

**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. 13348
ORDER NO. R-12275**

**APPLICATION OF MARBOB ENERGY CORPORATION 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 November 18, 2004, at Santa Fe, New Mexico, before Examiner David R. Catanach.

NOW, on this 14th day of January, 2005, 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) The applicant, Marbob Energy Corporation ("Marbob" or "applicant") seeks an order pooling all uncommitted mineral interests from the surface to the base of the Morrow formation underlying the S/2 of Section 12, Township 17 South, Range 31 East, NMPM, Eddy County, New Mexico, in the following manner:

the S/2 to form a standard 320-acre spacing and proration unit for any formations and/or pools spaced on 320 acres within this vertical extent which presently include but are not necessarily limited to the Undesignated Fren-Morrow Gas Pool;

the SW/4 to form a standard 160-acre spacing and proration unit for any formations and/or pools spaced on 160 acres within this vertical extent; and

the NE/4 SW/4 to form a standard 40-acre spacing and proration unit for any formations and/or pools spaced on 40 acres within this vertical extent which presently include but are not necessarily limited to the Undesignated Grayburg-Jackson (Seven Rivers-Queen-Grayburg-San Andres) Pool.

(3) The above-described units ("the Units") are to be dedicated to the applicant's Knockabout Federal Well No. 1 which is to be drilled at a standard well location 1830 feet from the South line and 1980 feet from the West line (Unit K) of Section 12.

(4) At the hearing, Marbob requested that its application be amended to pool only that vertical interval from a correlative depth of 4,230 feet (as found on the Compensated Neutron/Lithodensity well log for the BTA 8809 JV-P Puckett Well No. 1 (API No. 30-015-25976) located 1880 feet from the North and East lines (Unit G) of Section 25, Township 17 South, Range 31 East, NMPM, Eddy County, New Mexico) to the base of the Morrow formation.

(5) Mary T. Ard, The W.W.I. 1990 Trust, The S.J.I., Jr. 1990 Trust, The P.I.P. 1990 Trust, Iverson III, Inc., The S.J. Iverson Trust, and the Edward R. Hudson Trust 4, (collectively the "Iverson Group") who own approximately 22.77% of the working interest in the proposed Units, appeared at the hearing and presented evidence in opposition to Marbob's request to designate Hudson Oil Company of Texas as the operator of the proposed Knockabout Federal Well No. 1.

(6) As of the hearing date, the owners of approximately 77% of the working interest in the proposed Units have voluntarily agreed to participate in the drilling of the proposed well. The remaining working interest, owned entirely by the Iverson Group, is not voluntarily committed to the proposed well at this time.

(7) Marbob is an owner of an oil and gas working interest within the Units. Marbob has the right to drill and proposes that Hudson Oil Company of Texas ("Hudson") drill the Knockabout Federal Well No. 1 to test the Morrow formation at a standard well location within the NE/4 SW/4 of Section 12.

(8) Marbob has made a good faith effort to secure the voluntary agreement of the Iverson Group, but has been unable to do so.

(9) Marbob requests that Hudson be named operator of the subject well and of the Units. This request is made for the following reasons:

- (a) the proposed Units are contained within a four-section federal lease that encompasses Sections 12, 13, 24 and 25, Township 17 South, Range 31 East, NMPM. Hudson is the operator of the shallow producing horizons on this federal lease. If Hudson operates the proposed well, all oil production from oil pools in the well will qualify for federal royalty reduction. This royalty reduction will economically benefit all interest owners in the well; and
- (b) the owners of approximately 77% of the working interest in the Units have agreed to allow Hudson to drill and operate the proposed Knockabout Federal Well No. 1.

(10) The Iverson Group opposes the designation of Hudson as the operator of the subject well and of the Units. In support of its position, the Iverson Group presented evidence that demonstrates that:

- (a) most, if not all of the Iverson Group has, in the past, participated as a working interest owner with Hudson on numerous shallow oil wells on this federal lease;
- (b) the Iverson Group has had difficulty dealing with Hudson as operator of these shallow wells. As a result, the Iverson Group filed a lawsuit against Hudson in the Fifth Judicial District Court, Eddy County, New Mexico in 1997. The lawsuit alleged that Hudson failed to operate the wells in a prudent manner and mismanaged the properties. The lawsuit was settled in December, 1997. The settlement agreement stipulated, in part, that Hudson's operatorship was terminated as to rights for all depths below the stratigraphic equivalent of the base of the San Andres formation (shown as a depth of 4,230 feet in the BTA 8809 JV-P Puckett

Well No. 1, as further described in Finding No. 4 above);

- (c) Hudson owns no interest in the subject well or Units; and
- (d) Hudson has very limited experience drilling and operating deep wells in this area.

(11) The Iverson Group does not object to Marbob drilling and operating the proposed Knockabout Federal Well No. 1.

