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. 10656
ORDER NO. R-9845

APPLICATION OF MITCHELL ENERGY CORPORATION FOR COMPULSORY POOLING AND AN UNORTHODOX GAS WELL LOCATION, LEA COUNTY, NEW MEXICO.

ORDER OF THE DIVISION

BY THE DIVISION:

This cause came on for hearing at 8:15 a.m. on January 21, 1993, at Santa Fe, New Mexico, before Examiner Michael E. Stogner.

NOW, on this 15th day of February, 1993, the Division Director, having considered the testimony, the record and the recommendations of the Examiner, and being fully advised in the premises,

FINDS THAT:

(1) Due public notice having been given as required by law, the Division has jurisdiction of this cause and the subject matter thereof.

(2) The applicant, Mitchell Energy Corporation ("Mitchell"), seeks an order pooling all mineral interests from the top of the Wolfcamp formation to the base of the Pennsylvanian formation, underlying the W/2 of Section 28, Township 20 South, Range 33 East, NMPM, Lea County, New Mexico, forming a 320-acre gas spacing and proration unit for all formations and/or pools developed on 320-acre spacing within said vertical extent, which presently includes, but is not necessarily limited to, the Undesignated Halfway-Atoka Gas Pool and the Undesignated South Salt Lake-Morrow Gas Pool.

(3) The applicant has the right to drill and proposes to drill its Tomahawk "28" Federal Com Well No. 1 at an unorthodox gas well location 1650 feet from the North line and 1980 feet from the West line (Unit F) of said Section 28.

(4) Strata Production Company ("Strata") appeared at the hearing in opposition to the granting of Mitchell's application.

(5) The operating rights (working interests) for all of Section 28, except the S/2 S/2 and the SW/4 NE/4, are subject to Joint Operating Agreement No. 1130 between Mitchell Energy Corporation, Santa Fe Energy Operating Partners, L.P., and Maralo Inc. designating Mitchell Energy Corporation as the operator. The SW/4 NE/4 is an unleased federal oil and gas tract. The S/2 SW/4 and SW/4 SE/4 is a federal oil and gas lease with record title and operating rights (no overriding royalty) held by Strata Production Corporation. The SE/4 SE/4 is a federal oil and gas lease held by Pitche Energy.

(6) Mitchell has proposed to all working interest owners the formation of the subject spacing unit and drilling of the subject well and has obtained the voluntary agreement of 75% of the working interest ownership in the subject spacing unit for the proposed well.

(7) At all times relevant hereto, the S/2 SW/4 which constitutes the remaining 25% working interest in the subject spacing unit has been under the ownership and control of Strata.

(8) Despite good faith efforts undertaken over a reasonable period of time, Mitchell has been unable to reach a voluntary agreement with Strata concerning voluntary participation in the subject spacing unit and the proposed well.

(9) Strata appeared at the hearing in opposition to Mitchell's proposed W/2 orientation of the spacing unit, the well location, and the overhead charges. In addition, Strata contended that Mitchell had failed to provide notification to Strata's "undisclosed partners" as identified on Mitchell Exhibit No. 17 in this case.

(10) In support of its motion for continuance, Strata claimed that Mitchell knew all along that Strata had "undisclosed partners" and it was Mitchell's duty to request Strata to disclose the names and addresses and then to provide those parties with an opportunity to join or compulsory pool each party.

On the notice issue raised by Strata, Mitchell presented exhibits and testimony which demonstrated that:

> *(a) abstracts and Title Opinions established that Strata held the record title and all operating rights to the S/2 SW/4 of said Section 28 as of the date the well was proposed to Strata (November 20, 1992), and as*

of the date Strata received notification of the compulsory pooling application (December 20, 1992), and as of the date of the hearing in this case;

(b) *by letter dated November 20, 1992 Mitchell proposed to Strata the subject well and proposed spacing unit requesting voluntary participation in the well or in the alternative, proposed farmout terms to Strata;*

(c) *on November 20, 1992, Mitchell was the first working interest owner in Section 28 to propose a Morrow gas well to the working interest owners;*

(d) *although Strata declined to participate in the well, during the next two months, Mitchell and Strata through numerous telephone calls and correspondence between the parties discussed other alternatives including Mitchell purchasing or farming in Strata's interest;*

(e) *Mitchell understood and believed that Strata was dealing for and on behalf of Strata and all of Strata's "undisclosed partners;"*

(f) *by letter dated December 30, 1992 (Mitchell Hearing Exhibit No. 12), Strata offered to sell Mitchell 100% of its record title and operating rights and this offer included representations that while Strata had "undisclosed partners" Strata had the right, power and authority to bind said undisclosed partners; and*

(g) *after negotiations between Mitchell and Strata failed, by letter dated January 13, 1993, Strata for the first time provided Mitchell with the names and addresses of Strata's fifteen "undisclosed partners." (Mitchell Hearing Exhibit No. 17), but no evidence was provided that these "partners" owned an interest in the mineral estate.*

FINDING: At all times during negotiations and at the time the application was filed and notice was given, Strata was the record title owner of the mineral interests in question and the Division has jurisdiction over the interest held in Strata's name.

