

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. 13,757

APPLICATION OF LCX ENERGY, LLC, FOR)
COMPULSORY POOLING, EDDY COUNTY,)
NEW MEXICO)

ORIGINAL

REPORTER'S TRANSCRIPT OF PROCEEDINGS

EXAMINER HEARING

BEFORE: DAVID R. CATANACH, Hearing Examiner

August 17th, 2006

Santa Fe, New Mexico

2006 AUG 31 AM 10 26

This matter came on for hearing before the New Mexico Oil Conservation Division, DAVID R. CATANACH, Hearing Examiner, on Thursday, August 17th, 2006, at the New Mexico Energy, Minerals and Natural Resources Department, 1220 South Saint Francis Drive, Room 102, Santa Fe, New Mexico, Steven T. Brenner, Certified Court Reporter No. 7 for the State of New Mexico.

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August 17th, 2006
 Examiner Hearing
 CASE NO. 13,757

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APPLICANT'S WITNESS:	
<u>LARRY GILLETTE</u> (Engineer)	
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A P P E A R A N C E S

FOR THE DIVISION:

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By: OCEAN MUNDS-DRY

* * *

1 WHEREUPON, the following proceedings were had at
2 8:29 a.m.:

3 EXAMINER CATANACH: All right, at this time we'll
4 call Case 13,757, the Application of LCX Energy, LLC, for
5 compulsory pooling, Eddy County, New Mexico.

6 Call for appearances in this case.

7 MR. HALL: Mr. Examiner, Scott Hall, Miller
8 Stratvert, PA, Santa Fe, on behalf of the Applicant, LCX
9 Energy, LLC, and I have one witness this morning.

10 EXAMINER CATANACH: Any additional appearances in
11 this case?

12 MS. MUNDS-DRY: Ocean Munds-Dry for Yates
13 Petroleum Corporation, Mr. Hearing Examiner. We have no
14 witnesses, and I believe -- we understand that Yates signed
15 the AFE late last night, so we think that they have reached
16 agreement, but we're just entering our appearance, just in
17 case.

18 EXAMINER CATANACH: Okay, will the witness please
19 stand to be sworn in?

20 LARRY GILLETTE,
21 the witness herein, after having been first duly sworn upon
22 his oath, was examined and testified as follows:

23 DIRECT EXAMINATION

24 BY MR. HALL:

25 Q. For the record, please state your name.

1 A. Larry Gillette.

2 Q. Mr. Gillette, where do you live and by whom are
3 you employed?

4 A. I live in Midland, Texas, and I'm employed by LCX
5 Energy, LLC.

6 Q. And what do you do for LCX?

7 A. I'm a petroleum engineer.

8 Q. And you've previously testified before the
9 Division and had your credentials as an expert petroleum
10 engineer accepted as a matter of record; is that right?

11 A. Yes.

12 Q. And you're familiar with the Application that's
13 been filed in this case and the lands that are the subject
14 of the Application?

15 A. Yes.

16 MR. HALL: Mr. Examiner, we'd offer Mr. Gillette
17 as a qualified expert petroleum engineer.

18 EXAMINER CATANACH: Mr. Gillette is so qualified.

19 Q. (By Mr. Hall) Briefly, Mr. Gillette, explain to
20 the Examiner what it is LCX seeks in this Application.

21 A. We want to pool this acreage to cover all
22 formations that can be spaced at 320 acres, and
23 specifically we're looking at the Wolfcamp zone, and we
24 want to form a south-half 320-acre unit with LCX Energy as
25 the operator.

1 Q. Okay. Let's turn to what's been marked as
2 Exhibit 1. Would you identify that, please?

3 A. I believe it's the plat.

4 Q. And does it reflect the unit configuration for
5 the well and the surface and bottomhole location?

6 A. Yes.

7 Q. And what are those?

8 A. Surface location is 660 from the west line, 960
9 from the south line, and the bottomhole location is 660
10 from the west line, 960 from the south line --

11 Q. All right.

12 A. -- of Section 21.

13 Q. Now, has this well been drilled?

14 A. The well has been drilled and completed and is --
15 the gas pipeline is in place, we're waiting to put it down
16 the line.

17 Q. All right, it's not been placed on production as
18 of today?

19 A. Not yet.

20 Q. And is LCX seeking immediate authority to place
21 the well on production, even interim authority, before the
22 issuance of a compulsory pooling order in this case?

