

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:)
APPLICATION OF CHI OPERATING, INC.,)
FOR COMPULSORY POOLING, LEA COUNTY,)
NEW MEXICO)

CASE NO. 13,815

ORIGINAL

REPORTER'S TRANSCRIPT OF PROCEEDINGS

EXAMINER HEARING

BEFORE: DAVID R. CATANACH, Hearing Examiner

November 9th, 2006

Santa Fe, New Mexico

2006 NOV 20 PM 12 50

This matter came on for hearing before the New Mexico Oil Conservation Division, DAVID R. CATANACH, Hearing Examiner, on Thursday, November 9th, 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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I N D E X

November 9th, 2006
 Examiner Hearing
 CASE NO. 13,815

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APPLICANT'S WITNESS:	
<u>JOHN W. QUALLS</u> (Landman)	
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A P P E A R A N C E S

FOR THE DIVISION:

DAVID K. BROOKS, JR.
Assistant General Counsel
Energy, Minerals and Natural Resources Department
1220 South St. Francis Drive
Santa Fe, New Mexico 87505

FOR THE APPLICANT:

HOLLAND & HART, L.L.P., and CAMPBELL & CARR
110 N. Guadalupe, Suite 1
P.O. Box 2208
Santa Fe, New Mexico 87504-2208
By: WILLIAM F. CARR

* * *

1 WHEREUPON, the following proceedings were had at
2 9:08 a.m.:

3 EXAMINER CATANACH: Call Case 13,815, the
4 Application of Chi Operating, Inc., for compulsory pooling,
5 Lea County, New Mexico.

6 Call for appearances.

7 MR. CARR: May it please the Examiner, William F.
8 Carr with the Santa Fe office of Holland and Hart, L.L.P.
9 We represent Chi Operating, Inc., in this case. I would
10 ask that the record reflect that my witness, John Qualls,
11 has previously been sworn and his credentials as an expert
12 in petroleum land matters accepted and made a matter of
13 record.

14 EXAMINER CATANACH: Are there any additional
15 appearances in Case 13,815? There are none.

16 Let the record show that Mr. Qualls has been
17 sworn in in the previous case and has been qualified.

18 And you may proceed.

19 JOHN W. QUALLS,

20 the witness herein, having been previously duly sworn upon
21 his oath, was examined and testified as follows:

22 DIRECT EXAMINATION

23 BY MR. CARR:

24 Q. Mr. Qualls, are you familiar with the Application
25 filed in this case on behalf of Chi?

1 A. Yes.

2 Q. And are you familiar with the status of the lands
3 in the area that's the subject of this Application?

4 A. Yes.

5 Q. Would you briefly review for Mr. Catanach what it
6 is that Chi seeks in this case?

7 A. We seek an order pooling all mineral interest
8 from the surface to the base of the Cisco/Canyon in the
9 northeast quarter of Section 11, 14 South, 34 East, Lea
10 County, New Mexico.

11 Q. For pooling all formations on 160 spacing in the
12 northeast quarter?

13 A. Yes, sir.

14 Q. We're also seeking an order pooling the southeast
15 of the northeast quarter as well; is that correct?

16 A. Yes.

17 Q. What is the name of the well that will be drilled
18 on these pooled spacing units?

19 A. It's the Elkan Number 2, to be drilled 1980 from
20 the north line and 660 from the east line of Section 11.

21 Q. And that's a standard location?

22 A. Yes, sir.

23 Q. Would you identify and review for Mr. Catanach
24 Exhibit Number 1?

25 A. Exhibit Number 1 is a land plat showing the

1 northeast quarter of Section 11, 14 South, 34 East, Lea
2 County, New Mexico.

3 Q. And the spacing unit is -- the pooled area is
4 shaded in yellow; is that correct?

5 A. Yes.

6 Q. And the location of the proposed well is also
7 indicated?

8 A. I'm not sure if it's on there. It's 1980 from
9 the north and 660 --

10 Q. Okay.

11 A. -- from the east. It would be in the southeast
12 of the northeast quarter.

13 Q. Let's go to Exhibit 2. Would you review this for
14 Mr. Catanach?

15 A. Exhibit 2 is an ownership breakdown of the leases
16 in the area, showing Chesapeake with a 38.4375 percent,
17 Pride with a 6.25 percent, and Chi with a 55.3125 percent.

18 Q. And these percentages are based on a 160-acre
19 spacing unit?

20 A. Yes.

21 Q. Behind this, marked as Exhibit Number 3, we have
22 the APD for the well?

23 A. Yes.

24 Q. And then behind that we have correspondence; is
25 that correct?

1 A. Yes.

2 Q. When did you first propose this well?

3 A. I started talking to Pride back in July -- I
4 believe July 28 was my first letter to them. I tried
5 numerous phone calls, and then I sent them a certified
6 letter August the 17th of 2006.

