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

APPLICATION OF VENDERA RESOURCES III, LP, VENDERA MANAGEMENT III, LLC AND HIGHMARK OPERATING, LLC TO APPROVE A FORM C-145 NAMING HIGHMARK ENERGY OPERATING, LLC AS THE SUCCESSOR OPERATOR OF THE CENTRAL VACUUM UNIT, LEA COUNTY, NEW MEXICO.

CASE NO. 21704

CHEVRON U.S.A. INC.'S REPLY IN SUPPORT OF ITS MOTION TO DISMISS

Chevron U.S.A. Inc. ("Chevron") submits this reply in support of its Motion to Dismiss Vendera's Application in Case No. 21704. For the reasons stated below and in Chevron's Motion, Vendera's application should be dismissed.

INTRODUCTION

Vendera's response offers no valid basis to deny Chevron's motion to dismiss. There can be no dispute, and Vendera makes none, that before the Division can grant Vendera the relief sought in its application, it will have to resolve multiple hotly contested matters of contract interpretation. Vendera mistakenly asserts that the Statutory Unitization Act allows the Division to do this, but it does not. Instead, the Act expressly limits the Division's jurisdiction, power, and authority to matters relating to obtaining greater ultimate recovery, prevention of waste, and the protection of correlative rights.

Recognizing that the Division does not have the power to adjudicate the contract disputes between the parties, Vendera raises for the first time in its response allegations of waste and impairment of correlative rights. Having failed to raise these allegations in its application, they are not only irrelevant and immaterial, but also raise substantive issues regarding Vendera's

application and notice that, under the Division's guidance and regulations, independently require dismissal.

Lastly, Vendera relies on inapposite Division cases to support its position. The cases cited do not stand for the proposition that the Division has authority to decide private contractual disputes regarding the validity and effectiveness of votes to remove and replace an operator.

None of Vendera's arguments have merit, and Chevron's motion should be granted.

ARGUMENT

A. The Statutory Unitization Act Limits the Division's Jurisdiction, Power, and Authority to Matters that Relate Only to Increasing Ultimate Recovery, Prevention of Waste, and Protection of Correlative Rights.

Vendera incorrectly contends that the Statutory Unitization Act authorizes the Division to decide a private contractual dispute over the validity and effectiveness of votes purporting to remove Chevron as operator and select HighMark Energy as successor operator. The express language of the Act, conferring limited jurisdiction and authority on the Division, forecloses that argument.

Contrary to Vendera's interpretation, the Act does not specially empower the Division to decide disputed private contractual matters, such as removal and selection of a successor operator. The Act expressly provides that, "[s]ubject to the limitations of the [Act], the Division's "jurisdiction, power and authority" is "to make and enforce such orders and do such things as may be necessary or proper to carry out and effectuate the purposes of the [Act]." *See* § 70-7-3 (emphasis added). The Legislature explicitly limited the purposes of the Act to obtaining greater ultimate recovery, preventing waste, and protecting correlative rights. *See* § 70-7-3.

As provided by the Legislature, the express purposes of the Act therefore limit the Division's jurisdiction and authority to making independent findings and determinations

on matters related to increasing ultimate recovery, preventing waste, and protecting correlative rights. Vendera highlighted this provision of the Act in its response[1] but did not explain that the purposes of the Act actually limit the Division's jurisdiction and authority to its traditional areas of expertise in technical oil and gas matters. This limitation precludes the Division from entertaining, let alone deciding, a private contractual dispute between Chevron and Vendera over whether purported votes to remove and replace Chevron as operator of the Central Vacuum Unit were valid and effective.

In its correspondence with the Division, Vendera acknowledges and confirms that its dispute with Chevron, and the relief requested, is purely contractual in nature. *See* Correspondence from C. Lensing to E. Ames, dated January 13, 2021, at p. 3, attached as **Exhibit A** ("Vendera and HighMark respectfully request your assistance and guidance to effectuate the contractual rights exercised by the Working Interest Owners of the CVU when they voted to remove Chevron and replace it with HighMark." (emphasis added)). Determination of such disputes falls outside the scope of the Division's limited jurisdiction and authority prescribed by the Act.

Vendera nevertheless suggests that because the Act requires Division orders approving statutory units to include provisions for the selection, removal, or substitution of an operator and for voting procedures, it necessarily authorizes the Division "to determine the operator of the CVU." *See* Vendera Resp. at 4, ¶ 12; *see also* § 70-7-7(G) & (H). That contention misreads the statute and ignores the express limitations imposed on the Division's jurisdiction.

[1] *See* Vendera's Response at 3, ¶ 10.

Read as a harmonious whole, the Act's express limitations authorize the Division to make independent findings and determinations only on matters within its delegated jurisdiction and authority. *See State v. Wilson*, 2010-NMCA-018, ¶ 9, 228 P.3d 490 (stating that statutes "must be read as a whole, construing each section so as to produce a harmonious whole"). As to Section 70-7-7(G) and (H), the Act merely requires that unit agreements approved by the Division include certain prescribed provisions, which include mechanisms so unit operations and management may continue beyond the original operator. These provisions do not separately empower the Division to decide a disputed operatorship. To read such authority into these statutory provisions would contravene the express limitations imposed by the language of the Act itself.

