

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.: 14662

APPLICATION OF OGX RESOURCES
LLC FOR APPROVAL OF A NON-STANDARD
OIL SPACING AND PRORATION UNIT AND
COMPULSORY POOLING, EDDY COUNTY,
NEW MEXICO.

ORIGINAL

REPORTER'S TRANSCRIPT OF PROCEEDINGS
EXAMINER'S HEARING

BEFORE: DAVID K. BROOKS, Legal Examiner
TERRY WARNELL, Technical Examiner

DATE: June 9, 2011
Santa Fe, New Mexico

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This matter came on for hearing before the New Mexico Oil Conservation Division, DAVID K. BROOKS, Legal Examiner, and TERRY WARNELL, Technical Examiner, on Thursday, June 9, 2011, at the New Mexico Energy, Minerals and Natural Resources Department, 1220 South St. Francis Drive, Room 102, Santa Fe, New Mexico.

REPORTED BY: Irene Delgado
Paul Baca Professional Court Reporters
500 Fourth Street, NW, Suite 105
Albuquerque, NM 87103

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A P P E A R A N C E S

FOR THE APPLICANT:

JIM BRUCE ESQ.
P.O. Box 1506
Santa Fe, NM 87504-1506

FOR CHESAPEAKE:

HOLLAND & HART, LLP
MICHAEL FELDEWERT, ESQ.
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I N D E X

GARLAND LANG III

Direct by Mr. Bruce 04

Cross by Mr. Feldewert 10

WILLIAM HARDIE

(Testimony and exhibits incorporated from Case 14661)

Direct by Mr. Bruce 12

EXHIBITS 1 -7 ADMITTED 09

EXHIBITS A - E-2 ADMITTED 20

1 EXAMINER BROOKS: And at this point we will
2 call Case Number 14662, Application of OGX Resources
3 LLC for approval of non-standard oil spacing unit and
4 compulsory pooling, Eddy County, New Mexico. Call for
5 appearances.

6 MR. BRUCE: Mr. Examiner, Jim Bruce
7 representing the applicant. I have two witnesses who
8 were previously sworn involved.

9 EXAMINER BROOKS: Very good.

10 MR. FELDEWERT: Mr. Examiner, Michael
11 Feldewert on behalf of Chesapeake Operating LLC.

12 EXAMINER BROOKS: Very good. The witnesses
13 having already been sworn, it won't be necessary to do
14 that again. I suppose, reflecting the way things are
15 done in court, I should admonish the witnesses that
16 they are still under oath in case they have any
17 temptation to lie. You may proceed, Mr. Bruce.

18 MR. BRUCE: I'm calling Mr. Lang back to the
19 stand. If the record could reflect that he was
20 qualified as an expert landman.

21 EXAMINER BROOKS: The record so reflects.

22

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1 GARLAND H. LANG III

2 (Having been previously sworn, testified as follows:)

3 DIRECT EXAMINATION

4 BY MR. BRUCE:

5 Q. Mr. Lang, would you identify Exhibit 1 and
6 describe what Exhibit 1 is?

7 A. Exhibit 1 is the land plat showing our proposed
8 proration unit drilling unit for the Sidewinder Number
9 1H, in Section 32 of 26, 29.

10 Q. And what is the second page of the exhibit?

11 A. The second page of the exhibit is the proposed
12 proration unit. There is a mistake on the dedicated
13 acreage. It says 138 acres, but it's actually 126
14 acres which it comprises Lots 1, 2, 3 and 4 in the
15 south 34 acres of the North Half North Half of Section
16 32 of 26 South 29 East.

17 EXAMINER BROOKS: That was 120?

18 WITNESS: Six acres.

19 EXAMINER BROOKS: 126 acres.

20 Q. And, Mr. Lang, why did you seek to include the
21 south 34 acres of the North Half North Half of Section
22 32 in this area?

23 A. Basically Section 32 is 256 acres or --

24 Q. 252.

25 A. Yeah. So it's basically half -- basically one

1 half is going to be the proration unit for the Number 1
2 and the Number 2 Well we plan on drilling in the future
3 will embrace the remaining half of the section.

