

**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. 13724
ORDER NO. R-12609**

**APPLICATION OF CHAPARRAL OIL AND GAS COMPANY FOR APPROVAL
OF A NON-STANDARD GAS SPACING AND PRORATION UNIT, SAN JUAN
COUNTY, NEW MEXICO.**

ORDER OF THE DIVISION

BY THE DIVISION:

This case came on for hearing at 8:15 a.m. on June 8, 2006, at Santa Fe, New Mexico, before Examiner William V. Jones.

NOW, on this 8th day of August, 2006, 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, Chaparral Oil and Gas Company ("Chaparral"), seeks to establish a non-standard 160-acre gas spacing and proration unit within the Basin-Fruitland Coal Gas Pool (71629) to comprise the NW/4 of Section 24, Township 28 North, Range 11 West, NMPM, San Juan County, New Mexico, to be dedicated to the applicant's proposed Sally Well No. 4 (API No. 30-045-33539) which will be located at a standard gas well location within Unit F of Section 24.

(3) The W/2 of Section 24 is included in the Basin-Fruitland Coal Gas Pool. This pool is "unprorated" and is therefore not subject to Part 8 of the Division's statewide rules entitled "*Gas Proration and Allocation*" (Rules 601 through 606).

(4) The Basin-Fruitland Coal Gas Pool is governed by the "Special Rules and Regulations for the Basin-Fruitland Coal Gas Pool," as promulgated by Division and Commission Order R-8768, as amended. The following portions relate to gas spacing unit size and to well density within each gas spacing unit.

(a) Commission Order R-8768-F, Rule 4: "Each standard gas spacing unit will consist of 320 acres, more or less, comprising any two contiguous quarter sections of a single governmental section, being a legal subdivision of the United States Public Lands Survey."

(b) Division Order R-8768-A, Rule 6, provides a way for the Division Director to grant an exception to the requirements of Rule 4. In brief, a non-standard gas spacing unit must consist of contiguous areas, lie wholly within a governmental half section (unless the unit conforms to a previously approved Mesaverde or Dakota spacing unit), and waivers or proof of notice must be obtained from [offset operators or owners of **undrilled** tracts] and all operators owning interests in the portion of the half section that would not be included in the proposed non-standard gas spacing unit. In addition, the Division Director, at his discretion, may set any application under Rule 6 for public hearing.

(c) Commission Order R-8768-F, Rule 7(c), defines a Low Productivity Area and a High Productivity Area within the consolidated boundaries of the Basin-Fruitland Coal Gas Pool. Rule 7(d) provides for an Optional Infill Well (second well in the gas spacing unit) within a standard 320-acre gas spacing unit for both the Low and the High Productivity Area. The notice requirements prior to approving the Optional Infill Well are different for each of these two areas.

(5) The Sally Well No. 4 has been permitted to be drilled by the United States Bureau of Land Management ("USBLM") and the Oil Conservation Division and is proposed to be drilled 1475 feet from the North line and 1635 feet from the West line in Section 24 to a total depth of 1960 feet and is to be completed in the Basin-Fruitland Coal Gas Pool (71629).

(6) Division records indicate that the Sally Well No. 2 operated by Chaparral was already located in Unit F of Section 24 and was completed in the Fruitland Sand and in the Pictured Cliffs formations. Both of these formations are located in pools spaced on 160 acres, with spacing units consisting of the NW/4 of Section 24.

(7) No other party appeared at the hearing or otherwise opposed this application.

(8) The applicant presented the following testimony at the hearing from a Landman.

(a) Chaparral's proposed Sally Well No. 4 would ideally be located in, and have dedicated to it, a Basin-Fruitland Coal gas spacing unit consisting of the W/2 of Section 24. The E/2 of Section 24 is already formed into a Fruitland Coal gas spacing unit and has an active well operated by Burlington Resources.

(b) The minerals in the W/2 of Section 24 are owned by the federal government and leased to all lessees within the W/2 at one-eighth royalty.