The Act thus makes no allowance for the Division to decide the validity or effectiveness of a voting procedure or purported removal of an operator. The express limitations imposed by the Legislature are dispositive of the issue and confirm that the Division has no power to decide such matters.

1. The Division has no Jurisdiction or Authority to Decide "Private Rights" in a Contractual Dispute Between Parties to a Unit Agreement.

The Division does not have jurisdiction to determine "private rights" regarding a contractual dispute between parties regarding the validity and effectiveness of a vote to remove and replace Chevron.

Under its Legislative grant, the Division has jurisdiction and authority only to determine "public rights" relating to the public issue of conservation of oil and gas and the prevention of waste, not private contractual rights between parties to a unit agreement. *See, e.g.*, *Hartman v. El Paso Nat. Gas Co.*, 1988-NMSC-080, ¶¶ 29-31, 763 P.2d 1144 (recognizing distinction between "public rights vs. private rights" with respect to the

Division) (citing *Tenneco Oil Co.*, 687 P.2d 1049). Its express powers extend to preventing waste and protection of correlative rights, not the adjudication of private rights between parties to a unit agreement. *See, supra*, Pt. A; *see also Marbob Energy Corp. v. New Mexico Oil Conservation Comm'n*, 2009-NMSC-013, ¶ 2, 206 P.3d 135.

In general, "[r]espective rights and obligations of parties are to be determined by the district court." *Tenneco Oil Co.*, 687 P.2d at 1053; *see also Samson Res. Co. v. Oklahoma Corp. Comm'n*, 742 P.2d 1114, 1116. "The Oil Conservation Commission is a creature of statute, expressly defined, limited and empowered by the laws creating it." *Santa Fe Expl. Co. v. Oil Conservation Comm'n of State of N.M.*, 1992-NMSC-044, ¶ 27, 835 P.2d 819.

The Division thus has no jurisdiction or authority to rule on a dispute, between private parties, over contractual provisions governing the removal and selection of unit operators or the voting procedures at issue.

B. Vendera's Arguments Regarding Waste and Impairment of Correlative Rights Are Immaterial Because the Application Makes No Such Allegations as a Basis for its Change of Operator Request.

Vendera's application asks the Division to substitute HighMark as operator of the Central Vacuum Unit pursuant to the Division's authority under 19.15.9.B NMAC, not over concerns for waste or impairment of correlative rights. In its application, Vendera makes no allegations regarding waste or correlative rights as a basis for Chevron's removal. It merely alleges that enough working interest owners voted to remove Chevron as operator and to select HighMark as the new operator under the governing unit agreement that the Division should approve the requested operator change without Chevron's consent. *See* Vendera Application at ¶ 7, Case No. 21704.

Having brought no allegations of waste or impairment of correlative rights in its application, Vendera's arguments raised in response to Chevron's motion regarding such purported concerns, along with the attached exhibits, are immaterial and irrelevant to the matter. *See* Rule 11-401 NMRA (limiting what is "relevant" to facts that are "of consequence in determining the action"). Here, because Vendera's application limited its request to invoke the Division's authority under 19.15.9.B NMAC, where the C-145 is not signed by the current operator of record, arguments regarding waste and correlative rights have no bearing on a decision. The Division must ignore them.

C. Vendera's Failure to Allege Waste and Impairment of Correlative Rights Requires Dismissal Under the Division's Written Guidance and Notice Rules.

The Division's written guidance provides that matters material to an application but not identified in the application constitute a deficiency, justifying dismissal. *See* OCD's Notice on Material Changes or Deficiencies in Applications Submitted to the OCD Engineering Bureau, Effective June 11, 2020.

Vendera's allegations of waste and impairment of correlative rights were not included in its application. In its response to Chevron's motion to dismiss, Vendera now relies on these missing allegations as a basis for the Division's "jurisdiction and authority to remove Chevron as operator of the CVU." *See* Vendera Resp. at 5, ¶ 19. But having failed to include them in its application, Vendera cannot now rely on them as a basis for its requested relief. To do so demands dismissal under the Division's written guidance because the allegations are purportedly "of consequence" to Vendera's application but were not included.

In addition, the failure to identify the allegations in Vendera's application raises substantive notice issues under the Division's written guidance and the rules governing

adjudicatory hearing notice. Division guidance requires dismissal if the "nonexistence" of the allegation is of consequence to the public notice. Division rules also require a "reasonable identification of the adjudication's subject matter that alerts persons who may be affected[.]" 19.15.4.10.A(6) NMRA.

The recent allegations of waste and impairment of correlative rights significantly change the basis for Vendera's application and its requested relief from the stated reliance on 19.15.9.B NMAC. The failure to include the allegations in the application is a material deficiency that independently justifies dismissal because the application and notice failed to alert Chevron, and the public, that Vendera's application would rely on such allegations.