23 A. Yes, we are.

24 Q. And what is the reason for that?

25 A. Well, there's been evidence out there that a well

1 that's shut in for a time after it's frac'd and not cleaned
2 up totally, can damage the wells, lower the production. So
3 we want to try to get the well on as fast as possible.

4 Q. With these horizontal drills, do these involve
5 four-stage fracs along the length of the wellbore?

6 A. Right, there's -- We go in there with brine water
7 nowadays and do four separate stages, and -- with some CO₂
8 to help bring the well back.

9 Q. The fact that you have additional -- the four-
10 stage frac, does that increase the risk there may be well
11 damage from allowing it to be shut in?

12 A. Well, we've got to -- You want to keep these
13 wells flowing continuously after you frac them; it seems
14 like they'll clean up better.

15 And if you have shut them in, that water tends to
16 sit out there, and then you might lose your ability to
17 clean that up after the well's been shut in for a while,
18 so...

19 Q. Has LCX previously received authorization to
20 produce a well before the issuance of a compulsory pooling
21 order?

22 A. Yes, our 1625 Fed Com 61, we received permission
23 to open it up before the compulsory --

24 Q. Okay.

25 A. -- was approved.

- 1 Q. Let's look at what we've marked as Exhibit Number
2 2. Is this a breakout of the interest owners in the well?
3 A. Yes.
4 Q. And can you tell us what percentage in the 320-
5 acre unit is voluntarily committed to the well now? Would
6 you identify those interest owners?
7 A. Oh, the ones that have approved it already?
8 Q. Yes.
9 A. That would be Yates, LCX, Parallel Petroleum,
10 Capstone, Elger Exploration, Timothy R. MacDonald -- let's
11 see who else -- and of course there's Yates Drilling
12 Company, Myco Industries, Abo Petroleum Corp., and Marathon
13 Oil has approved and CMW Interests. I believe that's them.
14 Q. All right. Are the interest owners we're seeking
15 to pool at this point, are they Westway Petroleum --
16 A. Westway Petroleum, yes.
17 Q. -- Hunt Oil --
18 A. Hunt, yes.
19 Q. -- the A.L. Mangum/Elliott Trust interests?
20 A. Yes.
21 Q. And what is the percentage of the unjoined
22 interest that you seek to pool?
23 A. Let's see, there's like -- a little over 1
24 percent.
25 Q. Approximately 5.14 acres in the well?

1 A. Right.

2 Q. Okay. And is LCX seeking the imposition of a
3 200-percent risk penalty against those unjoined working
4 interests?

5 A. Yes.

6 Q. Does LCX also seek to be designated operator of
7 the well?

8 A. Yes.

9 Q. In your opinion, has LCX made a good faith effort
10 to locate all of the unjoined working interest owners and
11 communicate with them in order to obtain their voluntary
12 participation in the well?

13 A. Yes, we've -- Do you want me to elaborate on
14 that?

15 Q. Yeah, why don't you explain those efforts?

16 A. We created -- put together an AFE back in
17 December, around December 20th, '05, and we sent that to
18 Yates, and we have that as an exhibit.

19 Q. Is that Exhibit 3?

20 A. Exhibit 3.

21 Q. Is Exhibit 3 the transmittal letter for the first
22 AFE?

23 A. Right, to Chuck Moran. And then later on in
24 February, '06, February 15th, we -- or 16th, we sent out a
25 JOA to all the working interest owners. That should be

1 Exhibit 4.

2 Q. All right. And is Exhibit 5 a brief copy of the
3 JOA?

4 A. Yes.

5 Q. It was sent to all interest owners?

6 A. Right, and that was put together in January.

7 Q. Okay.

8 A. That JOA went out 2-16-06.

9 Q. All right, let's look at Exhibit Number 6.
10 Identify that, please.

11 A. Let's see, is that this -- Yeah, Exhibit 6 is
12 your -- it's an updated AFE that we put together later on,
13 because the cost had increased on drilling and completion
14 of these wells. And we sent this out to all the working
15 interest owners also --

16 Q. All right.

17 A. -- and that was done in May.

18 Q. Now let's turn to Exhibit Number 7. Would you
19 identify that, please?

20 A. That's this other AFE -- Let's see. This is the
21 first AFE that went out, that we sent out in December, and
22 Yates signed it.

23 Q. And did Yates return it to LCX on August 4th of
24 this year?

25 A. Yes.

1 Q. And is it your understanding that Yates has now
2 agreed to execute the updated AFE and participate in the
3 well?

4 A. Yes, according to our lawyer he talked to Chuck
5 Moran late last night, and they're agreeing to the new
6 updated AFE and drilling the well, and we're supposed to
7 have an engineering meeting next week with their people,
8 and at that time they'll execute the AFE.

