STATE OF NEW MEXICO
ENERGY AND MINERALS DEPARTMENT
OIL CONSERVATION DIVISION
STATE LAND OFFICE BUILDING
SANTA FE, NEW MEXICO
7 July 1983

COMMISSION HEARING

IN THE MATTER OF:

Application of El Paso Natural Gas Company for the reclassification of marginal gas wells in the prorated gas pools of southeast New Mexico and the suspension of certain proration rules.	CASE 7858
Application of Doyle Hartman for classification as marginal of all wells in the prorated gas pools of southeast New Mexico.	CASE 7905

BEFORE: Commissioner Ramey and Commissioner Kelley

TRANSCRIPT OF HEARING

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MR. RAMEY: The hearing will come to order.

This is a continuation of the June 8th hearing in Case Number 7858 and Case Number 7905.

Is there anyone here today who wishes to make an appearance who did not make an appearance at the June 8th hearing?

Mr. Pearce, did you have something you wished to say?

MR. PEARCE: Mr. Chairman, one order of business before we begin.

I have been handed a stipulation and order of dismissal, which has been agreed to by counsel for El Paso Natural Gas Company and Doyle Hartman, and with your permission, I will read this stipulation to other parties to this matter in the audience, and if they can indicate if they have an objection to this matter, I think we can proceed a little more quickly.

The stipulation and order of dismissal states:

The undersigned applicants and parties by and through their counsel of record hereby stipulate and agree that Indian Basin Upper Pennsylvanian Gas Pool be, and is hereby dismissed and deleted from application and further consideration in the above styled cases.

Subsequent to signature blocks for El

Paso Natural Gas and Doyle Hartman and Moran Exploration Company, there is an order provision to be signed by the Commission, which states:

It is ordered that the Indian Basin Upper Pennsylvanian Pool is hereby dismissed and deleted from further consideration in the above styled cases.

At this time I would ask other counsel in this proceeding if they can on the basis of hearing that stipulation indicate any objections, and there being none, I would suggest that the Commission can enter this order and the case can proceed a little more quickly.

MR. RAMEY: Being no objections, we will so enter the order.

MR. PEARCE: Thank you, sir.

MR. RAMEY: I think we had Mr. Nutter on the stand at the end of the hearing the other day. I would request that he take the stand.

You may proceed, Mr. Carr.

MR. CARR: Mr. Ramey, as you will recall, at the June hearing on Mr. Hartman's proposal some confusion developed as to how that plan would be implemented. The confusion seemed to stem from Exhibit Number Twenty-two, which was offered on behalf of Mr. Hartman.

In an effort to clarify how Mr. Hartman's proposal can be implemented, I would request permission to present limited direct examination with Mr. Nutter. This examination will be limited to how Mr. Hartman's

proposal will be implemented and it all springs from Exhibit 22 previously submitted into evidence.

MR. RAMEY: I think that might be a good idea, Mr. Carr, personally.

DANIEL S. NUTTER,

being called as a witness and being duly sworn previously upon his oath, testified as follows, to-wit:

Q Mr. Nutter, will you please refer to Exhibit Number Twenty-two and just briefly, using that as a starting point, explain how Mr. Hartman's proposal would be implemented?

A Yes. You'll recall that Exhibit Number Twenty-two was a handwritten, sloppy looking, exhibit that was a tabulation of 1982 average adjusted nominations; 1982 average top allowable factors for the fifteen prorated gas pools in southeast New Mexico, and also a tabulation of the 1983 June nominations and the so-called June '83 ceiling which would be placed on wells in each of the prorated gas pools.

Confusion developed as to just what this meant and how this so-called ceiling would be applied. I therefor prepared several exhibits which are based on the data and are background for the data which was presented on Exhibit Number Twenty-two.

Now does the Commission have the exhi-

bits?

MR. CARR: No, just a second. Mr. Nutter, would you please now refer to what has been marked as Hartman Exhibit Twenty-three and review this for the Commission?

A Yes, I will. The first two columns on the previously mentioned Exhibit Number Two were the 1982 average adjusted nominations and the '82 average top allowable factors.

Exhibit Number Twenty-three is a tabulation of the actual nominations and factors for each month in 1982. Over in the righthand column, then, is the average, which was developed for 1982, both of adjusted nominations and factors.

The nominations, as indicated by the footnotes are in thousands of Mcf; the factors are in Mcf; therefor, we would see for the Atoka Pennsylvanian Pool the nominations for the -- the average nominations were 188,400 Mcf for each month. The average factor for each top allowable well would have been 47,204.9 Mcf for the month.

All right, the -- so that's the derivation of the first two columns on Exhibit Number Twenty-two.

Q Will you now refer to Exhibit Number Twenty-four and review this for the Commission?