4 Q. So each project area will be equal in size?

5 A. Correct.

6 Q. For the Numbers 1 and 2 Wells?

7 A. That's right.

8 Q. And that is in the North Half North Half, that is
9 OGX acreage --

10 A. Correct.

11 Q. -- as far as acreage owned jointly by the parties
12 in this well. And again, are you just seeking to force
13 pool the Bone Spring Formation?

14 A. We are.

15 Q. And who do you seek to pool -- identify Exhibit 2
16 for the Examiner and describe who you seek to pool.

17 A. Exhibit 2 shows the working interest owners,
18 proposed working interest owners. Everybody else has
19 executed the joint operating agreement except for
20 Chesapeake. They are -- that's why we are here to
21 force pool them. They've got a point 10180415 percent
22 working interest in the proposed unit.

23 Q. Would you identify Exhibit 3-A for the Examiner
24 and describe that?

25 A. Exhibit 3-A is a lease or copy of a certified

1 letter, dated March 23, 2011, sent to Chesapeake
2 Exploration LLC, proposing the well that had -- we
3 included a copy of the AFE and the C-102 plat.

4 Q. And did you follow that up with a letter dated
5 May 5? The last one.

6 A. With the operating agreement?

7 Q. Yes.

8 A. Yes. May 5, we included a copy of the proposed
9 operating agreement.

10 Q. And, again, did you have any telephone or e-mail
11 discussions with Chesapeake regarding this?

12 A. I have -- I have had several just like before
13 asking what they are going to do about this well
14 proposal and other well proposals.

15 Q. And, again, until a couple of days ago, you
16 received no affirmative response from Chesapeake?

17 A. That's true.

18 Q. Did the phone conversation a couple of days ago
19 from one of the principals in your company include this
20 acreage, also?

21 A. It did.

22 Q. Okay. And, again, they mentioned the term
23 "assignment," but you have not seen any written term
24 assignment?

25 A. No.

1 Q. In your opinion, has OGX made a good-faith effort
2 to obtain the voluntary joinder of Chesapeake in this
3 well?

4 A. We have.

5 Q. Exhibit 3-B is a letter to Ms. Audrey Emmet. Why
6 do you seek to pool her interest? You don't list her
7 in your Exhibit 2 as a working interest owner.

8 A. She is owner of 1/64 owner of non-participating
9 royalty interest.

10 Q. And you need to obtain --

11 A. Obtain her -- but she did sign this.

12 Q. Oh.

13 A. Last week.

14 Q. She did sign it?

15 A. Yeah. So I think -- I think she is okay.

16 Q. So we --

17 A. We haven't recorded it, but we have it. She has
18 ratified.

19 Q. So we don't need to pool her non-participating
20 interest at this time?

21 A. No.

22 Q. Okay. And what is Exhibit 4?

23 A. Exhibit 4 is a copy of the authorization for
24 expenditure for the Sidewinder Number 1H, dated March
25 22, 2011. We've got a dry hole cost of 1,527,330 and a

1 completion cost of 4,107,460 for a total cost of
2 5,634,790.

3 Q. And is that cost in line with the cost of other
4 wells drilled to this depth in this area of Eddy
5 County?

6 A. It is.

7 Q. And do you request that OGX be appointed operator
8 of the well?

9 A. We do.

10 Q. Do you have a recommendation for the amounts
11 which OGX should be paid for its supervision and
12 administrative expenses?

13 A. 6,000 a month drilling overhead and 600 a month
14 operating overhead.

15 Q. And are these amounts equivalent to those
16 normally charged by OGX and other operators in this
17 area for wells of this depth?

18 A. It is.

19 Q. And do you request that the rates be adjusted
20 under the Copas Accounting Procedure?

21 A. We do.

22 Q. Does OGX request the maximum cost plus 200
23 percent risk charge?

24 A. We do.

25 Q. And was Chesapeake notified of this hearing?

1 A. They were.

2 Q. And is that reflected in Exhibit 5?

3 A. It is.

4 Q. What does Exhibit -- Exhibit 6 reflect?

5 A. Exhibit 6 reflects the offsetting operators to
6 the Sidewinder Number 1H.

7 Q. Okay. Chesapeake was notified as previously
8 indicated. Was GP II notified of this application?

9 A. Yes, they were.

10 Q. Is that reflected in Exhibit 7?

11 A. It is.

12 Q. Were Exhibits 1 through 7 prepared by you or
13 under your supervision or compiled with the company
14 business records?

