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. 13870
ORDER NO. R-12754

APPLICATION OF QUEST CHEROKEE, LLC FOR APPROVAL OF AN APPLICATION FOR PERMIT TO DRILL, LEA COUNTY, NEW MEXICO.

ORDER OF THE DIVISION

BY THE DIVISION:

This case came on for hearing at 8:15 a.m. on February 15, 2007, at Santa Fe, New Mexico, before Examiner David R. Catanach.

NOW, on this 3rd day of May, 2007, 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) The applicant, Quest Cherokee, LLC ("Quest") seeks approval of a Division Form C-101 (Application for Permit to Drill, Re-Enter, Deepen, Plugback or Add a Zone ("APD")) for its State 9-4 Well No. 1, which is proposed to be drilled at a standard oil well location 990 feet from the North line and 2310 feet from the West line (Unit C) of Section 9, Township 18 South, Range 38 East, NMPM, Lea County, New Mexico, to test the San Andres formation, Undesignated West Bishop Canyon-San Andres Pool (Oil – 05790). The NE/4 NW/4 of Section 9 is to be dedicated to the well forming a standard 40-acre oil spacing and proration unit for this pool.

(3) Barbara A. Cox, Steve Cox, Lee Roberson and Tom Duncan, ("The Cox Group") all surface owners at or in the vicinity of Quest's proposed well, appeared at the hearing in opposition to the application.

(4) At the hearing, Quest testified that the advertisement for this case

incorrectly stated the name of its proposed well. Quest's evidence shows the name of the proposed well to be the West Bishop State Well No. 1, hereinafter referred to as the "subject well" or "proposed well".

(5) The evidence and testimony presented demonstrates that prior to Quest filing an APD for the proposed well, the Hobbs District office of the Division ("Hobbs OCD") received a letter of objection to the proposed well dated December 1, 2006, from Mr. Michael Newell, legal counsel for the opponents in this case. The Hobbs OCD subsequently advised Quest that the APD for the proposed well would not be approved at the district level, and that the application would require a hearing before a Division examiner.

(6) Quest presented evidence that demonstrates that:

(a) the proposed well is located on the northern edge of the city of Hobbs, New Mexico. While the well is not located within the city limits of Hobbs, it is located in a populated area containing houses, schools and businesses;

(b) the NW/4 of Section 9 is contained within State of New Mexico Lease No. VA-3080. This lease was obtained by Upland Corporation on February 1, 2004. The acreage was subsequently assigned to Chesapeake Exploration Limited Partnership ("Chesapeake") and then to Tierra Oil Company, LLC ("Tierra"). Quest has purchased the right to develop this lease from Tierra. Pursuant to the term assignment from Chesapeake to Tierra, Quest is obligated, unless an additional extension of time is obtained, to commence drilling the proposed well by May 1, 2007;

(c) the proposed well is situated in empty pastureland that is bordered on the north and west by family residences. The closest residence appears to be approximately 600 feet northwest of the proposed well; and

(d) the surface of the land on which the proposed well is located is owned by Barbara A. Cox.

(7) Prior to Quest obtaining the rights to develop the NW/4 of Section 9, Tierra conducted an investigation into the surface issues at the proposed well site. As evidence in support of its application, Quest presented the following additional evidence obtained by Tierra:

(a) Tierra contacted the Hobbs City Engineer's office and verified that the drill site for the proposed well is not located within the city limits of Hobbs, nor within any extra territorial jurisdiction controlled by the city of Hobbs;

(b) Tierra contacted the Lea County Manager and verified that there are no county regulations applicable to the acreage at the drill site;

(c) Tierra verified with the New Mexico State Land Office that there are no special lease stipulations that would govern development at the proposed well site; and

(d) Tierra stated that a portion of the surface fee acreage within the NE/4 NW/4 of Section 9 may be within a housing subdivision known as the Country Living Estates Subdivision No. 2. The covenants for this subdivision state that the land is to be used for residential purposes, and that no noxious or offensive trade or activity is to occur on the land. However, the covenants do not specifically restrict oil and gas activity, which, in any event, would not be binding on the reserved mineral interest of the State of New Mexico.

(8) Quest has attempted to negotiate with Barbara A. Cox regarding surface use issues at the proposed well site, but has been unsuccessful in these efforts.

(9) The proposed West Bishop State Well No. 1 is Quest's attempt to re-establish production within the West Bishop Canyon-San Andres Pool. There are currently no active wells producing from this pool.

