

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

**APPLICATION OF FAE II OPERATING, LLC
FOR STATUTORY UNITIZATION,
LEA COUNTY, NEW MEXICO.**

CASE NO. 22972

**FAE II OPERATING, LLC'S MOTION FOR DETERMINATION ON RATIFICATION
REQUIREMENT OF PHASED ALLOCATION FORMULA
UNDER THE STATUTORY UNITIZATION ACT**

FAE II Operating, LLC ("FAE") submits the following Motion for Determination on Approval Requirement of Phased Allocation Formula Under the Statutory Unitization Act. For the reasons discussed below, FAE requests that the New Mexico Oil Conservation Division ("Division") issue an order determining that FAE may satisfy the 75% ratification requirement set forth in Section 70-7-8(A) of the New Mexico Statutory Unitization Act ("the Act") by demonstrating that 75% of the cost bearing and non-cost bearing interests have approved the first phase of FAE's proposed two-phase allocation formula.

I. INTRODUCTION

FAE's application seeks statutory unitization of the proposed South Jal Unit ("Unit"), an enhanced oil recovery unit comprised of approximately 19,369.77 acres of federal, state, and fee lands located in Lea County.¹ FAE proposes to allocate costs and revenues among the tracts included in the Unit based using a two-phase methodology, as required by the Bureau of Land Management ("BLM"). See Unit Agreement, attached to FAE's Application as Exhibit 1, at p. 8

¹ In related Case No. 22971, FAE seeks approval of the Project for enhanced oil recovery and qualification of the Project for the recovered oil tax rate.

(filed July 5, 2022); *see also* Affidavit of Huxley Song, attached as Exhibit A. Both the BLM and the New Mexico State Land Office have issued preliminary approval of the Unit Agreement.

Under the first phase of the two-phase allocation formula, costs and revenues will be allocated based on the production of oil from July to December 2021. The Phase II formula takes effect after 36 months of unit operations and allocates costs and revenues based on the remaining recoverable oil in place. *See id.* Although FAE has proposed a two-phase allocation formula, it intends to develop the entire Unit once it obtains approval. Stated differently, the allocation formula – but not the development plan – changes between Phase I and Phase II.

FAE has secured the ratification of its plan for unit operations from more than 75% of the Phase I interest owners. *Id.* Because the Unit Agreement has been approved by those persons who will be required to initially pay at least 75% of the costs of the unit operations, and also by the owners of at least 75% of the non-cost bearing interests, the ratification of the required Phase I interest owners meets the 75% approval requirement of Section 70-7-8(A) and permits the Division to enter an order approving the plan for unit operations.

II. ARGUMENT

The Statutory Unitization Act authorizes the Division to approve a proposed unit that has been ratified by 75% of the interest owners who will initially bear the costs of unit operations and 75% of the non-cost bearing interest owners.

FAE's application for statutory unitization of the South Jal Unit meets the threshold criteria for approval under Section 70-7-8(A) because more than 75% of the interests who will initially bear the costs of unit operation, and more than 75% of the non-cost bearing interests, have approved the Phase I plan for unit operations. The Legislature adopted the Act in 1975 to provide for the unitized management, operation and further development of oil and gas properties "to the end that greater ultimate recovery may be had therefrom, waste prevented, and correlative rights

protected of all owners of mineral interests in each unitized area.” NMSA 1978, § 70-7-1. The Act applies to “any type of operation that will substantially increase the recovery of oil above the amount that would be recovered by primary recovery alone and not to what the industry understands as exploratory units.” *See id.* Thus, through the Act, the Legislature adopted a public policy of promoting enhanced oil recovery projects within the state.

The Act sets forth several criteria that apply to the Division’s approval of statutory units.

One of those requirements, which is contained in Section 70-7-8(A), provides:

No order of the division providing for unit operations shall become effective unless and until the plan for unit operations prescribed by the division has been approved in writing by those persons who, under the division's order, *will be required initially to pay at least seventy-five percent of the costs of the unit operations, and also by the owners of at least seventy-five percent of the production or proceeds thereof* that will be credited to interests which are free of cost such as royalties, overriding royalties and production payments, and the division has made a finding either in the order providing for unit operations or in a supplemental order that the plan for unit operations has been so approved.

See § 70-7-8(A) (emphasis added). The plain language of this provision establishes that the Division may approve a statutory unit when 75% of the interests who will initially be required to pay the costs of operations, and 75% of the non-cost bearing interests, have approved the unit agreement.

The language of Section 70-7-8(A) must be construed in accordance with established principles of statutory construction. In this regard, New Mexico law establishes that “[w]hen statutory language is clear and unambiguous, [this Court] must give effect to that language and refrain from further statutory interpretation.” *Marbob Energy Corp. v. New Mexico Oil Conservation Comm'n*, 2009-NMSC-013, ¶ 9, 146 N.M. 24. Moreover, the words contained in a statute are presumed to have been intentionally used, and all words included in a statute must be given effect. *See, e.g., Baker v. Hedstrom*, 2013-NMSC-043, ¶ 24, 309 P.3d 1047

(“the Legislature is presumed not to have used any surplus words in a statute; each word is to be given meaning.”) (internal citations omitted).

