

**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. 13302
ORDER NO. R-5209-A**

**APPLICATION OF HEC PETROLEUM, INC. FOR COMPULSORY POOLING,
EDDY COUNTY, NEW MEXICO.**

ORDER OF THE DIVISION

BY THE DIVISION:

This case came on for hearing at 8:15 a.m. on July 22, 2004, at Santa Fe, New Mexico before Examiner Michael E. Stogner.

NOW, on this 4th day of August, 2004, 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) HEC Petroleum, Inc. ("HEC" or "Applicant") seeks an order pooling all uncommitted mineral interests from the surface to the base of the Morrow formation underlying the E/2 of Section 7, Township 22 South, Range 27 East, NMPM, Eddy County, New Mexico, to form a standard 320-acre stand-up deep gas spacing unit [Division Rule 104.C (2)] for any and all formations and/or pools developed on 320-acre spacing within that vertical extent, which presently include but are not necessarily limited to the Undesignated East Carlsbad-Wolfcamp Gas Pool (74160), Undesignated Carlsbad-Strawn Gas Pool (74040), Undesignated South Carlsbad-Strawn Gas Pool (74120), Undesignated Tansill Dam-Atoka Gas Pool (85900), and South Carlsbad-Morrow Gas Pool (73960).

(3) This unit is to be dedicated to the Applicant's proposed Douglas Com. Well No. 2 (API No. 30-015-33501) to be directionally drilled from a surface location 2460 feet from the North line and 300 feet from the East line (Unit H) of Section 7, to a standard bottomhole deep gas well location at a measured depth of approximately 12,071 feet (11,700 feet TVD) pursuant to Division Rules 104.C (2) (a), 104.C (2) (b), 111.A (7), and 111.C (2) within the SE/4 SE/4 (Unit P) of Section 7.

(4) The Applicant is a working interest owner within the subject 320-acre unit and therefore has the right to drill for and develop the oil and gas minerals underlying this unit.

(5) Gas production from the South Carlsbad-Morrow Pool underlying the E/2 of Section 7 is currently dedicated to HEC's Douglas Com. Well No. 1 (API No. 30-015-21802), located at an unorthodox deep gas well location 2410 feet from the North line and 560 feet from the East line (Unit H) of Section 7. This well is the subject of Division Order No. R-5209, issued in Case No. 5666 on April 27, 1976, which authorized the drilling of this well at an unorthodox (deep) gas well location and pooled all mineral interests in and below the Pennsylvanian formation underlying the E/2 of Section 7.

(6) By directional drilling its proposed infill Morrow deep gas well in the E/2 of Section 7, HEC will utilize the existing drill pad for its Douglas Com. Well No. 1 resulting in minimal surface disturbance and is necessary due to the close proximity of these wells to the City of Carlsbad.

(7) Two or more separately owned tracts are embraced within this 320-acre unit, and/or there are royalty interests and/or undivided interests in oil and gas minerals in one or more tracts included in the unit that are separately owned.

(8) There are certain mineral interest owners within this unit that have not agreed to pool their interests.

(9) No party affected by this application appeared at the hearing or objected to this application.

(10) To avoid the drilling of unnecessary wells, protect correlative rights, prevent waste, and afford to the owner of each interest in the unit the opportunity to recover or receive without unnecessary expense its just and fair share of hydrocarbons, this application should be approved.

(11) Applicant, who, pursuant to Division Rule 104.C (2) (c), is the current operator of the above-described Douglas Com. Well No. 1 and 320-acre deep gas spacing unit in the South Carlsbad-Morrow Gas Pool, should also be designated the operator of the proposed well.

(12) Pursuant to Division Rule 35.A, any pooled working interest owner who does not pay its share of estimated well costs should have withheld from production its share of reasonable well costs plus an additional 200 percent thereof as a reasonable charge for the risk involved in the drilling of the proposed Douglas Com. Well No. 2.

(13) Applicant proposed fixed overhead and administrative costs for its proposed Douglas Com. Well No. 2 to be \$6,473.99 per month while drilling and \$949.53 per month while producing.

(14) The latest available "*Fixed Rate Overhead Survey 2003-2004*," published by Ernst & Young, L.L.P. of Houston, Texas (available on the internet at: www.ey.com/us/energy), shows average overhead rates of \$5,167.00 per month while drilling (\$6,000.00 median) and \$631.00 per month while producing (\$600.00 median) for wells drilled to a depth of 12,500 feet in Eddy County, New Mexico.

(15) While the proposed drilling rate exceeds the published average, the Division has authorized \$6,500.00 in compulsory pooling orders for wells to similar depths in southeast New Mexico in the recent past. However, the proposed \$949.53 producing rate far exceeds the published average and the rate awarded operators in previous Division compulsory pooling orders.

(16) Applicant testified that the proposed \$949.53 producing well rate is necessary because the well will be a directional wellbore and is within a residential/city environment. Further, Applicant testified that the overhead charges for participating parties within the existing Douglas Com. Well No. 1 are currently subject to this producing well rate.

(17) Such overhead and administrative charges are deemed to be fair and reasonable and should therefore be included in the provisions of this order.

(18) Reasonable charges for supervision (combined fixed rates) should be fixed at \$ 6,473.99 per month while drilling and \$ 949.53 per month while producing, provided that these rates should be adjusted annually pursuant to Section III.1.A.3 of the COPAS form titled "*Accounting Procedure-Joint Operations*." The operator should be authorized to withhold from production from this well the proportionate share of both the supervision charges and the actual expenditures required for operating the well, not in excess of what are reasonable, attributable to each pooled working interest.