9 Q. And when we say Yates, we mean Yates Petroleum
10 Corporation, Yates Drilling Company, Myco Industries --

11 A. Myco --

12 Q. -- Abo Petroleum?

13 A. Right.

14 Q. And based on those representations to LCX
15 yesterday, we're not seeking to force pool the Yates
16 interest; is that right?

17 A. Yes.

18 Q. All right. Let's look back at Exhibit 6, which
19 is the May AFE. Would you identify those well cost totals
20 on there, please?

21 A. Yes, dryhole cost is \$1,358,000, and completed
22 total is \$2.467 million.

23 Q. All right. And are you satisfied that the costs
24 reflected on that AFE are in line with what's being charged
25 by other operators in the area --

1 A. Yes.

2 Q. -- for similar wells?

3 A. Right, real close.

4 Q. And what is LCX's estimate of drilling and
5 producing overhead rates for the well?

6 A. Our overhead rate while drilling is \$5500, and
7 producing overhead will be \$550 a month.

8 Q. And are those rates also in line?

9 A. Those are in line.

10 Q. Okay. Are you recommending that those rates and
11 charges be incorporated into the order that issues by the
12 Division from this hearing?

13 A. Yes.

14 Q. And is LCX requesting that the order provide for
15 an adjustment of the drilling and producing overhead rates
16 in accordance with the current COPAS bulletin?

17 A. Yes.

18 Q. In your opinion, Mr. Gillette, would granting
19 LCX's Application be in the interest of conservation,
20 prevention of waste and protection of correlative rights?

21 A. Yes.

22 Q. And were Exhibits 1 through 7 prepared by you or
23 compiled by you?

24 A. Yes.

25 MR. HALL: At this point, Mr. Examiner, we would

1 also Exhibit 8, which is our notice affidavit for the
2 Application. Move the admission of all of those exhibits,
3 and that concludes our direct of this witness.

4 EXAMINER CATANACH: Exhibits 1 through 8 will be
5 admitted.

6 Do you have any questions, Ms. Munds-Dry?

7 MS. MUNDS-DRY: No questions.

8 EXAMINATION

9 BY EXAMINER CATANACH:

10 Q. Mr. Gillette, have you spoken to Hunt Oil,
11 Westway Petroleum and A.L. Mangum -- is it the A.L. Mangum
12 individual? I thought that was a trust. Mangum. Is that
13 the interest you're pooling, the A.L. Mangum?

14 A. It shows on the fractional interest list here
15 A.L. Mangum individually.

16 Q. Okay. Have you spoken to the parties that you're
17 pooling today?

18 A. Not directly, just by mail and with these AFEs --

19 Q. And what --

20 A. -- notifications.

21 Q. I'm sorry, what did they receive from you guys?
22 The initial well proposal?

23 A. They received this May AFE and the JOA, I
24 believe. That was mailed to them. And we sent that AFE
25 out under a blanket letter, of course, just saying working

1 interest owners.

2 Q. Okay. The May AFE and what else?

3 A. The JOA.

4 Q. So did they not get an initial well proposal from
5 you guys?

6 A. They just really -- They got this AFE, is what
7 they got.

8 Q. So you don't know what the status of their --
9 whether they're going to joint or whether they're --

10 A. Well, we have approved AFEs on some of these,
11 don't we?

12 Q. No, the parties that you're pooling, you don't
13 know if they're going to join in the well or if they have a
14 problem with anything, or you haven't spoken to them?

15 A. No, we haven't spoken to them, no. You know, we
16 weren't aware of these people being involved at the time of
17 drilling the well. We were on a deadline --

18 Q. That brings me to my --

19 A. -- lease --

20 Q. Go ahead.

21 A. -- lease deadline. All we knew, we knew that
22 Yates was involved, and --

23 MR. HALL: Mr. Examiner, I can elaborate, if you
24 like.

25 EXAMINER CATANACH: Sure, go ahead.

1 MR. HALL: First initial determination of
2 interest based on a title opinion showed a larger interest
3 for the Yates Petroleum entities, and it turned out that
4 Yates was the unit operator under an old working interest
5 unit that included these other interest owners that were
6 subsequently notified with the AFE and the joint operating
7 agreement. So they were numerous, they were all contacted,
8 they were provided with the AFE and the JOA. Many of them
9 responded and have joined in the well. Others, we simply
10 got no response. I believe in particular the A.L. Mangum
11 interest, there was direct contact with Mr. Mangum and he
12 indicated that he owned no interest in the property. So
13 we're seeking to pool this interest in any event.