D. Reliance on Matador Case No. 15772 is Misplaced Because it Involved Issues Implicating Only the Division's Authority to Prevent Waste and Protect Correlative Rights, Not a Dispute Over Private Contractual Provisions.

Vendera's reliance on Case No. 15772 and its resulting order in support of using 19.15.9.B NMAC as the basis for the removal and replacement of Chevron as unit operator is misplaced. The facts and order in that case make it entirely inapposite.

Case No. 15772 did not involve a dispute over a private contractual agreement. Unlike the circumstances in this case, no disputed private contractual provisions, mechanisms, or rights were at issue at all. The allegations raised by Matador in its application in Case No. 15772 also squarely and solely invoked the Division's authority to act to prevent waste and protect correlative rights. Unlike Vendera's application here,[2] Matador did not ask the Division to rule on a purely private, contractual dispute.

[2] *See* Vendera Application Case No. 21704 at ¶¶ 3-7.

In Case No. 15772, Matador alleged in its application that the operator of an out-of-compliance, inactive well on an expired lease had failed to comply with the provisions of a settlement agreement with the Division. *See* Application Case No. 15772, attached as **Exhibit B**. Because the operator's lease had expired,[3] the well was inactive and out of compliance, and the operator had violated the terms of the Division's settlement agreement, the operator had no legal right to operate the well. *See id.* at 3, ¶ 9. The operator nevertheless refused to properly plug and abandon its well and refused to transfer operatorship to Matador so Matador could properly plug and abandon it. The inactive well interfered with Matador's ability to complete and produce its proposed horizontal well in the same zone. Unless the well was properly plugged and abandoned it would impair Matador's correlative rights and cause waste because Matador was not able to access the remaining reserves in the same zone. *See generally*, Exhibit B.

After notice and hearing, at which Matador presented extensive evidence and testimony on the status of the expired lease and inactivity of the well and the Division confirmed that the operator and well were out of compliance and had no right to produce the well, the Division entered Order No. R-14183-A making Matador operator of the well. Critically, the Division determined that approving the change of operator would allow for the proper abandonment of the inactive well and for Matador to drill its proposed horizontal well, "thereby preventing waste, and protecting correlative rights." *See* Order No. R-14183-A, ¶ 16, attached as **Exhibit C**.

Conversely, Vendera has made no allegations in this case of waste or impairment of correlative rights in its application. *See, supra*, Pt. B and C. The issue here is whether

[3] The operator presented no conflicting evidence that its lease remained in good standing. *See* Order No. R-14183-A, ¶ 14.

the purported votes to remove Chevron and to select HighMark Energy are valid and effective under the governing unit agreement. As discussed above, that issue is beyond the jurisdiction and authority for the Division to decide. But even if Vendera had properly alleged waste and impairment of correlative rights in its application, the Division still would be without authority to decide operatorship in this matter because change of operatorship is governed by a private, contractual provision over which the Division has no jurisdiction or authority.

CONCLUSION

For the reasons stated, Chevron U.S.A. Inc. respectfully requests that the Division grant its Motion to Dismiss, deny Vendera or HighMark operatorship of the CVU, and reject any Form C-145 submitted by Vendera or HighMark without Chevron's consent and signature.

Respectfully submitted,

HOLLAND & HART, LLP

Michael H. Feldewert
Adam G. Rankin
Julia Broggi
Kaitlyn A. Luck
Post Office Box 2208
Santa Fe, New Mexico 87504
TEL: (505) 988-4421
FAX: (505) 983-6043 Facsimile
mfeldewert@hollandhart.com
agrankin@hollandhart.com
kaluck@hollandhart.com

ATTORNEYS FOR CHEVRON U.S.A. INC.

CERTIFICATE OF SERVICE

I hereby certify that on March 24, 2021, I served a copy of the foregoing document to the following counsel of record via Electronic Mail to:

James Bruce
Post Office Box 1056
Santa Fe, New Mexico 87504
505-982-2043
jamesbruc@aol.com

Attorney for Vendera Resources III, LP and Vendera Management III, LLC and HighMark Energy Operating, LLC

Adam G. Rankin

EXHIBIT A

2626 Cole Ave., Suite 750, Dallas, TX, 75204
www.venderaresources.com

PO Box 9307, Tyler, TX, 75711
www.highmarkenergyoperating.com

January 13, 2021

***Via Electronic Mail*: eric.ames@state.nm.us**
Eric Ames, Attorney
New Mexico Energy, Minerals and Natural Resources Department
Oil Conservation Division
1220 South St. Francis Drive
Santa Fe, New Mexico 87505

Re: Transition from Chevron (removed Unit Operator) to HighMark (selected Successor Unit Operator) for Central Vacuum Unit, Lea County, New Mexico

Dear Mr. Ames:

This letter is on behalf of Vendera Resources III, LP, Vendera Management III, LLC (collectively "Vendera") and HighMark Energy Operating, LLC ("HighMark"), OGRID No. 330412, to request the OCD's assistance and guidance in facilitating the transition of removed Unit Operator Chevron U.S.A., Inc. ("Chevron") to HighMark as the selected Successor Unit Operator for the Central Vacuum Unit ("CVU") situated in Lea County, New Mexico.

