

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

**APPLICATION OF CAZA PETROLEUM,
INC. FOR A NON-STANDARD OIL
SPACING AND PRORATION UNIT
AND COMPULSORY POOLING,
LEA COUNTY, NEW MEXICO**

**Case No. 15437 (*de novo*)
Order No. R-14191-A**

ORDER OF THE COMMISSION

BY THE COMMISSION:

This matter came on for hearing at 9:00 a.m. on November 10, 2016, at Santa Fe, New Mexico, before the Oil Conservation Commission ("the Commission").

NOW, on this 10th day of February, 2017, the Commission, having considered the testimony and the record,

THE COMMISSION FINDS THAT:

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

(2) Caza Petroleum, Inc. ("Caza" or "Applicant") seeks approval of a non-standard 160.16-acre oil spacing and proration unit (the "Unit") for oil production in the Lea; Bone Spring, South pool (pool code 37580), comprising the W/2 W/2 of Section 19, Township 20 South, Range 35 East, NMPM, Lea County, New Mexico. Applicant further seeks an order pooling all uncommitted interests in the Unit for the Bone Spring formation.

(3) The Unit will be dedicated to Applicant's Igloo 19 State Well No. 7H ("the proposed well"; API No. 30-025-42361), a horizontal to be drilled from a surface location 200 feet from the South line and 750 feet from the West line (Lot 4) to a standard terminus 330 feet from the North line and 350 feet from the West line (Lot 1) of Section 19. The completed interval of the proposed well would be orthodox.

(4) The proposed well is in the Lea; Bone Spring, South Pool. Spacing in that pool is governed by statewide Rule 19.15.15.9.A NMAC, which provides for standard 40-acre units, each comprising a governmental quarter-quarter section, and 330-foot setbacks from the unit boundaries. The proposed Unit and project area would consist of four adjacent quarter-quarter sections.

(5) Legacy Reserves LP ("Legacy"), the leasehold owner of Lots 1 & 2 (W/2 NW/4) of Section 19 appeared at the hearing and presented evidence and testimony in opposition to the application.

(6) COG Operating LLC ("COG") also entered an appearance in the Commission proceeding, but did not present any evidence at the Division hearing.

(7) This case was originally heard by the Oil Conservation Division on March 3, 2016. At that Division hearing, Caza presented evidence and testimony in support of the application, and Legacy presented evidence and testimony in opposition to the application.

(8) Division Order No. R-14191 was entered in Case No. 15437 on July 14, 2016. Order No. R-14191 denied the application of Caza.

(9) On August 1, 2016, Caza filed an application for a hearing *de novo* before the Commission.

(10) The following proceedings took place before the Commission:

(a) The Commission conducted a hearing on Caza's *de novo* application on November 10, 2016.

(b) Counsel for the New Mexico State Land Office ("SLO") appeared at the outset of the hearing and objected to the hearing going forward because the SLO had not received timely notice of the hearing as required by 19.15.4.12(A)(1) NMAC.

(c) The Commission then went into executive session to conduct deliberations on SLO's motion for a continuance. The Commission concluded that the SLO was not entitled to receive notice of the hearing pursuant to 19.15.4.12(A)(1) NMAC, and denied the motion for a continuance.

(d) At the conclusion of the hearing, the Commission left the record open to allow the SLO to submit a written statement addressing its position in the case.

(e) On November 16, 2016, the SLO submitted its written statement, which asserted that the SLO was entitled to receive notice of the hearing under 19.15.4.12(A)(1) NMAC. The SLO's written statement further asserted that, in the absence of such notice, the Commission lacked jurisdiction to proceed with the November 10, 2016 hearing.

(f) On December 19, 2016, Caza's counsel sent a letter to the Commission Chairman in response to the SLO's written statement, stating that

19.15.4.12 is not relevant because Caza is not seeking to pool any interests of the Commissioner of Public Lands.

(11) Caza appeared at the *de novo* hearing through counsel and presented the following evidence in support of its application:

(a) Notice of the proposed Unit was provided to all surrounding affected parties within the Bone Spring formation.

(b) Notice of the proposed Unit was provided to Legacy as an uncommitted working interest owner in the Unit, and a party subject to the pooling provisions of this application.

(c) Caza has engaged in good faith negotiations with Legacy to obtain its voluntary joinder in the well.

(d) All of Section 19 Township 20 South, Range 35 East is comprised of State of New Mexico lands.

(e) Caza has a 70% interest in the SW/4 of Section 19 ("Caza tract").

(f) Within the Bone Spring formation, there are multiple producing intervals that have been successfully targeted by horizontal wells in this area, including the First, Second and Third Bone Spring Sand intervals.

(g) Caza's proposed Igloo 19 State Well No. 7H is proposed to be drilled to test the Second Bone Spring Sand interval.

(h) Caza's preferred well orientation for all three of the target Bone Spring intervals is North-South.

(i) East-West Bone Spring horizontal wells in the vicinity of the proposed well have underperformed. In the case of the Third Bone Spring Sand interval, North-South horizontal wells have recovered two times as much oil as East-West oriented wells.

(j) Caza has drilled three (3) one-mile, North-South horizontal wells in the E/2 of Section 19. Two wells produce from the Second Bone Spring Sand interval and one well produces from the Third Bone Spring Sand interval.

(k) Because North-South Bone Spring horizontal wells are more economical than East-West wells, Caza's proposed well has a North-South orientation.

(l) Each quarter-quarter section in the W/2 W/2 of Section 19 would contribute more or less equally to production from the proposed well.

(m) A half-mile horizontal well drilled North-South in the SW/4 of Section 19 would be uneconomic.

(n) If Caza cannot drill a North-South well in the W/2 W/2 of Section 19, its acreage in the SW/4 of Section 19 will be stranded.