14 EXAMINER CATANACH: As far as you know, these
15 three parties did get notice, right?

16 MR. HALL: Yes.

17 EXAMINER CATANACH: So you do have good addresses
18 on that?

19 MR. HALL: Yes, and they were notified of the
20 hearing as well.

21 Q. (By Examiner Catanach) Okay. I'm a little
22 concerned in what seems to be a pattern with LCX of
23 drilling the wells before you pool the interest. Can you
24 tell me why that's being done?

25 A. Well, it's a matter of losing the state lease

1 that we have out there. This one had to be drilled by
2 sometime in June, late June, 1st of July, and the rig -- I
3 have two rigs running over there, and there was only one
4 slot to get this well drilled. We've had it permitted and
5 everything.

6 We were under the -- You know, when we bought
7 this deal we were well under the gun to get this stuff
8 drilled. I had to move rigs out of Texas over there to get
9 this done and stuff, so... The previous owner had not done
10 their full job on the land part of it.

11 Q. Is this -- Is there going to be more similar to
12 this, Mr. Gillette?

13 A. Shouldn't be, shouldn't be. I think we have an
14 understanding now with Yates. We got them involved in a
15 couple other deals. But I think now if we've gotten
16 through this one that the next deals with them will go
17 smoother, and we'll be able to avoid this with them. I
18 have one other well drilled that we are involved with Yates
19 on it also.

20 The rest of them, we're getting state units put
21 together, and this should be the last one we have to deal
22 with.

23 MR. HALL: Mr. Examiner, recently LCX acquired
24 Parengo -- it was a stock acquisition -- and with that they
25 acquired these Eddy County properties with short-term

1 leases on them, with upcoming expirations. That put LCX in
2 a bind. They've been working pretty furiously --

3 THE WITNESS: Yes.

4 MR. HALL: -- to preserve leases. I understand
5 they have four rigs working full time now --

6 THE WITNESS: Two rigs.

7 MR. HALL: Two rigs working full time --

8 THE WITNESS: Right.

9 MR. HALL: -- just on this prospect, to preserve
10 leases. It appears that they have everything in hand now.
11 So that's --

12 THE WITNESS: We had to catch up there at the
13 beginning. I mean, I had two months to get something going
14 when we bought his deal, and Parenco had effectively shut
15 down doing any land work or anything for -- As soon as they
16 knew they were going to sell it, which was in the previous
17 year, they just stopped land work over there. So when we
18 took it over, I had two months to get started, get rigs
19 over there and -- First lease started running out in June
20 of '05.

21 EXAMINER CATANACH: All right. Is there anything
22 else, Mr. Hall?

23 MR. HALL: No, sir.

24 EXAMINER CATANACH: As far as the authority to
25 produce, I'm not going to give anybody authority to produce

1 until this interest is consolidated. However, I will try
2 and get this order out in the next day or two, hopefully by
3 tomorrow, so you guys won't have too big a bind to wait on
4 me.

5 So there being nothing further in this case, Case
6 13,757 will be taken under advisement.

7 (Thereupon, these proceedings were concluded at
8 8:48 a.m.)

9 * * *

10
11
12
13
14 I do hereby certify that the foregoing is
15 a complete record of the proceedings in
16 the Examiner hearing of Case No. 13757,
17 heard by me on August 17, 2006.
18 David R. Lattin, Examiner
19 Oil Conservation Division
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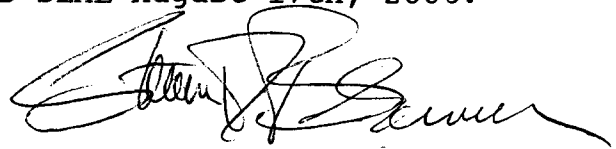
CERTIFICATE OF REPORTER

STATE OF NEW MEXICO)
) ss.
COUNTY OF SANTA FE)

I, Steven T. Brenner, Certified Court Reporter and Notary Public, HEREBY CERTIFY that the foregoing transcript of proceedings before the Oil Conservation Division was reported by me; that I transcribed my notes; and that the foregoing is a true and accurate record of the proceedings.

I FURTHER CERTIFY that I am not a relative or employee of any of the parties or attorneys involved in this matter and that I have no personal interest in the final disposition of this matter.

WITNESS MY HAND AND SEAL August 17th, 2006.



STEVEN T. BRENNER
CCR No. 7

My commission expires: October 16th, 2006