A Exhibit Number Twenty-four is entitled Hypothetical Fair Share Factors for 1983 Based on Ratio of

Average Adjusted Nominations for 1982 to Average Nonmarginal Factors as Compared to 1983 Monthly Nominations.

Now, the last two columns on Exhibit Number Twenty-two were June nominations and June ceiling factors only. What I've done here, I've taken from Exhibit Number Twenty-three the average adjusted nominations, they're in the first column to the left on Exhibit Number Twenty-four. I've taken the average factors which were derived on Exhibit Number Twenty-three, and listed them in the second column from the left on Exhibit Number Twenty-four. This gives us our average adjusted nominations, our average factors for each one of the pools for 1982.

Then I've taken the January nominations and developed by the same ratio method that was discussed before what the fair share factor -- I'm calling it a fair share factor rather than a ceiling now -- but what a fair share factor for each top allowable well would have been in 1983, based on those nominations and the ratio of nominations to factors in '82.

Now, for June we come over here and we have the same figures that were in columns three and four on Exhibit Number Twenty-two with a couple of exceptions, a couple of minor errors were found.

There was a substantial error in the calculation of the allowable -- of the adjusted nominations for the Monument-McKee. There was a misplaced decimal point and whereas the factor, the nominations had been shown in --

in Exhibit Number Twenty-two to be 556,600. The actual nominations averaged 92.3 thousand in that pool. That's the only one with any substantial change.

But on Exhibit Number Twenty-four we arrive at these fair share factors, which is the -- what a top allowable well would be. It would also be the limit at which no well, theoretically, would produce in excess under Mr. Hartman's proposal of reclassification as marginal.

This would be the ceiling, the cap, the maximum fair share factor.

Q Will you now refer to Exhibit Number Twenty-five?

A Exhibit Number Twenty-five is a mini-proration schedule for the first six months of 1983. I've taken six proration units and applied the Hartman formula for those six proration units.

The first well is Alpha Twenty-one's El Paso Plant. This well currently is -- or in the June schedule, at least, was classified as a nonmarginal well. It's overproduced; has a small acreage factor of .50.

The next well is the ARCO Oil and Gas Company Shipley AWN-6 in Unit E of Section 27, 22, 36. These are all in the Jalmat Pool, by the way. This well is also a nonmarginal well. It's on a standard sized unit. It has an underproduced status in the proration schedule.

The next proration unit is Conoco's Vaughn B-1, which is a multi-well unit. The 320-acre unit

has an acreage factor of 2. It is classified as marginal.

The next well is a marginal well on a standard sized 160-acre unit. It's the Gulf Jonda No. 3 in Section 11 of 23, 36; has a low production history.

The next two wells are Doyle Hartman wells, the first being the Bates BB&S in Section 29 of 25, 37. This well has an acreage factor of .75 and carries in the proration schedule as a nonmarginal well a small amount of overproduction.

The next well is the Husky Woolworth Well, which is a nonmarginal well on an acreage factor of in the June proration schedule.

Now, what I have done here for each one of these months, I have taken the ratio of the nominations for that respective month and compared them to the nominations, the average adjusted nominations for 1982. We'll see that January's nominations, which totaled 1,409,100, rounded off, were 134.91 percent of the 1982 average adjusted nominations. This would give us a factor of 1.3491.

Now, I've arrived at two fair shares here. The first fair share, which is listed under the heading January Fair Share, at 134.91 percent, would be the fair share based on average 1982 production for that well.

Then over to the right of that two columns is the maximum fair share with acreage factor. Now that is based solely on the application of the ratio of January nominations in 1983 to average adjusted nominations

lin 1982 times the top unit allowable in 1982, and we will see that in January that .50 acreage factor Alpha Twenty-one Well would have an allowable based on its 1982 production of 7069. It would have a maximum fair share with the acreage factor applied of 8,269.

Now, we'll go down to the Shipley Well. Based on its 1982 production it would only have a fair share factor of 10,831, because that well was curtailed a great deal in 1982, so its production was not high. So when we apply the -- the allowable factor of 134.91 percent to that, we only come up with an allowable of 10,831 for a fair share; however, under maximum fair share with acreage factor, because that well is on a full size unit, it would have a maximum fair share allowable of 16,539.

Now we'll go to the Conoco Vaughn Unit there. This is a marginal unit. The wells do not normally produce very much, and under the calculation applied to the '82 production it would have an allowable of 11,385; however, based on its large acreage factor it could have an allowable, a maximum fair share allowable, if the wells would make it, under the January formula of 33,077. The wells won't make that but if they were in condition to do so, that would be the maximum they could produce.

The Gulf Jonda Well is also a very small well. While it gets a fair share allowable of only 2169, it could produce up to 16,539.