(12) The Iverson Group also requested that any pooling order issued by the Division contain certain provisions not currently contained within a standard compulsory pooling order. These provisions, summarized briefly as follows, would grant additional rights to pooled working interest owners:

- (a) each pooled working interest owner shall have access at all reasonable times to the area pooled, and shall have access at reasonable times to information pertaining to the development or operation thereof;
- (b) at casing point in the Morrow formation, each pooled working interest owner shall have the opportunity to elect to either participate or not participate in the completion of the well. If such owner elects not to participate, the operator shall reimburse to that party its share of advance well completion costs. Such non-consent owners shall be subject to a 200% risk charge for such completion costs; and
- (c) the "Accounting Procedure Joint Operations" submitted as Applicant's Exhibit No. 5, shall be incorporated in its entirety.

(13) Division records demonstrate that both shallow and deep oil production has been encountered in Township 17 South, Range 31 East, NMPM. Although Marbob testified that it does not anticipate encountering shallow oil production in the Knockabout Federal Well No. 1, there exists a possibility that oil production from the Paddock, Yeso, Abo, Wolfcamp, Cisco/Canyon and/or Atoka formations may be encountered in the wellbore.

(14) Marbob's proposal to allow Hudson to drill and operate the Knockabout Federal Well No. 1 will economically benefit the working interest owners in the well in the event oil production is encountered.

(15) The evidence presented demonstrates only that there have been previous disagreements over operations in this area between the Iverson Group and Hudson. There is no evidence to demonstrate that Hudson has operated its wells in this area in an imprudent manner or otherwise mismanaged its properties.

(16) There is also no evidence to demonstrate that Hudson is not capable of drilling and operating the proposed Knockabout Federal Well No. 1 in a responsible and prudent manner.

(17) Marbob's request to allow Hudson to drill and operate the Knockabout Federal Well No. 1 is reasonable, justified, and should therefore be approved.

(18) There is not sufficient justification to amend the Division's standard compulsory pooling order by incorporating the Iverson Group's proposed additional pooling provisions.

(19) To avoid the drilling of unnecessary wells, protect correlative rights, prevent waste and afford to the owner of each interest in the Units the opportunity to recover or receive without unnecessary expense its just and fair share of hydrocarbons, this application should be approved by pooling all uncommitted interests, whatever they may be, in the oil and gas within the Units.

(20) Hudson Oil Company of Texas should be designated the operator of the subject well and of the Units.

(21) 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% thereof as a reasonable charge for the risk involved in drilling the well.

(22) Reasonable charges for supervision (combined fixed rates) should be fixed at \$5,500.00 per month while drilling and \$550.00 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."

IT IS THEREFORE ORDERED THAT:

(1) Pursuant to the application of Marbob Energy Corporation, all uncommitted mineral interests from a correlative depth of 4,230 feet (as found on the Compensated Neutron/Lithodensity well log for the BTA 8809 JV-P Puckett Well No. 1 (API No. 30-015-25976) located 1880 feet from the North and East lines (Unit G) of Section 25, Township 17 South, Range 31 East, NMPM, Eddy County, New Mexico) to the base of the the Morrow formation underlying the S/2 of Section 12, Township 17 South, Range 31 East, NMPM, Eddy County, New Mexico, are hereby pooled in the following manner:

the S/2 to form a standard 320-acre spacing and proration unit for any formations and/or pools spaced on 320 acres within this vertical extent which presently include but are not necessarily limited to the Undesignated Fren-Morrow Gas Pool;

the SW/4 to form a standard 160-acre spacing and proration unit for any formations and/or pools spaced on 160 acres within this vertical extent; and

the NE/4 SW/4 to form a standard 40-acre spacing and proration unit for any formations and/or pools spaced on 40 acres within this vertical extent which presently include but are not necessarily limited to the Undesignated Grayburg-Jackson (Seven Rivers-Queen-Grayburg-San Andres) Pool.

The above-described Units are to be dedicated to the applicant's Knockabout Federal Well No. 1 which is to be drilled at a standard well location 1830 feet from the South line and 1980 feet from the West line (Unit K) of Section 12.

(2) The operator of the Units shall commence drilling the proposed well on or before April 15, 2005 and shall thereafter continue drilling the well with due diligence to test the Morrow formation.

(3) In the event the operator does not commence drilling the proposed well on or before April 15, 2005, Ordering Paragraph (1) shall be of no effect, unless the operator obtains a time extension from the Division Director for good cause.

(4) Should the subject well not be drilled and completed within 120 days after commencement thereof, Ordering Paragraph (1) shall be of no further effect, and the Units created by this Order shall terminate unless the operator appears before the Division Director and obtains an extension of time to complete the well for good cause demonstrated by satisfactory evidence.

(5) Upon final plugging and abandonment of the subject well, the pooled Units created by this Order shall terminate, unless this order has been amended to authorize further operations.

(6) Hudson Oil Company of Texas is hereby designated the operator of the subject well and of the Units.

(7) 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 Units, including unleased mineral interests, who are not parties to an operating agreement governing the Units.) After the effective date of this order, the operator shall furnish the Division and each known pooled working interest owner in the Units an itemized schedule of estimated costs of drilling, completing and equipping the subject well ("well costs").

(8) 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."

(9) The operator shall furnish the Division and each known pooled working interest owner (including non-consenting working interest owners) 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.