Chevron has been removed as Unit Operator, and HighMark was selected as Successor Unit Operator and accepted in writing its duties and responsibilities. The only remaining step is for HighMark's selection to be approved by the Commissioner. As explained below, the State Land Office has indicated that communications about HighMark's approval are premature until the OCD "approves a change in operator for the unit wells." Unfortunately, Chevron has thus far not acknowledged its removal or HighMark's selection. Chevron has refused to sign the C-145 and has therefore impeded HighMark's ability to submit the C-145 under traditional circumstances. Vendera and HighMark request your help in effectuating the transition from Chevron to HighMark, including in providing any necessary additional approvals.

A. Chevron operated the CVU deficiently.

The field that ultimately became the CVU was discovered in the 1930s, began water flooding in the 1970s, and was turned to a CO2 flood in the 1990s. The CVU consists of approximately 90 active injection wells and 90 active producing wells that are producing from the Grayburg-San Andres Formations, at a relatively shallow depths of ~5,000 feet.

Chevron's operation of the CVU properties and treatment of its Working Interest Owners has been to Chevron's significant monetary gain, and to the great monetary loss and detriment of the Working Interest Owners and all other beneficiaries of the natural resource royalties generated by the CVU, including the State of New Mexico. After an operational history patterned with a lack of transparency and high-cost operations, Chevron as Unit Operator for the CVU, during the 2020 historic oil price downturn and world-wide pandemic, and continuing to this day, was and remains an absentee high-cost operator that refused to honor even simple data requests from its working

interest partners to which they have a right under the Unit Operating Agreement – Chevron would only allow the Working Interest Owners access to this critical information through an audit that would not be scheduled for at least eight months causing further undue delay and damage. Chevron refused to fulfill its obligations as Unit Operator and ordered its partners to communicate strictly with its outside counsel. Per records that Vendera has been able to review, the last general working interest owner meeting was in March of 2012, nearly 9 years ago.

There was a lack of organizational structure and focus from Chevron, and this is because it had no dedicated team to manage the CVU. There have been many instances of personnel turnover since 2018 and it is evident that Chevron's operations, engineering, accounting and commercial departments are disjointed and inefficient as to the CVU. There was no incentive for Chevron to optimize vendor costs, and due to Chevron's portfolio of assets across the mid-continent and globally, supply chain efforts to manage companywide vendor contracts limits the ability of Chevron to tailor a solution for the CVU. In fact, the CVU has become an afterthought for Chevron given in 2020 it was actively in late-term discussions to sell the CVU and other Vacuum properties, prior to the price crash. In addition to its lack of focus, Chevron's intrinsically high-cost operational structure has and will continue to lead to wasted and stranded reserves that will not be economically recoverable. This directly harms both the Working Interest Owners and the State of New Mexico as a mineral owner.

From a production standpoint, the CVU historically demonstrated a relatively flat production decline. However, due to slow or non-existent reactions from Chevron, the unit has realized a precipitous nearly 30% drop in oil production since 2018 – in 2018 the net CVU production was ~3,000 BOEPD whereas recent production records reflect 2,150 BOEPD. As an example, in the first half of 2018, there were 10+ injector wells that failed mechanical integrity tests, causing a 60% drop in CO2 injection. Instead of reacting and allocating available resources to the CVU mechanical integrity test failures, Chevron prioritized its unconventional program and allocated its rigs to other Chevron owned non-CVU properties. This lack of prioritization of the CVU led to a nine-month delay (causing the 60% drop in CO2 injection), and injection pattern dynamics were altered due to the operational downtime and field production had an observable trend in worsening declines. Chevron's inattentive operations and preferential treatment to non-CVU properties caused the demonstrable production destruction and further evidences harm to the Working Interest Owners and the State of New Mexico.

Most recently, since the pandemic began in March through only August 2020, and despite historically low commodity prices, Chevron, on a gross basis, produced approximately 370,000 barrels of oil and 112,000 barrels of plant products from the CVU alone. Despite generating negative cashflows to its Working Interest Owners, Chevron continued to produce and waste the CVU reserves even though oil prices reached historic lows and entered negative territory.

B. The Working Interest Owners removed Chevron and Selected HighMark.

The Unit Agreement authorizes Chevron's removal without cause – even though there is abundant evidence justifying Chevron's removal as the Unit Operator of the CVU. The Working Interest Owners made the prudent business decision (exercise their contractual right to remove and replace Chevron) and as such 12 out of 14 of the CVU Working Interest owners (representing over

90% of the Voting Interest after excluding Chevron's interest) voted to remove Chevron as Unit Operator and replace it with a low-cost prudent operator, HighMark.

