

**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. 13877
ORDER NO. R-12747-A**

**APPLICATION OF BOLD ENERGY, LP FOR APPROVAL OF AN
APPLICATION FOR PERMIT TO DRILL AND TO ALLOW TWO
OPERATORS ON A WELL UNIT, EDDY COUNTY, NEW MEXICO.**

ORDER OF THE DIVISION

BY THE DIVISION:

This case came on for hearing at 8:15 a.m. on May 10, 2007, at Santa Fe, New Mexico, before Examiner David R. Catanach.

NOW, on this 7th day of June, 2007, the Division Director, having considered the testimony, the record and the recommendations of the Examiner,

FINDS THAT:

(1) Due notice has been given, and the Division has jurisdiction of the parties and of the subject matter.

(2) Bold Energy, LP ("Bold" or "Applicant") filed this application seeking approval of its Application for Permit to Drill ("APD") for its proposed OXY Checker State Well No. 2 ("the proposed well"), to be located in the SW/4 NW/4 (Unit E) of Section 8, Township 19 South, Range 29 East, NMPM, Eddy County, New Mexico.

(3) Bold proposes to drill the proposed well to a depth sufficient to test the Wolfcamp and Canyon formations.

(4) Well spacing in the Wolfcamp and Canyon formations at this location is governed by statewide Rule 104.C(2), which provides that spacing units shall consist of 320 acres. Pursuant to this spacing pattern, the W/2 of Section 8 is dedicated to the OXY Checker State Well No. 1, located in the NW/4 SW/4 (Unit L) of Section 8. OXY USA WTP Limited Partnership ("OXY") is the operator of that well.

(5) Because the proposed well is to be located in a different quarter section from the Checker State No. 1 well, Rule 104.C(2) would permit a Wolfcamp or Canyon well at the location of the proposed well. However, Rule 104.E requires that an operator who proposes to drill a well in a spacing unit that is dedicated to another operator's existing well shall first give notice to the other operator.

(6) Bold notified OXY of its intent to drill the proposed well. OXY objected, and the Artesia District Office of the Division denied Bold's APD. Bold accordingly filed this application.

(7) Both Bold and OXY appeared at the hearing through counsel, and both parties offered testimony from experts in petroleum land matters. Neither party offered any geologic or engineering evidence.

(8) The parties' land witnesses testified to the following matters, which, except as expressly indicated below, were not controverted:

(a) Both Bold and OXY, along with others who did not appear in this case, own interests in the W/2 of Section 8.

(b) The owners of this tract are parties to a Joint Operating Agreement ("the JOA"), which was admitted in evidence. The JOA designates OXY as the operator of this unit.

(c) There previously existed a letter agreement between the parties that also contained provisions with respect to operation of wells on this land. However, the parties have now agreed to terminate that letter agreement, leaving the JOA as the only applicable agreement.

(d) On November 27, 2006, Bold sent OXY a proposal under the JOA for drilling the proposed well as a Wolfcamp/Canyon test. OXY did not elect to participate in the well. Under the terms of the JOA, OXY's failure to elect to participate constituted an election not to participate. However, at the time of this proposal, OXY had not agreed to termination of the letter agreement. OXY's witness testified that OXY did not consent to Bold's proposal under the JOA because OXY regarded the letter agreement as the controlling agreement at that time.

(e) Bold wants to drill the proposed well as a Wolfcamp/Canyon test, and does not want to drill to the deeper Morrow formation at this location.

(f) Bold is willing to, and in fact intends to, re-propose the proposed well under the JOA.

(g) OXY's witness testified that OXY preferred, if a well were drilled at the proposed location, that it be drilled to a depth sufficient to test the Morrow. However OXY's witness disclaimed knowledge as to whether OXY would propose a well, or whether it would, or would not, elect to participate in Bold's proposal, and disclaimed knowledge as to whether the proposed well could be subsequently deepened to test the Morrow.

(9) Counsel for OXY argued that the granting of this application would affect the economics of a Morrow well on this unit, and accordingly could cause waste, and impair correlative rights, by practically precluding development of otherwise recoverable gas. However, OXY presented no geologic testimony to indicate that the Morrow at this location would be an economic prospect in any case, nor did OXY's witness testify when, if at all, OXY proposes to pursue that prospect. Furthermore, there was no evidence as to whether the proposed well could be deepened to test the Morrow.

(10) Assuming that drilling a shallow well that would impair the economics of a contemplated deeper prospect might, in some cases, constitute waste or impair correlative rights, there is not sufficient evidence to resolve this case on that basis.

(11) The presentations of the parties focused on the legal rights of the parties to drill and operate the proposed well.

(12) Both parties agreed that their rights to drill and operate are now governed by the JOA. The JOA provides that the operator, and only the operator, may conduct operations on the unit, except in the case where a non-operator proposes an operation, and the operator does not elect to participate in that operation. In that case, the participating non-operators may designate one of them to conduct the operation.