15 A. They were.

16 Q. And, in your opinion, is the granting of this
17 application in the interest of conservation and
18 prevention of waste?

19 A. It is.

20 MR. BRUCE: Mr. Examiner, I would move the
21 admission of Exhibits 1 through 7.

22 EXAMINER BROOKS: Mr. Feldewert?

23 MR. FELDEWERT: I have no objection.

24 EXAMINER BROOKS: 1 through 7 admitted.

25 (Exhibits 1 through 7 admitted.)

1 MR. BRUCE: Pass the witness

2 EXAMINER BROOKS: Mr. Feldewert?

3 CROSS-EXAMINATION

4 BY MR. FELDEWERT:

5 Q. Mr. Lang, previously today you provided testimony
6 in Case 14661 about your efforts to reach a voluntary
7 agreement with Chesapeake. Do you recall that?

8 A. Uh-huh.

9 Q. Okay. Is your testimony, if I ask you the same
10 questions, would your testimony be the same that you
11 provided in Case 14661?

12 A. Yes.

13 Q. Okay. That would include both your good-faith
14 efforts to reach an agreement and the status of your
15 leases in the area?

16 A. Well, as pertaining to this well, we -- we have a
17 lease that Allar Company that comprises almost half the
18 unit that expires on June 20, and as I -- that's why we
19 are going to this hearing, but also we're going to file
20 a pooling designation that we sent to Chesapeake which
21 they haven't sent back, we are going to go ahead and
22 file ours just with our leases on it to pool that
23 acreage together because we own leases in both the same
24 acreage that Chesapeake owns in, and we also own the
25 Allar lease 100 percent, OGX does. So we are going to

1 file that pooling designation this week, and we are
2 going to have a drilling rig on location next week
3 drilling wells.

4 So we are going to go ahead and drill the
5 well with or without Chesapeake, but -- and Chesapeake,
6 we -- you talk about -- we are saving Chesapeake's
7 leases also because they have an August expiration date
8 and no response, nothing. We are saving Chesapeake's
9 lease.

10 Q. So your drilling the well is going to hold your
11 lease?

12 A. Hold my lease and Chesapeake's lease.

13 MR. FELDEWERT: Mr. Examiner, I don't have
14 any further questions.

15 EXAMINER WARNELL: No.

16 EXAMINER BROOKS: I don't have any -- I
17 didn't hear the -- was this 6,000 and 600 the overhead,
18 also?

19 WITNESS: Yes, sir.

20 EXAMINER BROOKS: You had no questions?

21 EXAMINER WARNELL: No questions.

22 EXAMINER BROOKS: Very good. Mr. Bruce,
23 anything further?

24 MR. BRUCE: Nothing further.

25 EXAMINER BROOKS: The witness may stand down.

1 MR. BRUCE: I have nothing further. Again, I
2 just incorporate Mr. Hardie's testimony into the record
3 and --

4 EXAMINER BROOKS: Okay. The court reporter
5 understood that instruction, I believe.

6 (The testimony of William Hardie as recorded
7 in Case Number 14661 is incorporated as follows per
8 order of Examiner Brooks.)

9 WILLIAM HARDIE

10 (Having been sworn, testified as follows:)

11 DIRECT EXAMINATION

12 BY MR. BRUCE:

13 Q. Would you please state your full name and city of
14 residence for the record?

15 A. William Hardie, and I live in Midland, Texas.

16 Q. Who do you work for and in what capacity?

17 A. I'm exploration manager for OGX Resources.

18 Q. Have you previously testified before the
19 Division?

20 A. I have.

21 Q. And were your credentials as an expert geologist
22 accepted as a matter of record?

23 A. They were.

24 Q. And are you familiar with the geology involved in
25 this application?

1 A. I am.

2 Q. And, for that matter, is the geology similar for
3 the next application?

4 A. It is very similar. The locations are just a
5 mile or so apart.

6 MR. BRUCE: Mr. Examiner, what I propose is
7 just to have Mr. Hardie testify at this point as to
8 both wells, and so that he doesn't have to come up and
9 regurgitate the testimony for the next application.

