractures N/S - tests were fracd
natural fractures also follow this pattern

applicable to 60 to 80 acre spacing)

mesa verde tight - will need to be fractured to produce

Point Lookout the best producer
Cliff House - wet

should be developed as stand-up

prime fracture orientation N/S

McElvain well wouldn't drain SE

multiple pay here—
test all formations while drilling
eg, PC
Gallup-Dakota
~~Mesa~~
mesa verde
Lewis Chacra

no other operator looking @ Gallup-Dakota

best producers have thinner reservoir rock rather than thicker rock—

McElvain
19-24
admitted

cover objection)

Cross

penalty? too close to S line

Tom Mullins

drainage/fractures on N/S basis (+ N 40°)

3-1 permeability – ex. 29

160 acre max. drainage area

estimates Dakota reserves in E/2
§30 → 326 MMcf

mesa verde uneconomic - 66 Mmcf - by itself

26-33
Simmons
admitted

Jackson / McElvain

125 net sand isopach map > 8% porosity

126 E to W trend
Menefee / Point Lookout intervals

127 location of existing wellbore better situated to
drain Mesaverde from S/2 "because trend
goes E - W

127- Complains about DJ Simmons theory
130 says papers don't address fracturing of Mesaverde
in § S.25

132 isopach maps prepared from porosity logs

136 Objective is Menefee & Point Lookout
intervals of Mesa-verde formation

137 believes well will be productive because of
production from wells in §§27, 17

137-8 Ex. 17 - correlation between sand thickness
and productivity? "general correlation";
but in §17, 18 production correlated w/
thicker sands; well in §29 - worse producer
& thicker sands

142 doesn't agree that fracture patterns influence
direction of drainage

143 fracturing in Gallup but believes it won't have any effect on §25 Mesaverde

143 doesn't know fracture direction in Gallup in vicinity of well

144 Sole basis for drainage of SE/4 dominantly location is porosity trends being E-W

146 claims mechanism for production is through the matrix -

147 If there is natural fracturing, it's influenced by structural features

148 ok prevailing stress trends in subject area

148-9 set of NE → SW and NW → SE trends no pure E-W trends !!

149 Blanco-Mesaverde is a tight sand gas reservoir

R-10987
Blanco - mesaverde
order

Gusek/Simmons

220 well in NE/4 §34 / Schalk 43-2
small amounts of gas - excessive water

NE/NW §13 tested water only

well in NW/4 §35, small amounts of gas

221 well in NW/4 §15 produced uneconomic amounts
93,000 MCF - all test included Gallup-Dakota
production

221-2 Nearest economic well 3 1/2 mile NW

225 high variability of production numbers in area
of subject is indicative of fracturing in
the area -

227 Emmendorfer used dipmeter - fracture log to
understand structural relationship of fracture
patterns in Marcos-Gallup
(directly underlies Mesaverde)

plotted fracture orientation measurements
on logs
Cullins Federal No. 6 - 104 samples taken from
breakouts & fractures show N-S orientation

228 Media Canyon No. 7 - 12 samples - N/S fracture orientation

Majority of fracturing is N/S to about N-40-degrees east orientation

229 tight sands - downspaced from 320 to 160 ac now to 80

Burlington research shows elliptical drainage pattern N-10-degrees-east

many papers support this in Mesa-verde, Gallup and Dakota

230 fair to extrapolate research to different areas of Basin - Burlington did a lot of work

232 matrix porosity has nothing to do with this - these wells will have to be artificially stimulated

233 standup units are the best - because will follow primary fracture orientation N-S N-40-degrees-east

234 no way to drain SE/4

234 reservoir very tight
drainage area between 80 to 160 acres
not drain SE/4

238 using an 8 percent porosity cutoff, likely
to to include wet or unproductive sands

DJ Simmons

246 DJ Simmons will drill
would like "opportunity" or "option"
to recomplete

263 could recomplete Mesaverde in "a couple
of months"

270 north-south orientation to permeability in the
area caused by natural fractures

271 fracture orientation in § 25 is north-south
to North-40-degrees-east

271 drainage patterns are elliptical - 3-to-1
(160 acres)(maximum drainage) permeability anisotropy
-higher permeability is three
times the shorter distance

★ 275 drainage patterns based on permeability of the
rocks - and hydraulic fracture direction

276 § 25 best developed w/ stand up 320s

277 deposition of sands is from northwest-se
direction in Point Lookout interval
(descriptive of Mesaverde in this §)

poss in favor of Simmons vs Gallup-Dakota?
uneconomic w/out Mesa Verde?

277- Nearby production verified

278 Nearby Gallup-Dakota production

282 Mesaverde uneconomic

282 not intending to complete in Mesaverde for several months or several years

284-5 Simmons well to Gallup is going to be "marginal"

297 Has "not committed to" a Mesaverde completion to interest owners - has not committed to a time frame -

298 agrees that DJ Simmons hasn't agreed to a Mesa Verde completion

302 McElvain's recompletion would predominantly drain the NW/4 on a 3-to-1 basis

303 Good faith: Std industry practice - call other interest owners

305 Simmons well in SE/4 not going to be drilled w/out add'l reserves in Mesaverde

307 Simmons sought voluntary agreement of other working interest owners for eval. of Mesaverde reserves in conjunction w/ Gallup-Dakota well

deny McEl in - let them develop w/ =
deny Simmons in Mesaverde; grant in Gallup-Dakota

Simmons - Dunn (landman) (183)

184 proposes well to test Gallup-Dakota - E/2 units
Bishop 25-1 2 Mesaverde
8174 feet

189 efforts to obtain consent detailed

192 procedure for obtaining consent:
well proposal + AFE
follow-up clarification
well plan

193 this was, TD
diligent

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

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

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

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

58 C.J.S. Mines and Minerals § 240.

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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