IT IS THEREFORE ORDERED THAT:

(1) Pursuant to the application of HEC Petroleum, Inc. (herein referred to as "Applicant"), all uncommitted mineral interests, whatever they may be, from the surface to the base of the Morrow formation at a measured depth of approximately 12,071 feet (11,700 feet TVD) underlying the E/2 of Section 7, Township 22 South, Range 27 East, NMPM, Eddy County, New Mexico, are hereby pooled to form a standard 320-acre stand-up deep gas spacing unit for any and all formations or pools developed on 320-acre spacing pursuant to Division Rule 104.C (2), which presently include, but are not necessarily limited to the Undesignated East Carlsbad-Wolfcamp Gas Pool (74160), Undesignated Carlsbad-Strawn Gas Pool (74040), Undesignated South Carlsbad-Strawn Gas Pool (74120), Undesignated Tansill Dam-Atoka Gas Pool (85900), and South Carlsbad-Morrow Gas Pool (73960).

(2) This 320-acre deep gas spacing unit shall be dedicated to the Applicant's proposed Douglas Com. Well No. 2 (API No. 30-015-33501) to be directionally drilled to the base of the Morrow formation from a surface location 2460 feet from the North line and 300 feet from the East line (Unit H) of Section 7, to a standard bottomhole deep gas well location, pursuant to Division Rule 104.C (2) (a), 104.C (2) (b), 111.A (7), and 111.C (2), within the SE/4 SE/4 (Unit P) of Section 7.

(3) Applicant is hereby designated the operator of the proposed well and of this unit.

(4) The operator of this unit shall commence drilling the proposed well on or before November 1, 2004, and shall thereafter continue drilling the well with due diligence to a depth sufficient to test the Morrow formation.

(5) In the event the operator does not commence drilling the proposed well on or before November 1, 2004, Ordering Paragraph (1) shall be of no effect, unless the operator obtains a time extension from the Division Director for good cause.

(6) Should the proposed well not be drilled and completed within 120 days after commencement thereof, the operator shall appear before the Division Director and show cause why Ordering Paragraph (1) should not be rescinded as to the proposed Douglas Com. Well No. 2.

(7) Upon final plugging and abandonment of the proposed well, the force-pooled unit created by this Order shall terminate, unless this Order has been amended to authorize further operations.

(8) After pooling, uncommitted working interest owners are referred to as pooled working interest owners. ("Pooled working interest owners" are owners of working interests in the unit, including unleased mineral interests, who are not parties to an operating agreement governing this unit.) After the effective date of this order, the operator shall furnish the Division and each known pooled working interest owner in the unit an itemized schedule of estimated well costs of drilling, completing, and equipping the proposed well ("well costs").

(9) Within 30 days from the date the schedule of estimated well costs is furnished, any pooled working interest owner shall have the right to pay its share of estimated well costs to the operator in lieu of paying its share of reasonable well costs out of production as hereinafter provided, and any such owner who pays its share of estimated well costs as provided above shall remain liable for operating costs but shall not be liable for risk charges. Pooled working interest owners who elect not to pay their share of estimated well costs as provided in this paragraph shall thereafter be referred to as "non-consenting working interest owners."

(10) The operator shall furnish the Division and each known pooled working interest owner (including each non-consenting working interest owner) an itemized schedule of actual well costs within 90 days following completion of the proposed 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 the schedule, the actual well costs shall be deemed to be the reasonable well costs. If there is an objection to actual well costs within the 45-day period, the Division will determine reasonable well costs after public notice and hearing.

(11) Within 60 days following determination of reasonable well costs, any pooled working interest owner who has paid its share of estimated well costs in advance as provided above shall pay to the operator its share of the amount that reasonable well costs exceed estimated well costs and shall receive from the operator the amount, if any, that the estimated well costs that it has paid exceeds its share of reasonable well costs.

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

- (a) the proportionate share of reasonable well costs attributable to each non-consenting working interest owner; and
- (b) as a charge for the risk involved in drilling the well, 200 percent of the above costs (see Division Rule 35.A).

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

(14) Reasonable charges for supervision (combined fixed rates) are hereby fixed at \$ 6,473.99 per month while drilling and \$ 949.53 per month while producing, provided that this rate shall be adjusted annually pursuant to Section III.1.A.3 of the COPAS form titled "*Accounting Procedure-Joint Operations*." The operator is hereby authorized to withhold from production the proportionate share of both the supervision charges and the actual expenditures required for operating the well, not in excess of what are reasonable, attributable to each pooled working interest owner.

(15) Except as provided in Ordering Paragraphs (12) and (14) above, all proceeds from production from the well that are not disbursed for any reason shall be placed in escrow in Eddy 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 the escrow agent within 30 days from the date of first deposit with the escrow agent.

(16) 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 this order. Any well costs or charges that are to be paid out of production shall be withheld only from the working interests' share of production, and no costs or charges shall be withheld from production attributable to royalty interests.

(17) Should all the parties to this compulsory pooling order reach voluntary agreement subsequent to entry of this order, that portion of this order authorizing compulsory pooling shall thereafter be of no further effect.

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(18) The operator of the above-described well and unit shall notify the Division in writing of the subsequent voluntary agreement of all parties subject to the forced pooling provisions of this Order.

(19) 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.



STATE OF NEW MEXICO
OIL CONSERVATION DIVISION

A handwritten signature in black ink, appearing to read "Mark E. Fesmire".

MARK E. FESMIRE, P. E.
Director