10 EXAMINER BROOKS: Okay. I think that would
11 be acceptable. Is there any objection, Mr. Feldewert?

12 MR. FELDEWERT: No objection.

13 EXAMINER BROOKS: Very good. Proceed.

14 Q. Mr. Hardie, I have lettered your exhibits. What
15 is Exhibit A?

16 A. Exhibit A is a regional structure map on the face
17 of the Avalon Shale. If I could, I would like to kind
18 of give the Examiner a little bit more of a regional
19 perspective on the play itself. I think it helps to
20 understand the larger play when you are looking at
21 individual locations as well.

22 So this is a -- this is a structure map on
23 the base of the Avalon Shale across -- the map's
24 dimensions are 70 miles wide and about 50 miles in
25 height. So it's a -- it's a pretty regional look at

1 the play itself. Structural contours have a 20-foot
2 contour interval, and they have been color coded by
3 elevation such that on the western side of the map is
4 the highest part of the Avalon. The base of the Avalon
5 Shale is at a depth of about 65 hundred feet. And then
6 as you move to the east from Eddy County into Lea
7 County, you approach the -- the basin axis, and it's
8 -- it's as deep as 95 hundred feet in the basin axis
9 in Lea County.

10 So there is a pretty significant structural
11 change that occurs across Southeast New Mexico. The
12 real significance of that is that the -- this change in
13 structure also coincides with a pretty dramatic change
14 in the GOR of the Avalon Shale as it's produced across
15 the Southern part of New Mexico.

16 In the Western reaches the Avalon Shale is
17 virtually all gas. There are no liquids associated
18 with it. If you look towards the middle of the map
19 like around the Poker Lake Unit, the GOR there is about
20 10,000 to 1. You start seeing some condensate being
21 produced.

22 By the time you get into Lea County in the
23 deeper parts of the basin, the GOR is closer to 3,000
24 to 1, so there is a significant change in the
25 production characteristics, and it's all associated

1 with structure.

2 Q. Okay. What is Exhibit B?

3 A. We are looking at the same regional map, only
4 this time we are looking at a Net Shale Isopach on the
5 Avalon Interval, and it's a -- it's a map that was
6 constructed with a gamma ray cutoff of 100 API units.
7 The color corresponding -- the color-filled contours
8 are coded such that the darker browns indicate thicker
9 Net Shale sequences, and the lighter colors indicate
10 thinner. In Eddy County your average thickness is 4-
11 to 500 feet and that's probably as thick as it gets
12 anywhere in Southeast New Mexico. In Lea County the
13 average thickness is probably less than 200 feet, and
14 both counties are equally productive.

15 The thick sequence that we see in Eddy
16 County, it's virtually impossible to drain all of that
17 with a single wellbore so that there really isn't much
18 difference in economics of Eddy or Lea based on this
19 map; it just kind of defines where the play actually
20 exists.

21 The other thing I have shown on this map, if
22 you look at the green sticks on there, those are wells
23 that have been drilled horizontally in the Avalon
24 Shale. And, as you can see, there are quite a few of
25 them. If you sit there and count them, there would be

1 about 180 of them that have actually been drilled
2 today, so this is a pretty active play. And as you can
3 see, it does extend into Texas, although Southeast New
4 Mexico has by far seen more drilling than Texas.

5 Q. Let's move on to a more localized area. What is
6 reflected in Exhibit C?

7 A. I think it would be probably useful to look at C
8 and D at the same time. I would like to start with the
9 cross-section. I believe that's Exhibit D. Exhibit D
10 shows -- shows about 2,000 feet of vertical section,
11 and the Avalon Shale is highlighted in the middle of
12 that. It's -- it's stratigraphically hung on the top
13 of the Bone Spring Formation, so it's not a structural
14 cross-section; it's stratigraphic.

15 The yellow at the top is the Basal Brushy
16 Canyon, and the yellow that you see at the bottom is
17 the First Bone Spring Sand. Everything in between is
18 what we consider the Avalon Shale, so it's everything
19 between the top of the Bone Spring Formation and top of
20 the First Bone Spring Sand.