(10) Within 60 days following determination of reasonable well costs, any pooled working interest owner who has paid its share of estimated 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 it has paid exceed its share of reasonable well costs.

(11) 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% of the above costs.

(12) The operator shall distribute the costs and charges withheld from production, proportionately, to the parties who advanced the well costs.

(13) Reasonable charges for supervision (combined fixed rates) are hereby fixed at \$5,500.00 per month while drilling and \$550.00 per month while producing, provided that these rates shall be adjusted annually pursuant to Section III.1.A.3. of the COPAS form titled "Accounting Procedure-Joint Operations." The operator is 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 pooled working interest owners.

(14) Except as provided in Ordering Paragraphs (11) and (13) 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.

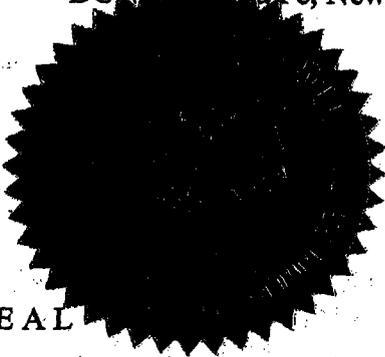
(15) Any unleased mineral interest shall be considered a seven-eighths (7/8) working interest and a one-eighth (1/8) royalty interest for the purpose of allocating costs and charges under this order. Any well costs or charges that are to be paid out of production shall be withheld only from the working interests' share of production, and no costs or charges shall be withheld from production attributable to royalty interests.

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

(17) The operator of the well and Units shall notify the Division in writing of the subsequent voluntary agreement of all parties subject to the forced pooling provisions of this order.

(18) 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.



SEAL

STATE OF NEW MEXICO
OIL CONSERVATION DIVISION

Handwritten signature of Mark E. Fesmire

MARK E. FESMIRE, PE
Director



December 20, 2004

BY HAND DELIVERY

Mr. David Catanach, Hearing Examiner
Oil Conservation Division
New Mexico Department of Energy,
Minerals and Natural Resources
1220 South Saint Francis Drive
Santa Fe, New Mexico 87505

2004 DEC 20 PM 4 22
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Re: Case No. 13348: Application of Marbob Energy Corporation for compulsory pooling, Eddy County, New Mexico.

Dear Mr. Catanach:

I have just reviewed the December 15, 2004 letter in the above referenced case from James Bruce, attorney for Mary T. Ard, W.W.I. 1990 Trust, S.J.I. 1990 Trust, the P.I.P. 1990 Trust, Iverson III, Inc., S. J. Iverson Trust, and Edward R. Hudson Trust 4. Certain statements in this letter require a response.

In Section A of the letter, Ard et al. cite the proposed Joint Operating Agreement for the subject well. When this Joint Operating agreement was proposed, Ard refused to sign it. Marbob submits that Ard does not now have standing to complain to the Division about a draft agreement that they have refused to execute.

In Section B of the letter, Ard's argument centers on a 1997 Eddy County District Court suit between certain parties in this pooling case. See, Ard et al. Exhibit 1. This suit was settled with no admission of wrong doing on the part of any of the named defendants in the suit. Consequently there is nothing before the Division on which a prudent operator determination can be made.

In Section C of Ard's letter, they express concern about Hudson's lack of experience in completing deep Morrow wells. While they expresses this concern, everyone except Ard has agreed that Hudson Oil Company of Texas is the proper operator for this well - including, at one time, even the Iversons.

To correct any confusion that I or my witnesses may have created in Ard's mind concerning the proposed operator for the Knockabout Federal Well No. 1 (See Section E of Mr. Bruce's letter), I would suggest they look at the application filed in this case and the proposed Joint Operating Agreement that the Iverson's at one time had agreed to sign. Both of these documents correctly designate Hudson Oil Company of Texas as the proposed operator of this well. If this application is approved, Hudson Oil Company of Texas will operate the well as the owners of over 77% of the working interest in this property desire. My November 30, 2004



quantified the benefits that will accrue from the operation of this well by Hudson Oil Company of Texas.

The special provisions that Ard seeks to have included in the order, go beyond the practice of the Division and, in most cases, amend the underlying agreement between the parties in a way that exceeds the power conferred on the Division by the Oil and Gas Act.

In this case, everyone, even the Ard et al. group, wants the well to be drilled. The only proposal before the Examiner is the Marbob application to pool the S/2 of Section 12, for the Knockabout Federal Well No. 1. Here, all statutory preconditions for a pooling order have been met. When this occurs, the Oil and Gas Act provides that "... the division, to avoid the drilling of unnecessary wells or to protect correlative rights, or to prevent waste, **shall pool** all or part of such lands or interests or both in the spacing or proration unit as a unit." NMSA 1978, §70-2-17.C. Marbob submits that, on the record in this case, it is entitled to an order pooling the subject lands and designating Hudson Oil Company of Texas operator of the well.

Your attention to this matter is appreciated.

Very truly yours,

William F. Carr

cc: Mr. E. Randall Hudson, III
Hudson Oil Company of Texas

James G. Bruce, Esq.