(13) In this case, Bold, a non-operator, proposed the drilling of the proposed well, and OXY, the operator, did not elect to participate. OXY's witness testified that OXY did not elect to participate because it believed that the prior letter agreement precluded Bold from making a proposal that required an election under the JOA. Bold disputes that contention. However, Bold does not dispute that it did not commence drilling the well within ninety days after the expiration of OXY's 30-day election time as provided in the JOA.

(14) If the Operator elects to participate in a proposed operation, the JOA clearly requires that the Operator commence the well within the prescribed 90-day period (or authorized extension), and that if it does not do so, a new proposal is required, regardless of the reason for the delay. Because the final sentence of paragraph VI.B.1 of the JOA, which imposes this requirement where the operator is a consenting party, is not repeated in paragraph VI.B.2 which imposes the same time requirement where the operator is not a consenting party, the JOA may be ambiguous as to the effect of failure

to commence the well within the 90-day period in the latter situation. However, it is difficult to conceive what reason the drafters of this form contract would have had for making consent or non-consent elections binding for only 90 days if the operator consented, but binding indefinitely if the operator did not consent.

(15) Regardless of the possible ambiguity of the JOA in this respect, Bold apparently does not now contend that OXY is bound by its failure to elect to participate in the proposed well pursuant to the November 27 proposal. To the contrary, Bold's witness not only repeatedly testified that Bold was willing to make a new proposal, but definitely stated that Bold would make such a proposal as soon as possible after the hearing. In view of this testimony, the Division need not be concerned with the possible ambiguity in the JOA, but can treat this case as one where the non-operator has declared an intention to propose a well under the JOA, but has not yet done so.

(16) The Division has no power to determine contractual rights. However, its decision to grant or deny an APD may affect the exercise of those rights.

(17) The courts of New Mexico have not decided any case which has involved the granting or withholding of an APD in a case that involved disputed titles or contractual rights.

(18) The Supreme Court of Texas, in *Magnolia Petroleum Co. v. Railroad Com'n*, 141 Tex 96, 170 SW2d 189 (1943), held that the Texas Railroad Commission could grant a drilling permit to an operator whose title was disputed, so long as that operator had a good faith claim to the land in question. That court reasoned that a permit from the Railroad Commission did not grant the operator a legal right to drill a well if it did not have the necessary property right. The Court noted, however, that "the Commission should deny the permit if it does not reasonably appear to it that the applicant has a good-faith claim in the property." 170 SW2d at 191.

(19) In this case, Bold's property right is not disputed. However, its right to exercise that property right by physically conducting operations on the land is subject to a condition precedent that it apparently does not dispute. It must first propose the well to the other parties to the JOA, and then its right to conduct operations arises if, but only if, the operator (OXY) elects not to participate. At the time of hearing, these events had not yet occurred. Accordingly it does not appear that Bold had a good faith basis for asserting, or even that it did assert, that it has a present legal right to enter the property to drill this well.

(20) This case is similar to Case No. 13215, decided by the New Mexico Oil Conservation Commission ("the Commission"). In that case an operator applied for permits to re-enter abandoned **geothermal** wells located on land the surface of which was controlled by the United States Forest Service. There, as here, the **applicant's** title to an

undivided mineral interest was undisputed. However, under applicable federal law, the applicant was required to obtain a surface use permit from the Forest Service prior to conducting operations on the land. At the time of the hearing, it had not done so. In Order No. 12093-A, entered on February 12, 2004, the Commission rejected the application, concluding that it was premature because the conditions necessary to the applicant's right to conduct operations had not occurred and might never occur. See Order R-12093-A, Finding Paragraphs 21 and 24. This decision appears to control the present case as it was presented in this record.

(21) Accordingly, **Bold's** application for APD approval should be denied, without prejudice to its **reassertion** should the conditions precedent to its right to conduct operations on the property be satisfied.

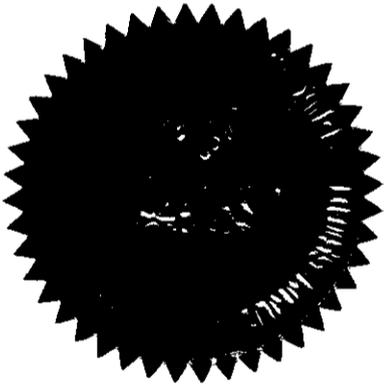
IT IS THEREFORE ORDERED THAT:

(1) The application of Bold Energy, LP for an APD for approval of its proposed OXY Checker State Well No. 2 is denied, without prejudice.

(2) It is assumed that if Bold can demonstrate that it has proposed this well in accordance with the terms of the JOA and OXY has not elected to participate, the **Artesia** District Office of the Division will approve an APD for this well without the necessity of a further hearing, unless OXY or some other party files an application requesting denial of the APD. Otherwise, this Order is not intended to suggest what decision the Division would make on any state of facts other than that shown at the hearing of this case.

(3) 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.



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STATE OF NEW MEXICO
OIL CONSERVATION DIVISION

A handwritten signature in black ink, appearing to read 'M. E. Fesmire'.

MARK E. FESMIRE, P.E.
Director