21 I have color coded the gamma ray in the
22 Avalon such that if it's got a shale characteristic as
23 being high gamma ray, it's painted brown, and if it's a
24 cleaner gamma ray, then it paints a blue picture, and
25 that represents the basic lithology of the Avalon.

1 The shales aren't true shales. They are
2 actually organic rich siltstone. The Avalon has a
3 quartz content of almost 80 percent. There is very
4 little clay content in it, actually, even though we
5 call it a shale. It looks like a shale, but it's an
6 organic, rich siltstone, and it's interbedded with
7 detrital carbonates, and that's the difference in the
8 net map that we just looked at. The brown represents
9 the compilation of the net thickness that you have seen
10 on the previous map.

11 The Exhibit C, is just kind of a zoomed-in
12 version of the two previous maps you looked at. On the
13 left is the Net Shale, and you can see highlighted on
14 there are the two locations that we are seeking to
15 pool. They exist in -- in Township 26 South, 29 East,
16 right on the Texas state line. And they have been --
17 they have been labeled the Copperhead Fee A Number 1H
18 and the Sidewinder Number 1H.

19 We expect about 500 feet of Net Shale in the
20 area of the Copperhead and about 400 feet of Net Shale
21 in the Sidewinder area. The map on the right is,
22 again, a structure map on the base of the Avalon Shale.
23 There is nothing particularly significant here, we are
24 just looking at regional dip at about 100 feet per
25 mile. No significant structures. This is not a

1 structural play.

2 And then also on both maps I have shown where
3 the cross-section of Exhibit B is shown, and it passes
4 just to the north of the these proposed locations.

5 Q. Mr. Hardie, will each quarter quarter section or
6 lot in each well unit contribute to production, in your
7 opinion?

8 A. They will all contribute to production and they
9 will contribute equally.

10 Q. Finally, Mr. Hardie, I have marked as Exhibits
11 E-1 and E-2 the -- the APDs for the Sidewinder Number
12 1, and E-2 is the APD for the Copperhead Fee Number 1,
13 and contained in there is the drilling prognosis for
14 each well. For the Examiners, could you describe how
15 OGX is currently drilling and completing these wells?

16 A. Those wells are fairly similar in the way they
17 will be drilled and completed. The one exception is
18 that the Copperhead Fee is going to be a longer lateral
19 because of the short sections we have right near the
20 state line, and its -- its lateral length is going to
21 be about 1,000 feet longer than the Sidewinder.

22 But we drill these -- we drill them vertically
23 to a depth of about 400 feet above where we intend to
24 go horizontal. We will run open hole logs at that
25 point and recalibrate exactly where we predict our

1 horizontal target to be, and we will develop the
2 horizontal plan at that time. And then the directional
3 company will guide us in cutting our curve, about a 400
4 foot radius curve, and that -- that puts the wellbore
5 in the proposed target zone, and then we drill
6 horizontally until we reach the target, which is
7 usually 330 feet or so before the end of the section in
8 the case of the Sidewinder, and about 1650 feet before
9 the end of the section in the case of the Copperhead
10 Fee.

11 Typically we -- we complete these wells
12 nowadays with a sliding sleeve system, and OGX has been
13 more recently actually cementing the sliding sleeve
14 casing in -- in the hole. They can also -- sliding
15 sleeves can also be used with swelling packers and
16 mechanical packers to isolate intervals, and we have
17 found that it's difficult to get that packer system in
18 the hole, and so we eliminated that and we just cement
19 the liner in place.

20 And then we typically employ a 20-stage frac
21 job that -- that has given us the best results to date.
22 It usually involves between 2 and 3 million pounds of
23 sand, and those 20 stages each receive about a -- I
24 think, about 150,000 pounds of sand, something like
25 that. That's the goal. If all the stages were to go

1 well, we would probably pump over 3 million pounds of
2 sand. Some of them don't go as well as others.

3 The stages are isolated one from the other by
4 a system of -- of balls that are -- one is the -- you
5 start out with the bigger balls and end up with smaller
6 ones at the end of the frac job, and the whole process
7 almost never stops, usually the best way to get a well
8 like that fracked with that many stages in the shortest
9 period of time.