HighMark has a proven history and proposes a focused asset management team that can optimize value for the CVU Working Interest Owners. HighMark will reduce lease operating expenses across the board; from field operations review and route optimization, to rebidding all services and evaluating all chemical changes and usage, to CO2 optimization – pattern reallocations and retiring mature patterns. Unlike Chevron, HighMark will not use the CVU as a training ground for its junior engineers. Instead, it will employ only fundamental and value add work. HighMark has already bid out and received quotes for operation of the CVU in preparation for taking over operations, and it would on average be 50% less expensive of an operator compared to Chevron. HighMark's low-cost, focused operations will directly correlate to an uplift in recoverable reserves and bolster the life span of the field, creating inherent value therein to the Working Interest Owners and the State of New Mexico.

C. Vendera and HighMark request the OCD's assistance and guidance in effectuating the transition.

During November and December 2020, communications were exchanged between Vendera and Chevron, as well as between both Vendera and Chevron and Ari Biernoff, General Counsel for the New Mexico State Land Office, concerning Chevron's removal as Unit Operator and replacement with HighMark as Successor Operator. Additionally, Chevron submitted a letter to Ms. Adrienne Sandoval of the Oil Conservation Division ("OCD") addressing this matter on December 3, 2020.

Despite being properly removed as a matter of law under the Unit Agreement by a vote of 90% of the Working Interest Owners (after excluding the Voting Interest of Chevron as the Unit Operator) and replaced by HighMark as the selected Successor Unit Operator, Chevron persists in unilaterally rejecting its removal and replacement. Vendera and HighMark write to you today after Vendera's most recent correspondence with Mr. Biernoff on January 5, 2021, wherein Mr. Biernoff accurately stated that no party had submitted the required applications for a change in operator for the CVU, such that our communications with him were premature until the OCD "approves a change in operator for the unit wells."

Under ordinary circumstances, a C-145 application submitted through the OCD's online permitting platform may presumably only be approved by the OCD if the application includes the certification and signature of both the current operator (Chevron) and the new operator (HighMark). HighMark has completed the C-145 to the extent possible, save Chevron's unwillingness to certify and sign the C-145. Chevron's refusal to recognize its removal as Unit Operator renders it impossible for HighMark to submit the C-145 application under traditional circumstances. Vendera and HighMark respectfully request your assistance and guidance to effectuate the contractual rights exercised by the Working Interest Owners of the CVU when they voted to remove Chevron and replace it with HighMark. Specifically, we request an avenue of relief whereby Chevron's certification and signature are not required to transfer operations of the CVU to HighMark, given Chevron will not provide such willingly.

EXHIBIT A

For background purposes, I have attached (i) the CVU Unit Agreement and Unit Operating Agreement, (ii) the chronological dialogue between Vendera, Chevron and the New Mexico State Land Office, and (iii) the letter to the OCD from Chevron. We look forward to working with you and your office on this matter.

Should you have any questions, please contact me.

Respectfully Submitted,

Vendera Resources III, LP and Vendera Management III, LLC

Collin Lensing

By: Collin Lensing
Title: COO & General Counsel

HighMark Energy Operating, LLC

Mark Land

By: Mark Land
Title: President

cc: Ari Biernoff *(on behalf of the NMSLO, via email)*
Adam G. Rankin. Esq. *(on behalf of Chevron, via email)*
Jason A. Newman, Esq. *(on behalf of Chevron, via e-mail)*

EXHIBIT B

BEFORE THE NEW MEXICO OIL CONSERVATION DIVISION

APPLICATION OF MATADOR PRODUCTION COMPANY AND MRC PERMIAN COMPANY TO REQUIRE LANEXCO INC. TO PLUG AND ABANDON THE CERRO COM. WELL NO. 1, OR IN THE ALTERNATVE TO REMOVE LANEXCO INC. AS OPERATOR OF RECORD OF THE CERRO COM. WELL NO. 1, EDDY COUNTY, NEW MEXICO. **Case No.** 15772

APPLICATION

Matador Production Company ("Matador") and MRC Permian Company ("MRC") apply for an order (i) requiring Lanexco Inc. ("Lanexco) to commence, within thirty days after entry of the requested order, the plugging and abandonment of the Cerro Com. Well No. 1, or (ii) in the alternative, removing Lanexco as operator of record of the Cerro Com. Well No. 1 and approving Matador as operator, and in support thereof, states:

1. Lanexco is the operator of record of the Cerro Com. Well No. 1 (API No. 30-015-22626), located 2080 feet from the north line and 760 feet from the west line (Unit E) of Section 11, Township 23 South, Range 27 East, N.M.P.M.

2. Lanexco is not in good standing with the Division.

3. MRC is the owner of fee oil and gas leases covering lands in the N/2 of Section 11. Matador (OGRID No. 228937) is the operating entity for MRC, and it is a registered operator in good standing with the Division.

4. The Cerro Com. Well No. 1 was completed in the Morrow formation in 1978, with the W/2 of Section 11 dedicated to the well. It was subsequently completed in the Wolfcamp formation (in two different zones) and was then completed in the Bone Spring formation. Lanexco obtained a downhole commingling order (DHC-774) from the Division in

EXHIBIT B

1990. According to Division records, the well is still open in both the Bone Spring and Wolfcamp formations.

5. The last reported production from the Cerro Com. Well No. 1 was in November 2011. Therefore, all oil and gas leases which were previously held by production from the well have expired.