(10) The proposed West Bishop State Well No. 1 is a northwest step-out from wells within Section 9 that previously produced from the West Bishop Canyon-San Andres Pool. Quest's geologic interpretation shows that there is a thickening of the San Andres pay zone within the NW/4 of Section 9.

(11) The West Bishop Canyon-San Andres Pool has been substantially depleted by production. Consequently, Quest does not expect to encounter abnormal pressures during the drilling of the well.

(12) Quest's evidence further shows that directionally drilling the proposed well from a different surface location would add substantial drilling costs and would likely render the drilling of the well uneconomic.

(13) Quest stated in its testimony that it is willing to do whatever the Division deems necessary in order to protect the health and safety of the residents and the public in this area from any potential hazards associated with drilling and producing the proposed West Bishop State Well No. 1.

(14) The Cox Group presented evidence to support its opposition to the drilling of the West Bishop State Well No. 1. Much of the data cited in its testimony was obtained from a publication entitled "Oil and Gas at Your Door? A Landowners Guide to Oil and Gas Development." This publication was developed by the Oil & Gas Accountability Project, Durango, Colorado. The specific complaints are described as follows:

(a) **The well is located in close proximity to houses, a school and a retirement home**. The proposed well is located approximately 567 feet from the nearest residence, approximately 1439 feet from an elementary school, and approximately 2055 feet from a retirement home;

(b) **Noise levels**. The Cox Group contends that noise levels during drilling and production operations at the proposed well will be excessive. In support of this contention, it cited a study conducted in La Plata County, Colorado that demonstrates that various oil and gas activities emit noise levels in the range of 50-88 DBA's (A-Weighted Decibel). Further evidence was presented to show that the State of Colorado has promulgated noise control regulations for oil and gas development in residential areas that limit noise levels to 50-55 DBA's at a distance of 350 feet from the source;

(c) **Property values**. The Cox Group contends that their property values will decline as a result of the drilling of the West Bishop State Well No. 1. In support of this contention, it cited a study conducted in La Plata County, Colorado which shows that despite an overall increase in housing values between 1990 and 2000, the selling price for properties that had an oil or gas well on them was 22% less than a similar property without a well on site;

(d) **Health and safety concerns related to the discharge of Hydrogen Sulfide (H_2S) and Volatile Organic Compounds (VOC's)**. The Cox Group is concerned that H_2S and VOC's will be discharged to the atmosphere from production facilities at or near the well site. Discharges of this nature may endanger the health and safety of the residents and the public in the vicinity of the well or the production facility;

(e) **Health, environmental and safety concerns related to the use of various chemical additives used in drilling and production operations**. The Cox Group is concerned that the use of chemicals and/or additives used in drilling and production operations will pose a threat to the surface and subsurface environment and pose safety and health hazards to the residents and the public in the vicinity of the proposed well;

(f) **The use of earthen pits for drilling and/or production operations may pose a threat to groundwater in the vicinity of the proposed well**. The Cox Group is concerned that the use of earthen pits for drilling and/or production operations may endanger ground water; and

(g) **The possibility of a well blowout during drilling operations poses a significant threat to the health and safety of the residents and the public in the vicinity of the proposed well**.

(15) Barbara A. Cox ("Mrs. Cox"), the surface owner at the proposed well site, testified at the hearing via conference phone from Hobbs, New Mexico. Mrs. Cox stated in her testimony that she is opposed to the drilling of the West Bishop State Well No. 1, even if the Division imposes additional requirements to protect the health and safety of the residents and the public.

(16) The Cox Group further contends that the application should be denied based upon Quest's failure to comply with Division rules and procedures, including:

(a) Quest's failure to register with the Division;

(b) Quest's failure to file Division Forms C-101 and C-102 (Well Location and Acreage Dedication Plat) with the Hobbs OCD; and

(c) Quest's notice of hearing incorrectly described the location of the West Bishop State Well No. 1 as being five miles north-northwest of Hobbs, New Mexico.

(17) Mr. Cliff Burch, Superintendent of the Hobbs Municipal Schools, sent a letter to the Division dated February 13, 2007. In his letter, Mr. Burch expressed concern that the West Bishop State Well No. 1, being in close proximity to the College Lane Elementary School, will pose a threat to the health and safety of the students attending that school.

(18) The position of the Cox Group is that the application of Quest should be denied. In the alternative, however, the Cox Group requests that in the event the application is approved, Quest should be required to take measures to protect the health and safety of the residents and the public, among them: i) the well and/or production facilities should be fenced; ii) pipelines should be employed to transport production or waste out of the area so as to minimize truck and transport traffic; iii) no flaring of gas or waste should be allowed; iv) the location should be constructed with a lightning suppression grid system; v) a vapor recovery system should be utilized; and vi) a closed loop drilling technology should be utilized.