(11) Mitchell has made a good faith effort to reach a voluntary agreement with the record owner of the interests and is entitled to compulsory pooling.

(12) It would circumvent the purposes of the New Mexico Oil and Gas Act to allow a party owning a working interest in the spacing unit at the time said party was served with a compulsory pooling application to avoid or delay having that entire percentage interest pooled by assigning, conveying, selling or otherwise burdening or reducing that interest after the application and notice of hearing are filed with the Division and served on the party.

(13) Strata's motion to continue for lack of notice to its "undisclosed partners" should be denied.

(14) Mitchell's estimated cost for a completed well is $1,377,300. with monthly overhead rates of $6,470 while drilling and $647 while producing.

(15) Strata stipulated to Mitchell's proposed estimate of well costs ("AFE") identified on Mitchell Exhibit No. 19 as fair and reasonable but requested the Ernst & Young tabulation of average overhead rates be applied in this case.

(16) Because a substantial majority of the working interest owners has agreed to overhead rates which have now escalated in accordance with COPAS procedures to be slightly in excess of the Ernst & Young average rates, the rates proposed by Mitchell are fair and should be adopted in this case.

(17) Based on the geologic evidence presented at the hearing, the orientation of the stand-up 320-acre spacing unit for the first well in said Section 28 serves to provide the best opportunity for full development of potential Pennsylvanian gas in the section with two wells.

(18) Because of a combination of archeological restrictions and surface use limitations, Mitchell has been unable to obtain approval from the United States Bureau of Land Management (BLM), which is the surface management agency for said section, for an acceptable standard gas well location in the W/2 spacing unit, and therefore seeks the proposed unorthodox location which it anticipates will satisfy all the requirements of the BLM.

(19) Approval of this application as set forth in the above findings and in the following order will serve to protect correlative rights, prevent waste and afford the owner of each interest in said unit the opportunity to recover or receive without unnecessary expense his just and fair share of the production in any pool resulting from this order.

(20) Mitchell Energy Corporation should be designated the operator of the subject well and unit.

(21) Any non-consenting working interest owner should be afforded the opportunity to pay his share of estimated well costs to the operator in lieu of paying his share of reasonable well costs out of production.

(22) Any non-consenting working interest owner who does not pay his share of estimated well costs should have withheld from production his share of reasonable well costs plus an additional 200 percent thereof as a reasonable charge for the risk involved in the drilling of the well.

(23) Any non-consenting interest owner should be afforded the opportunity to object to the actual well costs but actual well costs should be adopted as the reasonable well costs in the absence of such objection.

(24) Following determination of reasonable well costs, any non-consenting working interest owner who has paid his share of estimated costs should pay to the operator any amount that reasonable well costs exceed estimated well costs and should receive from the operator any amount that paid estimated well costs exceed reasonable well costs.

(25) $6470.00 per month while drilling and $647.00 per month while producing should be fixed as reasonable charges for supervision (combined fixed rates); the operator should be authorized to withhold from production the proportionate share of such supervision charges attributable to each non-consenting working interest, and in addition thereto, the operator should be authorized to withhold from production the proportionate share of actual expenditures required for operating the subject well, not in excess of what are reasonable, attributable to each non-consenting working interest.

(26) All proceeds from production from the subject well which are not disbursed for any reason should be placed in escrow to be paid to the true owner thereof upon demand and proof of ownership.

(27) Upon the failure of the operator of said pooled unit to commence drilling of the well to which said unit is dedicated on or before May 15, 1993, the order pooling said unit should become null and void and of no further effect whatsoever.

(28) Should all the parties to this force-pooling reach voluntary agreement subsequent to entry of this order, this order should thereafter be of no further effect.

(29) The operator of the well and unit should notify the Director of the Division in writing of the subsequent voluntary agreement of all parties subject to the force-pooling provisions of this order.