6. Due to the inactivity of the Cerro Com. Well No. 1 and the failure of Lanexco to file production reports, the Division notified Lanexco that it had revoked its authority to transport or inject as to all of its wells in New Mexico. Thereafter the Division filed an application (Case No. 15446) for a compliance order against Lanexco. Order No. R-14183 dismissed the case due to a Settlement Agreement between Lanexco and the Division dated June 8, 2016 (attached hereto as **Exhibit A**). The agreement required, among other things, that (i) Lanexco file all past due production reports, (ii) continue to file production reports even if there is no production from the well, (iii) meet the financial assurance requirements of Division regulations, and (iv) bring inactive wells into compliance. Lanexco has not complied with any of the provisions of the Settlement Agreement.

7. Applicant proposes to drill its Michael Collins 11-23S-27E RB Well No. 206H, a horizontal well, to a depth sufficient to test the Wolfcamp formation (Purple Sage-Wolfcamp Gas Pool), with the N/2 of Section 11 dedicated to the well.

8. Matador has obtained Order No. R-14332 from the Division pooling the N/2 of Section 11 so that it may drill the Michael Collins 11-23S-27E RB Well No. 206H. In the process of preparing to drill its well, Matador discovered that the Cerro Com. Well No. 1 was not plugged and abandoned in accordance with Division regulations. The Cerro Com. Well No. 1

EXHIBIT B

must be plugged and abandoned so that Matador can safely and properly drill and complete the Michael Collins 11-23S-27E RB Well No. 206H.

9. Lanexco has no legal right to produce the Cerro Com. Well No. 1; all it possibly owns is the right to remove equipment related to the well. It also has the obligation under the Oil and Gas Act and Division regulations to properly plug and abandon the well.

10. Matador and MRC have contacted Lanexco regarding the issues related to the unplugged status of the Cerro Com. Well No. 1, but Lanexco has taken no action to correct this situation.

11. In order to prevent waste and protect correlative rights, Lanexco must be required to take prompt action to properly plug and abandon the Cerro Com. Well No. 1. In the alternative, Lanexco should be removed as operator of the well by the Division, and Matador should be named operator of the Cerro Com. Well No. 1 so that it may plug and abandon the well before drilling its well.

WHEREFORE, applicants request that, after notice and hearing, the Division enter its order:

A. Requiring Lanexco to commence the plugging and abandonment of the Cerro Com. Well No. 1 within thirty days after entry of the order; and/or

B. Removing Lanexco as operator of the Cerro Com. Well No. 1 and approving a change of operator to Matador; and

C. Granting such further relief as the Division deems proper.

EXHIBIT B

Respectfully submitted,

James Bruce
Post Office Box 1056
Santa Fe, New Mexico 87504
(505) 982-2043

Attorney for MRC Permian Company and Matador Production Company

EXHIBIT C

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. 15772
ORDER NO. R-14183-A

APPLICATION OF MATADOR PRODUCTION COMPANY AND MRC PERMIAN COMPANY TO REQUIRE LANEXCO, INC. TO PLUG AND ABANDON THE CERRO COM WELL NO. 1, OR IN THE ALTERNATIVE, TO REMOVE LANEXCO, INC. AS OPERATOR OF RECORD OF THE CERRO COM WELL NO. 1, EDDY COUNTY, NEW MEXICO.

ORDER OF THE DIVISION

BY THE DIVISION:

This case came on for hearing at 8:15 a.m. on August 3, 2017, at Santa Fe, New Mexico, before Examiner Phillip R. Goetze.

NOW, on this 10th day of October, 2017, 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 of the subject matter.

(2) Matador Production Company and MRC Permian Company (collectively referred to as the "Applicant" or "Matador") seeks an order either (i) requiring Lanexco Inc. (the "Operator" or "Lanexco") to properly plug and abandon the Cerro Com Well No. 1 or (ii) removing Lanexco as operator of record of the well and designating Matador as operator, thereof.

(3) The Cerro Com Well No. 1 (the "Subject Well"; API No. 30-015-22626) is a gas well with a surface location of 2080 feet from the North line and 760 feet from the West line (Unit E) of Section 11, Township 23 South, Range 27 East, NMPM, in Eddy County, New Mexico.

(4) Matador appeared at the hearing through legal counsel and presented the following testimony:

(a) The Operator is registered under OGRID No. 13046 and is the operator of record for 51 wells in New Mexico, including the Subject Well.

(b) The Subject Well is a vertical gas well with an initial completion in the Morrow formation (in 1978) that was abandoned followed by shallower completions in the Wolfcamp formation in 1979 and in the Bone Spring formation in 1988.

(c) The Subject Well has two sets of open perforations: from 7404 feet to 7425 feet and from 9765 feet to 9817 feet. The perforations of the deeper zones have been properly isolated and abandoned as shallower zones were perforated.