(19) The evidence presented demonstrates that Quest's notice of hearing in this case is sufficient, and that the other procedural issues raised by the Cox Group are not grounds for dismissal or denial of this application.

(20) The evidence and testimony presented in this case demonstrates that Quest, by virtue of obtaining certain operating rights from Tierra, has the right to develop the oil and gas reserves underlying the NW/4 of Section 9.

(21) The geologic evidence presented by Quest is sufficient to justify the drilling of the West Bishop State Well No. 1 at the proposed location.

(22) "Correlative Rights" is defined by the New Mexico Oil and Gas Act [NMSA 1978, Section 70-2-33.H], in part, as "the opportunity afforded, as far as it is practicable to do so, to the owner of each property in a pool to produce without waste his just and equitable share of the oil or gas, or both, in the pool".

(23) In order to protect correlative rights, Quest should be authorized to drill its West Bishop State Well No. 1 at the proposed location in Section 9.

(24) The rights of a surface owner do not constitute "correlative rights" within the above definition.

(25) The Cox Group presented sufficient evidence to demonstrate that due to the proximity of the West Bishop State Well No. 1 to houses, schools and other facilities, Quest should be required to take special precautions during drilling and production operations.

(26) The New Mexico Oil and Gas Act [NMSA 1978, Section 70-2-12.B] authorizes the Division to "prevent fires", "to require wells to be drilled, operated and produced in such manner as to prevent injury to neighboring leases or properties" and "to regulate the disposition of nondomestic wastes resulting from oil and gas production".

(27) Quest presented little, if any, engineering evidence relating to its proposed drilling and production operations. Consequently, there is insufficient evidence to impose specific requirements at this time.

(28) The Hobbs OCD routinely approves, oversees and controls drilling and production operations within the city of Hobbs. Consequently, the Hobbs OCD should be the lead entity to determine the measures to be taken by Quest in order to protect the health and safety of the residents and the public at the vicinity of the well and production facilities, and in order to protect the surface and subsurface environment from contamination. The issues to be addressed by the Hobbs OCD should include, but are not necessarily limited to:

(a) blowout Prevention;
(b) possible use of closed loop drilling technology;
(c) fencing of the well and production facilities;
(d) the flaring or venting of H_2S and VOC's;
(e) pipelines and/or production facilities; and
(f) lightning protection

(29) Approval of the application, subject to certain provisions and restrictions relating to drilling and production operations, will afford the applicant the opportunity to produce its just and equitable share of the oil and gas reserves underlying the NE/4 NW/4 of Section 9, will allow the recovery of oil and gas reserves underlying the NE/4 NW/4 of Section 9 that may otherwise not be recovered, thereby preventing waste, and will protect the health and safety of the residents and the public in the vicinity of the well and production facilities.

IT IS THEREFORE ORDERED THAT:

(1) The applicant, Quest Cherokee, LLC is hereby authorized to drill its West Bishop State Well No. 1 at a standard oil well location 990 feet from the North line and 2310 feet from the West line (Unit C) of Section 9, Township 18 South, Range 38 East, NMPM, Lea County, New Mexico, to test the San Andres formation, Undesignated West Bishop Canyon-San Andres Pool (Oil – 05790). The NE/4 NW/4 of Section 9 shall be

dedicated to the well forming a standard 40-acre oil spacing and proration unit for this pool.

(2) Prior to commencing drilling and production operations, the applicant shall consult with the Hobbs OCD in order to determine the measures to be taken to protect the health and safety of the residents and the public at the vicinity of the well and production facilities, and in order to protect the surface and subsurface environment from contamination. The issues to be addressed by the Hobbs OCD shall include, but are not necessarily limited to:

(a) blowout prevention;
(b) possible use of closed loop drilling technology;
(c) fencing of the well and production facilities;
(d) the flaring or venting of H_2S and VOC's;
(e) pipelines and/or production facilites; and
(f) lightning protection.

(3) The Hobbs OCD shall issue a conditional APD approval setting forth the specific conditions it deems appropriate, and shall cause copies of the APD to be delivered to counsel who have appeared in this case.

(4) Quest shall not commence drilling operations until five business days after the issuance of the APD approval specifying applicable conditions, and shall conduct all operations in compliance with such conditions.

(5) Jurisdiction is hereby 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

MARK E. FESMIRE, P.E.
Director

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