Now, the Bates BB&S Well of Hartman had a

1982 average production of 9849. Its fair share based on production only would be 13,287; however, its maximum fair share, applying the proposed formula, would be 12,403, because it's on a short acreage factor, so that well would not be permitted to produce the fair share based on production. It would be limited to the fair share based on acreage factors.

The other well of Hartman averaged 5556 Mcf per month in '82. Its fair share, based on 1982 production would be 7496: however, its fair share based on the application of the acreage factors would be 8269. So in these two wells Hartman has one that would be limited by the maximum; he has another one that would be limited by his '82 production.

The '82 production figure is a tentative figure, however, it's not proposed as a limit. The limits are in the maximum fair share with acreage factor column.

Now we go on through the mini-proration schedule, we'll see that the February factor was 122.18 percent, because that month nominations were 1,276,000 as opposed to 1,044,000 in -- average in 1982.

So the allowables are a little bit less than they were in January.

We go down to March, this time the nominations totaled only 864,100, so the allowable factor applied to average adjusted nominations becomes only 82.73 percent and the allowables are getting less in March of '83.

Now we go to April, allowables dipped down to 535,000 and the acreage factor became 51 percent.

In May allowables climbed back up a little bit and the total nominations were 657,600. The theoretical maximum would be 62.96 percent and allowables have improved somewhat over the depressed allowables in April.

June, however, was the month that you'll recall from previous testimony that the allowables were very, very low. Nominations only totaled 32 percent of the average for 1982, and you'll see that the factors, the maximum factors, are the lowest of any time there. The maximum factor for an acreage -- maximum fair share, with acreage factor of 1.00 is only 3922, while these wells on short acreage factors have less than that.

Q Now, Mr. Nutter, to be sure there's no confusion on this point, the figure on this proration schedule that actually controls is the maximum fair share with acreage factor.

A That is correct. The other -- the other figure, the other column of fair share, is a guide. If the 1982 production is an indication of what the well will produce, that would give you an indication of what the well would produce under this month's allowable factor; however, we know that it's not truly indicative of what the wells will produce, because some of them were curtailed rather seriously in 1982; others were not curtailed quite so ser-

iously.

Q Will you now refer to what has been marked as Hartman Exhibit Number Twenty-six and review this for the Commission?

A Exhibit Twenty-six is a graphic depiction of what I've been trying to say. It simply is the depiction of the formula in which A equals B divided by C times D.

A is the curved month production ceiling, or, if you will, the fair share factor. That's equal to the current month pipeline nominations for a given pool, divided by the average adjusted monthly nominations for 1982 for that pool, times the average monthly allowable for an acreage factor of one in the pool.

It tabulates those figures which were depicted earlier, then, on Exhibit Number Twenty -- in the righthand column of Exhibit Number Twenty-three and in the first two columns on Exhibit Number Twenty-four, the nominations and the average factors developed for 1982.

Q Will yo now review Exhibit Number Twenty-seven?

A Exhibit Number Twenty-seven shows how this would be applied. It's an example of how it would be applied. It's pretty much a repeat of the mini-proration schedule which was previously discussed, only it's for the month of June.

Here the nominations were 334,211 Mcf. The average nominations for the previous year were

1,044,000. You divide the current month nominations -- current nominations of B by C, and come up with the -- you multiply that by the average factor for the Jalmat Pool in 1982, which 12,000,259 per month and you come up with A, which is the fair share maximum for the month of June.

Now, these figures show that a factor of 1 would get a fair share allowable, or fair share factor, of 3,000, 922 for an acreage factor of 1.

If you went up to a 640-acre unit, that figure would be increased to 15,668; a 40-acre well would get 981.

This is the application of the formula.

Q Now, Mr. Nutter, in an effort to bring this all together, could you briefly summarize for the Commission how Mr. Hartman's proposal can be implemented?

A Yes. One, all southeast prorated wells would be classified as marginal.

Two, each gas purchaser to implement any necessary production cutbacks by as equally as is practicable restricting on a time basis each prorated well access to that purchaser's gathering system.

Three, any southeast prorated well that is truly nonmarginal and which has sufficient excess producing capacity shall be further restricted in its production by being assigned a monthly fair -- a maximum fair share factor, which shall be calculated by the formula set out in Exhibit Number 26, Entitled Formula for Calcula-

tion of production ceiling.

Four, for a given prorated well each pipeline purchaser is to balance out with all other wells in the pool over a specified period of time access that the well has to the pipeline sytem. The ultimate responsibility for policing the actual time access to the pipeline system shall be left to each individual operator.

Q Mr. Nutter, will you now refer to Exhibits Twenty-nine and Thirty and review those for the Commission. There is no Exhibit Number Twenty-eight.