(o) Yates Petroleum Corporation, Abo Petroleum Corporation, MYCO Industries, Inc. and Sharbro Energy, LLC, all of whom own interests in the SW/4 of Section 19, have provided letters supporting Caza's application.

(12) Legacy appeared at the *de novo* hearing through counsel and presented the following evidence in opposition to Caza's application:

(a) Legacy is the operator of the Federal Exploratory Lea Unit ("the Lea Unit"), which comprises 2,559.68 acres, more or less, of the following Federal and State lands in Lea County, New Mexico:

Township 20 South, Range 34 East, NMPM

Section 11: E/2
Section 12: All
Section 13: All
Section 14: NE/4
Section 24; N/2

Township 20 South, Range 35 East, NMPM

Section 18: W/2
Section 19: NW/4

(b) The Bureau of Land Management ("BLM") has designated Legacy the operator of the Lea Unit.

(c) Legacy owns 100% of the interest in the NW/4 of Section 19, which is part of the Lea Unit.

(d) If Caza's application is granted, the BLM would require Legacy to operate the well pursuant to existing agreements within the Lea Unit.

(e) Legacy has a comprehensive development plan for the Lea Unit which includes the drilling of thirty-six (36) North-South horizontal wells from twelve (12) multi-well pads to develop the First, Second and Third Bone Spring Sand intervals.

(f) Some of the wells included in the development plan have been drilled, and some of the wells have applications for permit to drill ("APDs") that have been approved by BLM.

(g) Legacy's development plan includes the drilling of six (6) one-and one-half (1 1/2) mile, North-South horizontal wells whose project areas would include: i) the W/2 W/2 of Section 18 and Lots 1 & 2 of Section 19; and ii) the E/2 W/2 and E/2 NW/4 of Section 19.

(h) The six (6) wells are to be drilled from two (2) multi-well pads, designated by Legacy as pads 11 and 12, in the SW/4 of Section 19. The BLM mandated the locations of pads 11 and 12, and approved them on August 6, 2015.

(i) Legacy has constructed pads 11 and 12 at a cost of \$200,000 each.

(j) The BLM has approved Legacy's APDs for the Lea Unit Well No. 59H, to be drilled from pad 11, and the Lea Unit Well No. 62H, to be drilled from pad 12. These wells will be drilled to develop the Third Bone Spring Sand interval within the NW/4 of Section 19 and W/2 of Section 18.

(k) If Caza's application were granted, Legacy would lose its \$400,000 investment in pads 11 and 12 and would incur additional expense to restore the surfaces of pads 11 and 12 and construct new multi-well pads.

(l) Legacy would also incur the expense of installing a new tank battery, at a cost of \$157,000, because Caza's proposed well would be initiated outside of the boundary of the Lea Unit.

(m) There are equivalent numbers of North-South and East-West Bone Spring horizontal wells in the vicinity of the proposed well, indicating that there is no orientation preference for Bone Spring horizontal wells.

(n) The rock quality in the Bone Spring intervals within the NW/4 of Section 19 is much better than the rock quality in the SW/4 of Section 19.

(o) There would be an inequitable allocation of reserves if the proposed well is drilled and produced.

(p) If the proposed well were drilled, Legacy would be constrained to drill one-mile, North-South horizontal wells in the W/2 of Section 18, resulting in the stranding of 120 Lea Unit acres.

(q) Granting Caza's application would negatively impact Legacy's development plan for the Lea Unit.

(r) Granting the application would result in waste and impair the correlative rights of Legacy and the other owners of interests in the Lea Unit.

THE COMMISSION CONCLUDES AS FOLLOWS:

(13) The Commission has jurisdiction over the parties and the subject matter of this case.

(14) Proper notice of Caza's application has been given.

(15) Legacy's proposed plan of development for the Lea Unit, including the W/2 of Section 18 and the NW/4 of Section 19 will maximize the recovery of hydrocarbons from these Unit tracts.

(16) The evidence presented indicates that development of the W/2 W/2 of Sections 18 & 19 with one mile horizontal wells in each section will likely result in reduced recovery from those tracts due to well setback limitations, thereby causing waste.

(17) Legacy has acted in prudent manner to ensure that the correlative rights of all interest owners in the Lea Unit are protected.

(18) Legacy presented sufficient evidence and testimony to demonstrate that its correlative rights and those of the interest owners in the Lea Unit will be adversely affected by approval of Caza's application.

(19) The evidence presented indicates that the S/2 of Section 24, being the offset acreage to the west of the Caza tract, is currently undeveloped in the First, Second and Third Bone Spring Sand intervals. Also, all of Section 30, being the offset acreage to the south of the Caza tract is currently undeveloped in the First and Third Bone Spring Sand intervals. Lastly, the SE/4 of Section 19, being the offset acreage to the east of the Caza tract, is currently undeveloped in the First Bone Spring Sand interval.

(20) With regards to the development of the SW/4 of Section 19, the evidence shows that Caza has various options to develop that tract in conjunction with offset tracts to the west, east and south.

(21) In order to prevent waste and protect correlative rights, the application of Caza in this case should be denied.

IT IS THEREFORE ORDERED THAT:

(1) The application of Caza Petroleum, Inc. for a non-standard oil spacing and proration unit comprising the W/2 W/2 of Section 19, Township 20 South, Range 35 East, NMPM, Lea County, New Mexico and for compulsory pooling of the non-standard unit, is hereby denied.

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

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

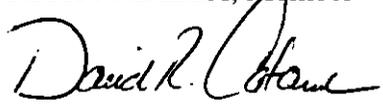
STATE OF NEW MEXICO
OIL CONSERVATION COMMISSION



ROBERT BALCH, Member



PATRICK PADILLA, Member



DAVID R. CATANACH, Chair

SEAL