IT IS THEREFORE ORDERED THAT:

(1) The motion of Strata Production Company to continue this matter for lack of notice to its "undisclosed partners" as identified on Mitchell Energy Corporation's Exhibit No. 17 in this case is hereby **denied.**

(2) All mineral interests, whatever they may be, from the top of the Wolfcamp formation to the base of the Pennsylvanian formation, underlying the W/2 of Section 28, Township 20 South, Range 33 East, NMPM, Lea County, New Mexico, are hereby pooled to form a standard 320-acre gas spacing and proration unit for all formations and/or pools developed on 320-acre spacing within said vertical extent, which presently includes, but is not necessarily limited to the Undesignated Halfway-Atoka Gas Pool and the Undesiganted Salt Lake-Morrow Gas Pool, said unit to be dedicated to its Tomahawk "28" Federal Com Well No. 1 to be drilled at an unorthodox gas well location 1650 feet from the North line and 1980 feet from the West line (Unit F) of said Section 28.

PROVIDED HOWEVER THAT, the operator of said unit shall commence the drilling of said well on or before the 15th day of May, 1993, and shall thereafter continue the drilling of said well with due diligence to a depth sufficient to test the above-described area.

PROVIDED FURTHER THAT, in the event said operator does not commence the drilling of said well on or before the 15th day of May, 1993, Decretory Paragraph No. (2) of this order shall be null and void and of no effect whatsoever, unless said operator obtains a time extension from the Division for good cause shown.

PROVIDED FURTHER THAT, should said well not be drilled to completion, or abandonment, within 120 days after commencement thereof, said operator shall appear before the Division Director and show cause why Decretory Paragraph No. (2) of this order should not be rescinded.

(3) Mitchell Energy Corporation is hereby designated the operator of the subject well and unit.

(4) After the effective date of this order and within 90 days prior to commencing said well, the operator shall furnish the Division and each known working interest owner in the subject unit an itemized schedule of estimated well costs.

(5) Within 30 days from the date the schedule of estimated well costs is furnished to him, any non-consenting working interest owner shall have the right to pay his share of estimated well costs to the operator in lieu of paying his share of reasonable well costs out of production, and any such owner who pays his share of estimated well costs as provided above shall remain liable for operating costs but shall not be liable for risk charges.

(6) The operator shall furnish the Division and each known working interest owner an itemized schedule of actual well costs within 90 days following completion of the well; if no objection to the actual well costs is received by the Division and the Division has not objected within 45 days following receipt of said schedule, the actual well costs shall be the reasonable well costs; provided however, if there is an objection to actual well costs within said 45-day period the Division will determine reasonable well costs after public notice and hearing.

(7) Within 60 days following determination of reasonable well costs, any non-consenting working interest owner who has paid his share of estimated costs in advance as provided above shall pay to the operator his pro rata share of the amount that reasonable well costs exceed estimated well costs and shall receive from the operator his pro rata share of the amount that estimated well costs exceed reasonable well costs.

(8) The operator is hereby authorized to withhold the following costs and charges from production:

(A) The pro rata share of reasonable well costs attributable to each non-consenting working interest owner who has not paid his share of estimated well costs within 30 days from the date the schedule of estimated well costs is furnished to him; and

(B) As a charge for the risk involved in the drilling of the well, 200 percent of the pro rata share of reasonable well costs attributable to each non-consenting working interest owner who has not paid his share of estimated well costs within 30 days from the date the schedule of estimated well costs is furnished to him.

(9) The operator shall distribute said costs and charges withheld from production to the parties who advanced the well costs.

(10) \$6,470 per month while drilling and \$647 per month while producing are hereby fixed as reasonable charges for supervision (combined fixed rates); the operator is hereby authorized to withhold from production the proportionate share of such supervision charges attributable to each non-consenting working interest, and in addition thereto, the operator is hereby authorized to withhold from production the proportionate share of actual expenditures required for operating such well, not in excess of what are reasonable, attributable to each non-consenting working interest. The operator is hereby authorized to make annual adjustments of said combined fixed rates as of the first day of April each year in accordance with the COPAS accounting schedule utilized by the industry.

(11) Any unleased mineral interest shall be considered a seven-eighths (7/8) working interest and a one-eighth (1/8) royalty interest for the purpose of allocating costs and charges under the terms of this order.

(12) Any well costs or charges which are to be paid out of production shall be withheld only from the working interest's share of production, and no costs or charges shall be withheld from production attributable to royalty interests.

(13) All proceeds from production from the subject well which are not disbursed for any reason shall be placed in escrow in Lea County, New Mexico, to be paid to the true owner thereof upon demand and proof of ownership; the operator shall notify the Division of the name and address of said escrow agent within 30 days from the date of first deposit with said escrow agent.

(14) Should all the parties to this force-pooling reach voluntary agreement subsequent to entry of this order, this order shall thereafter be of no further effect.

(15) The operator of the subject well and unit shall notify the Director of the Division in writing of the subsequent voluntary agreement of all parties subject to the force-pooling provisions of this order.

(16) Jurisdiction of this cause 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.

STATE OF NEW MEXICO
OIL CONSERVATION DIVISION

WILLIAM J. LEMAY
Director

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