(c) Chaparral and its partner group own 100% of the NW/4 of Section 24. The royalty burden in the NW/4 is approximately 18 percent.

(d) The owners in the SW/4 of Section 24 are General Minerals Corporation and Ronnie L. Morehead. The working interest owners in the SW/4 have in the past added additional royalty burdens to their interests until the resulting net revenue interest is only 45 percent after payout.

(e) The interest owners in the SW/4 have been contacted by the applicant and have been notified in writing of the intention to form a non-standard spacing unit in the NW/4 of Section 24. The interest owners in the SW/4 have verbally stated they would rather not join in Chaparral's proposed well. They prefer to form their own non-standard proration unit for Basin-Fruitland Coal gas and drill their own well.

(f) Chaparral's AFE to drill the 2000 foot deep Fruitland Coal well is \$381,000. The Fruitland Coal is expected to be approximately 13 feet thick, which is usually considered adequate. However, a nearby well to the northeast has recently been completed at a disappointing rate.

(g) The economics of drilling the proposed Sally Well No. 4 with an 82 percent net revenue interest is expected to be marginal. The predicted economics after forming a W/2 gas spacing unit and absorbing the heavier burdens of the SW/4 would not allow this well to be drilled.

(9) The examiner concludes as follows.

(a) This area of the Basin-Fruitland Coal gas pool is considered to be in the "Low Productivity Area". The applicant is predicting a marginal coal gas well, which is likely given records on offset production. The applicant did not present or include other geologic or engineering estimates of variations between the acreage in the SW/4 and the NW/4.

(b) This argument for formation of a non-standard gas spacing unit is based solely on assumed economics under two different royalty burdens. Rigorous economics were not shown. However, it is reasonable to assume the drastically increased royalty burdens on owners within the NW/4 resulting from including the acreage in the SW/4 within a standard gas spacing unit would delay or maybe deter drilling of this proposed well.

(c) The Special Pool Rules for the Basin-Fruitland Coal gas pool in Rule 7 allow a well density of one well per 160 acres. The formation of this proposed

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unit in the NW/4 will not prevent the owners of the SW/4 from forming their own identically sized unit and drilling their own Fruitland Coal gas well.

(d) If the well is delayed or not drilled, the mineral interest owner, which is the federal government, would suffer delayed royalties or none at all. The applicant's correlative right to develop this 160-acre lease area would also be impaired.

(e) The applicant has provided notice of its intentions to affected parties as required in Rule 6 of Division Order R-8768-A, and no party has objected to this application.

(10) This application should be approved in order to prevent waste and protect correlative rights.

IT IS THEREFORE ORDERED THAT:

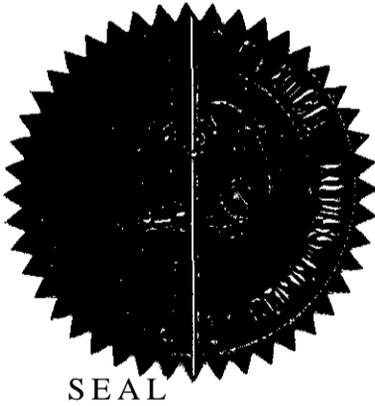
(1) The application of Chaparral Oil and Gas Company ("Chaparral") for an exception to Rule 4 of the "Special Rules and Regulations for the Basin-Fruitland Coal Gas Pool," as promulgated by Order R-8768, as amended, in order to establish a non-standard 160-acre gas spacing unit within the Basin-Fruitland Coal Gas Pool (71629) comprising the NW/4 of Section 24, Township 28 North, Range 11 West, NMPM, San Juan County, New Mexico, is hereby approved.

(2) This unit shall be dedicated to Chaparral's proposed Sally Well No. 4 (API No. 30-045-33539) to be located at a standard gas well location within Unit F of Section 24.

(3) Chaparral shall file a Form C-102 with the Division reflecting the non-standard 160-acre spacing unit within 30 days from the date of this order.

(4) Jurisdiction is hereby 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

MARK E. FESMIRE P.E.
 Director