(d) Applicant provided a summary of production history for the Subject Well noting that the last reported production was November 2011. Included in this summary were affidavits from mineral interest owners documenting the failure to offer any compensation for production in the period following November 2011.

(e) Applicant submitted a photographic record of a recent field inspection of the wellhead and related production equipment for the Subject Well. This record established the Subject Well as being shut in with the production equipment either in poor condition or inoperable.

(f) Applicant summarized the compliance effort by the Division involving Lanexco that includes the Subject Well:

(i) The Division issued a second letter of violation to the Operator on January 26, 2016, citing failure to file monthly production reports as required under Rule 19.15.7.24 NMAC. The letter revoked the authority to transport from or inject into all wells operated by Lanexco.

(ii) Subsequently, the Division's Compliance and Enforcement Bureau made application to obtain a compliance order to require Lanexco to fulfill numerous outstanding obligations under Division rules. The application was assigned Case No. 15446 and was heard before Division Examiners on May 12, 2016, and June 9, 2016.

(iii) The Bureau entered into a Settlement Agreement (under Case No. 15446) with Lanexco on June 9, 2016. Under the terms of the agreement, the Operator was required to complete the reporting of monthly production, provide adequate financial

assurance, and to either return inactive wells to beneficial use or properly plug and abandon them if unproductive.

(iv) The Division issued a letter of violation dated April 17, 2017, citing the Operator for not properly plugging and abandoning the Subject Well.

(g) Applicant provided a summary of the leasing history for the parcel containing the Subject Well and a chronology of Applicant's effort to obtain leases for the purpose of drilling a horizontal well. Applicant contended that leases held by Lanexco that are associated with the Subject Well are no longer valid.

(h) Applicant noted that portions of their leases within the N/2 of Section 11 will begin expiring on November 19, 2017, if the drilling of the Applicant's well is not commenced.

(i) Applicant has proposed the Michael Collins 11-23S-27E RB Well No. 206H (the "Applicant's well"), a horizontal well with a surface location 2051 feet from the South line and 405 feet from the East line (Unit I) of Section 11, Township 23 South, Range 27 East, NMPM. The Applicant's well is proposed to test the Wolfcamp formation at a true vertical depth of approximately 9350 feet.

(j) The proposed completed interval for the Applicant's well will be from east to west within the S/2 N/2 of Section 11. A portion of the completed interval will be located within 200 feet of the surface location of the Subject Well and closer to the open perforations in the Wolfcamp formation.

(k) Applicant presented testimony that the Subject Well, in its current status, has the potential of impacting the hydraulic fracturing results for the Applicant's well, thereby degrading the quality of the horizontal well completion, resulting in poor production and creating waste of hydrocarbon resources.

(l) Applicant provided a proposed plugging plan for the Subject Well and noted that plan had been submitted to Lanexco for consideration.

(m) Applicant referenced Case No. 15527, Division Order No. R-14228, as precedence for consideration in this case. The Division there designated a new operator for an existing, inactive well held through a prior claim by a different operator.

(5) Lanexco and the Compliance and Enforcement Bureau (the "Bureau") entered appearances through legal counsel and provided testimony regarding the application. No other party appeared at the hearing or otherwise opposed the granting of the application.

(6) Under cross examination by Lanexco, a witness called by Matador stated that it had not attempted to assess the potential of leases being held by production from wells other than the Subject Well. Lanexco's attorney further noted that Matador had not provided a copy of the title opinion used to assess lease status as part of Matador's exhibits.

(7) The Bureau offered no testimony as to the requests contained in the application, but stated in the record that the Subject Well was not compliant with the Division rules regarding plugging and abandonment and financial assurance.

(8) Based on Division records, the Division approved a compulsory pooling order, Order No. R-14332, for a 320-acre gas spacing unit in the Wolfcamp formation (Purple Sage; Wolfcamp (Gas) Pool) that encompasses the N/2 of Section 11, Township 23 South, Range 27 East, NMPM. The unit is dedicated to the Applicant's Michael Collins 11-23S-27E RB Well No. 206H.

The Division Concludes as Follows:

(9) Lanexco is the Operator of record for the Subject Well and is responsible for compliance with the Oil and Gas Act and Division Rules.

(10) The Subject Well qualifies as "inactive" because the well has not been used for beneficial purposes for a period that exceeds one (1) year plus 90 days and has not been placed in approved temporary abandonment status. The inactive Subject Well is classified with a status of "temporary abandonment" as defined in Division Rule 19.15.2.7(T)(3) NMAC.

(11) As established by the evidence provided at hearing, the Operator is in violation of Division Rule 19.15.8.9 NMAC. The Operator is required to have additional financial assurance on the Subject Well, as it has been in temporary abandonment for more than four years, and the Operator has failed to provide the Division with the requisite financial assurance for the Subject Well.