7 Q. And have you been able to reach an agreement with
8 Pride?

9 A. No, sir, I haven't talked to anybody at Pride.

10 Q. Have they responded to any of your
11 correspondence?

12 A. No.

13 Q. Has Chesapeake agreed to voluntarily commit its
14 interest to the well?

15 A. Yes, Chesapeake has signed an AFE.

16 Q. So the only interest being pooled is the interest
17 of Pride Energy Company?

18 A. Yes.

19 Q. And that is a 6.25-percent working interest in
20 the well?

21 A. Yes.

22 Q. Could you identify what has been marked as
23 Exhibit Number 5?

24 A. Exhibit Number 5 is the AFE for the Elkan Number
25 2.

1 Q. And what are the costs reflected on this exhibit?

2 A. Dryhole cost would be \$1,297,066.50; completed
3 well would be \$1,872,817.77.

4 Q. Are these costs in line with what has been
5 incurred by Chi in drilling other wells in the area?

6 A. Yes.

7 Q. Is Exhibit Number 6 a copy of the operating
8 agreement for this well?

9 A. Yes.

10 Q. Are the COPAS accounting procedures attached to
11 this JOA?

12 A. Yes.

13 Q. Do these procedures provide for periodic
14 adjustment of the overhead and administrative costs
15 incurred while drilling or producing the well?

16 A. Yes.

17 Q. And does Chi request that the order entered in
18 this case also provide for adjustment of these costs in
19 accordance with these COPAS procedures?

20 A. Yes, sir.

21 Q. Have you made an estimate of the overhead and
22 administrative costs to be incurred while drilling this
23 well and while producing it, if it is successful?

24 A. Yes.

25 Q. What are those?

1 A. Drilling rate will be \$6000 a month, the
2 producing rate will be \$600 a month.

3 Q. And these are again from the Ernst and Young
4 average figures for a well in this area to this depth?

5 A. Yes.

6 Q. Do you recommend these figures be incorporated
7 into the order that results from this hearing?

8 A. Yes.

9 Q. Does Chi request that a maximum charge for risk
10 of 200 percent be imposed on each working interest that
11 isn't voluntarily committed to the well?

12 A. Yes.

13 Q. And does Chi seek to be designated operator of
14 the well?

15 A. Yes.

16 Q. What is the status of the well at this time?

17 A. We're building location now and moving the rig in
18 probably in the next three or four days.

19 Q. In your opinion, will granting this Application
20 and the drilling of this well be in the best interest of
21 conservation, the prevention of waste and protection of
22 correlative rights?

23 A. Yes.

24 Q. Is Exhibit Number 7 an affidavit confirming that
25 notice of this Application has been provided in accordance

1 with the rule to the Division?

2 A. Yes.

3 Q. And the return receipt showing it was received by
4 Pride is also enclosed; is that right?

5 A. Yes.

6 Q. Also attached is a copy of the legal
7 advertisement that was run in the Lovington paper?

8 A. Yes.

9 Q. Were Exhibits 1 through 7 prepared by you or
10 compiled at your direction?

11 A. Yes.

12 MR. CARR: May it please the Examiner, at this
13 time we'd move the admission into evidence of Chi Exhibits
14 1 through 7.

15 EXAMINER CATANACH: Exhibits 1 through 7 will be
16 admitted.

17 MR. CARR: And that concludes my examination of
18 Mr. Qualls.

19 EXAMINATION

20 BY EXAMINER CATANACH:

21 Q. Mr. Qualls, who is Darr Angell?

22 A. He was a -- he's a surface owner and a mineral
23 owner out there that I just got leased last week. We've
24 been talking with him and we sent him a lease back in June
25 or July, and he said he was going to sign it and he finally

1 sent it in.

2 Q. Okay, your Application does say from the surface
3 to the base of the Morrow, but you're just pooling from the
4 surface to the base of the Cisco/Canyon?

5 MR. CARR: That is correct.

6 MR. BROOKS: No questions.

7 EXAMINER CATANACH: All-righty, that's -- I think
8 that's it.

9 MR. CARR: That concludes our presentation in
10 this case.

11 EXAMINER CATANACH: There being nothing further,
12 Case 13,815 will be taken under advisement.

13 Let's take a 15-minute break.

14 (Thereupon, these proceedings were concluded at
15 9:16 a.m.)

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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. 13815,
heard by me on November 9, 2006
David R. Catanch, Examiner
Oil Conservation Division

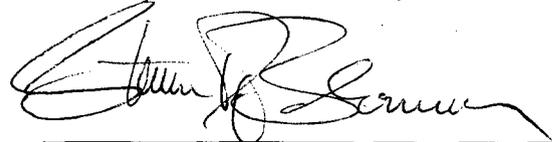
CERTIFICATE OF REPORTER

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 November 11th, 2006.



STEVEN T. BRENNER
 CCR No. 7

My commission expires: October 16th, 2010