In this case, the plain language of Section 70-7-8(A) only requires ratification by those interest owners who are *initially* required to bear 75% of the costs of unit operations or derive proceeds from those operations. The Legislature intentionally included the word “initially” and it must be applied. Further, the use of “thereof” with respect to ratification by owners of production or proceeds makes clear that approval by these interest owners relates only to the same initial 75% of cost bearing working interests. *See State v. Jade G.*, 2007-NMSC-010, ¶ 18, 141 N.M. 284 (words in a statute are presumed to be used in their ordinary and usual sense); *Cambridge English Dictionary*: “Thereof” defined as “of or about the thing just mentioned;” *see also Lucero v. Richardson & Richardson, Inc.*, 2002-NMCA-013, ¶ 18, 131 N.M. 522 (“[W]here general words follow an enumeration of persons or things of a particular and specific meaning, the general words are not construed in their widest extent but are instead construed as applying to persons or things of the same kind or class as those specifically mentioned.”) (citing *State v. Foulentfont*, 1995-NMCA-028, ¶ 9, 119 N.M. 788 (describing the ejusdem generis rule of statutory construction).

The Legislature’s unambiguous use of the words “initially” and “thereof” demonstrates that it intended to permit statutory unitization when at least 75% of interest owners in the *initial phase of unit operations* have ratified the operating plan. Conversely, the use of the word “initially” demonstrates that those interest owners who will not bear the initial costs of unit production need not ratify the plan for unit operations prior to the Division entering an order approving the plan and finding that the requisite percentage of interest owners have ratified the plan. To hold otherwise would write the term “initially” out of the statute, which is not permitted by New

Mexico's rules of statutory construction, and would controvert the Act's purpose of encouraging enhanced oil recovery projects to fully deplete reserves.

As explained by Mr. Song, FAE has obtained the required approval of its plan for unit operations of at least 75% of the Phase I interest owners. *See* Exhibit A. In accordance with the clear and unambiguous plain language of Section 70-7-8(A), the approval of 75% or more of the interest owners in Phase I is sufficient to establish ratification of the unit under Section 70-7-8(A) of the Statutory Unitization Act.

III. CONCLUSION

Section 70-7-8(A) requires approval of the unit operating plan by at least 75% of the interest owners who will initially be required to pay, or derive proceeds from, the unit development. Here, the costs and revenues of the proposed South Jal Unit will be allocated in two phases, and FAE has obtained approval from the requisite percentage of interest holders for the first phase. Accordingly, FAE has satisfied the requirements of Section 70-7-8(A) and the Division should issue an order to that effect.

Respectfully submitted,

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Certificate of Service

I hereby certify that a true and correct copy of the foregoing motion was sent by electronic mail on this 29th day of September, 2022, to the following counsel of record.

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SELF-AFFIRMED STATEMENT OF HUXLEY K. SONG

1. I am the Chief Executive Officer of FAE II Operating, LLC (“FAE”). I am over 18 years of age, have personal knowledge of the matters addressed herein, and am competent to provide this Self-Affirmed Statement.

2. I am familiar with FAE’s application for approval of its proposed South Jal Unit (“Unit”), the plan for unit operations, and FAE’s discussions with the Bureau of Land Management (“BLM”) regarding initial approval of the Unit Agreement.

3. FAE seeks authorization to develop the Unit under the Statutory Unitization Act, NMSA 1978, Sections 70-7-1 *et seq.* The unitized interval includes the Yates, Seven Rivers, and Queen formations, and the Unit area comprises approximately 19,369.77 acres of federal, state, and fee lands located in Lea County.

4. FAE intends to develop the Unit using secondary and tertiary recovery methods to maximize the production of hydrocarbons from reserves that have otherwise been depleted.

5. FAE worked with the BLM to obtain approval of the proposed Unit Agreement, which is attached to FAE’s Application as Exhibit 1. The BLM has issued preliminary approval of the Unit Agreement.

Exhibit A

6. As requested by the BLM, the proposed Unit Agreement includes a two-phased approach to the allocation of costs and revenues. The Phase I formula allocates costs and revenues based on the production of oil from July to December 2021 and will apply for 36 months. The Phase II formula takes effect after 36 months and allocates costs and revenues based on the remaining recoverable oil in place. *See* Unit Agreement, attached to FAE's Application as Exhibit 1, at p. 8.

7. Although FAE has proposed a two-phase allocation formula, development will be conducted uniformly throughout the Unit in both phases and will result in substantially greater production of oil than would otherwise have been recovered through primary recovery.

8. The cost allocation formula, consisting of two phases, is fair and reasonable.

9. FAE has diligently sought to obtain approval of the Unit Agreement from the requisite percentage of interest owners in the Unit.

10. FAE has obtained over 75% approval from both cost bearing and non-cost bearing interests with respect to Phase I of the Unit. Thus, the Unit Agreement has been approved by those persons who will be required initially to pay at least seventy-five percent of the costs of the unit operations, and also by the owners of at least seventy-five percent of the production or proceeds thereof that will be credited to interests which are free of cost such as royalties, overriding royalties and production payments.

11. I understand this Self-Affirmed Statement will be used as written testimony in this case. I affirm my testimony above is true and correct and is made under penalty of perjury under the laws of the State of New Mexico. My testimony is made as of the date identified under my signature below.



Huxley K. Song

Date: 9/28/22