10 Q. Mr. Hardie, were Exhibits A, B, C, and D prepared
11 by you?

12 A. They were.

13 Q. And were Exhibits E-1 and E-2 compiled from
14 company business records?

15 A. They were.

16 Q. In your opinion, is the granting of both
17 applications in the interest of conservation and
18 prevention of waste?

19 A. They are.

20 MR. BRUCE: Mr. Examiner, I would move the
21 admission of Exhibits A through E-2.

22 MR. FELDEWERT: No objection.

23 EXAMINER BROOKS: A through E-2 are admitted.

24 (Exhibits A through E-2 admitted.)

25 MR. BRUCE: I pass the witness.

1 MR. FELDEWERT: I have no questions.

2 EXAMINER BROOKS: Okay. Just one. When you
3 were describing your drilling procedure, you said you
4 drilled vertically through 4- or 500 feet above where
5 you intended to go horizontal. I just was unsure if
6 you meant -- because I know the way some other
7 operators do things -- if you meant above or below.

8 WITNESS: Above.

9 EXAMINER BROOKS: Okay.

10 WITNESS: If we had wanted to cut a pilot
11 hole and look at the section vertically, we would have
12 probably drilled below it, but we don't typically do
13 that anymore.

14 EXAMINER BROOKS: Okay. Mr. Warnell?

15 EXAMINER WARNELL: No questions.

16 (The incorporated testimony of Mr. Hardie as
17 previously recorded in Case 14661 is concluded.)

18 EXAMINER BROOKS: Do the parties want to
19 discuss what we need to do in this case? Or do you --
20 are you going to request a continuance in this case,
21 also?

22 MR. FELDEWERT: For the same reasons,
23 Mr. Examiner, since there is an effort -- since there
24 is a possibility we might be able to reach an
25 agreement, in order to engage in good-faith efforts, we

1 ask this case be continued for two weeks like the
2 previous case and we can report back.

3 MR. BRUCE: Mr. Examiner, I don't mind
4 reporting back, but because of the time deadlines, I
5 would object to a continuance in this matter. They
6 first contacted Chesapeake with a letter dated March
7 23, and until two days ago have never gotten a response
8 out of Chesapeake regarding this well, and I -- the
9 well we'll be drilling regardless before the pooling
10 order issues, no doubt, but nonetheless -- and we don't
11 mind reporting back on further discussions, and -- but
12 if I could just -- OGX will continue to negotiate
13 regardless of whether this hearing is continued or not,
14 but I would object to a continuance because we do need
15 to get this pooling order out as soon as possible.

16 EXAMINER BROOKS: Okay. I think that that
17 point is well taken, and it seems that, while the
18 negotiations are relatively broad in scope, they
19 basically involve this other well that, of course, I
20 don't know what the time constraints are on that other
21 well, but Chesapeake obviously has the right --
22 Division orders are not res judicata, and Chesapeake
23 has the right to make a motion to reopen a prior case
24 if they feel that that is necessary.

25 At this time we will take Case Number 14662

1 under advisement.

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I do hereby certify that the foregoing is
 a complete record of the proceedings in
 the Examiner hearing of Case No. 14662
 heard by me on June ~~6~~ 9 2011
 David K. Brody, Examiner
 Oil Conservation Division

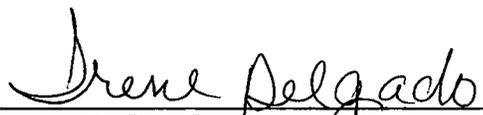
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REPORTER'S CERTIFICATE

I, IRENE DELGADO, New Mexico CCR 253, DO
HEREBY CERTIFY that on June 9, 2011, proceedings in the
above-captioned case were taken before me and that I
did report in stenographic shorthand the proceedings
set forth herein, and the foregoing pages are a true
and correct transcription to the best of my ability.

I FURTHER CERTIFY that I am neither employed
by nor related to nor contracted with any of the
parties or attorneys in this case and that I have no
interest whatsoever in the final disposition of this
case in any court.

WITNESS MY HAND this _____ day of _____
_____.


Irene Delgado CCR 253
Expires: 12-31-11