(12) The Settlement Agreement between Lanexco and the Bureau is still in effect, but there is no evidence, as of the date of the final hearing, that Lanexco has addressed either the financial assurance issue or the inactive well status of the Subject Well.

(13) The Division has issued Division Order No. R-14332 that authorizes the Applicant to pool all uncommitted mineral interests in the Wolfcamp formation for the unit which is the N/2 of Section 11 and includes a portion of the spacing unit previously dedicated to the Subject Well for production from the Wolfcamp formation.

(14) Although the Division does not have jurisdiction to determine the validity of, or title to, an oil and gas lease, Lanexco' s claim that leases associated with the Subject Well or other wells operated by Lanexco may be held by production is not substantiated by the evidence.

(15) Applicant has sufficiently demonstrated that the Subject Well offers a high probability for interference with the proper completion of the Applicant's well resulting in waste of resources and possible impacts on correlative rights.

(16) Approval of the change of operator to allow proper abandonment of the Subject Well will enable Applicant to drill a horizontal well that will efficiently produce the reserves underlying the unit, thereby preventing waste, and protecting correlative rights.

(17) The Division finds that Case No. 15527, Division Order No. R-14228, as a suggested precedent for ordering a change in operator in this case, is not applicable. However, NMSA 1978 §70-2-11(A) states:

> *"The division is hereby empowered, and it is its duty, to prevent waste prohibited by this act and to protect correlative rights, as in this act provided. To that end, the division is empowered to make and enforce rules, regulations and orders, and to do whatever may be reasonably necessary to carry out the purpose of this act, whether or not indicated or specified in any section hereof."* [Emphasis added]

(18) The evidence indicates that Lanexco failed to bring the Subject Well into compliance with Rule 19.15.25.8 NMAC by either plugging the well or placing the well into approved temporary abandonment status. The evidence further indicates that Lanexco failed to bring the Subject Well into compliance with Rule 19.15.8.9 NMAC (Financial Assurance). Given the lengthy period of non-compliance of Lanexco with regards to the Subject Well, the Division, in the course of its business, would normally bring a compliance action against Lanexco similar to the one Matador presented, requiring Lanexco to plug and abandon the Subject Well or place the well in approved temporary abandonment status, however, given that Lanexco has had ample opportunity to comply with Division rules, and given that the situation with Matador requires an expedient resolution of the issues surrounding the subject well and the drilling of the Michael Collins 11-23S-27E RB Well No. 206H, the application of Matador in this case should be approved.

(19) Division records indicate Matador, as of the date of this order, is in compliance with Division Rule 19.15.5.9 NMAC.

(20) The Division should approve the removal of Lanexco as operator of record for the Subject Well and designate Matador Production Company as operator for the purpose to plug and abandon the Cerro Com Well No. 1.

(21) In response to Applicant's request for compensation, the Division can only obligate financial assurance for the plugging and abandonment of a well conducted by the Division and not plugging operations completed by another operator.

IT IS THEREFORE ORDERED THAT:

(1) The Division hereby terminates the authority of Lanexco to act as Operator of record for the Cerro Com Well No. 1 (the "Subject Well"; API No. 30-015-22626) with a surface location of 2080 feet from the North line and 760 feet from the West line (Unit E) of Section 11, Township 23 South, Range 27 East, NMPM, in Eddy County, New Mexico.

(2) The application of Matador Production Company (OGRID No. 228937) to become the Operator of record for the Subject Well for the sole purpose of properly plugging and abandoning the Subject Well is hereby approved.

(3) Matador Production Company shall prepare and submit a sundry notice of intent with a plugging program to the Division's Artesia office for approval within thirty (30) days of the issuance date of this Order.

(4) As the Operator of record for the Subject Well, Matador Production Company shall be responsible for all costs associated with the plugging and abandonment of the well, including all the requirements of Division Rule 19.15.25.10 NMAC and all liabilities associated with any releases reported under Rule 19.15.29 NMAC, without compensation from the Division.

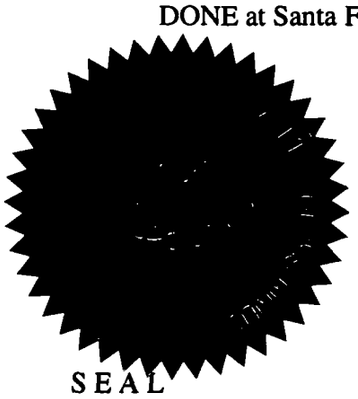
(5) The Division shall continue the implementation of the Settlement Agreement with Lanexco but shall exclude all subsequent violations and related fines associated with the Cerro Com Well No. 1 in any further compliance and enforcement activities.

(6) This Order shall become null and void if Lanexco Inc. and Matador Production Company agree to a Change of Operator, under Division Rule 19.15.9.9 NMAC, for the Subject Well. Final approval of the Change of Operator shall be subject to the approval of the Director after consultation with the Compliance and Enforcement Bureau.

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

EXHIBIT C

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



SEAL

STATE OF NEW MEXICO
OIL CONSERVATION DIVISION

David R. Catanach

DAVID R. CATANACH
Director