A You will recall that in the previous testimony I was discussing the hypothetical case where you had a 5-well prorated pool and the normal conditions, market demand was 1000 Mcf per day. Well No. 1 would make 450 Mcf a day; Well No. 2, 250; No. 3, 148 -- 140,000; Well No. 4, 128; and Well No. 5 would make 32.

Now, under the proposal by El Paso all of those wells would have been reclassified as nonmarginal and -- except No. 5, and they would have all been cut back to 117 Mcf.

Well No. 1 would lose 333 Mcf, or 74 percent of its previous production, based on a 50 percent cut in nominations.

Well No. 2 would lose 133 Mcf, or 53 percent.

Well No. 3 would lose 23 Mcf, or 16 percent.

Well No. 4 would lose 11 Mcf, or 8.5 percent.

Well No. 5 would stay the same with no loss.

That's depicted on Exhibit Number Twenty-nine.

Exhibit Number Thirty is a depiction of the same market situation where normally the wells were producing 1000 Mcf, where the pool and market went down 50 percent.

Under the Hartman proposal of limiting access to the pipelines by 50 percent, Well No. 1 would lose 50 percent of its production. Well No. 2 would lose 50 percent of its production; Well No. 3, 50 percent; and No. 4 and 5 would also lose 50 percent.

This is a depiction of the figures that I was trying to read into the record in the previous testimony, I think I didn't do a very good job of. I thought it would be clearer if I showed them in black and white.

We feel that case one of Attachment B, or Exhibit Number Thirty is a fairer and more equitable distribution of the depressed market that we have today than case -- that Exhibit Number Twenty-nine is.

Q Mr. Nutter, in your opinion, would granting the application of Mr. Hartman be in the best interest of conservation, the prevention of waste, and the

protection of correlative rights?

A I certainly think it would. Previous testimony indicated that this would result in a violation of correlative rights, the application of the El Paso formula.

Also, the testimony showed that you would have situations in which waste would actually occur as a result of the El Paso formula.

So I believe that this does protect correlative rights. It cuts everybody back equally. It's in the interest of the protection of correlative rights. The New Mexico Supreme Court has held that the protection of correlative rights is a necessary adjunct to the prevention of waste; therefor, I think it would also prevent waste.

Q Mr. Nutter, if Mr. Hartman's application is granted, does Mr. Hartman have staff available to work with the Commission in implementing the plan?

A I would like to stress that if the Hartman plan should be adopted, we would be most happy to work with Mr. Garcia and any other of the Commission or the Commission staff to implement the actual mechanics of this, and also to participate in any further hearing if it was found necessary in order to adopt the actual procedures.

Q In your opinion is it a proposal which can be practicably implemented by this Commission?

A Well, I certainly believe so. My little mini-proration schedule here was not worked on Harold Garcia's big computer; it was worked on my little pocket

culator, and if I can do it here for six wells, he could do it for 1200 wells with his big computer.

Q Mr. Nutter, were Exhibits Twenty-three through Twenty-seven and Twenty-nine and Thirty prepared by you or for you under your direction and supervision?

A Yes, they were.

MR. CARR: At this time, Mr. Ramey, we would offer into evidence Hartman Exhibits Twenty-three through Twenty-seven, Twenty-nine and Thirty.

MR. RAMEY: Hartman Exhibits Twenty-three through Twenty-seven, Twenty-nine and Thirty, will be admitted.

MR. CARR: We would tender Mr. Nutter for cross examination.

MR. RAMEY: Any questions of the witness? Mr. Kellahin.

MR. KELLAHIN: Thank you, Mr. Chairman.

CROSS EXAMINATION

BY MR. KELLAHIN:

Q Mr. Nutter, when was gas prorationing established in southeastern New Mexico, do you recall approximately when?

A Yes, 1954 was the original implementation of it. One of my exhibits showed -- well, Exhibit Number --

Exhibit Number One shows the annual production for each pool in southeast New Mexico, commencing with the year of the institution in that pool. It ranges anywhere from 1954 to 1974, I believe.

Q Since that period when prorationing was established in southeastern New Mexico, has the Division continued to use a method of well classification that included a category for marginal wells?

A Oh, yes.

Q What is your understanding of the definition of a marginal well?

A A marginal well, under the definition of the rules, the gas proration rules as set forth in Order No. R-1670, as amended, states that any well, which in a three-d23th period its best production is not equal to its average allowable, is automatically classified as marginal.

Q Once a well is classified as a marginal well, what is that well allowed to do in terms of its capacity to produce?

A It's permitted to produce at capacity, theoretically.

Q That well, then, if it's classified as a marginal well, is not restricted or curtailed in its production in the implementation of the proration formula.

A That is correct. As we pointed out, 95 percent of the prorated wells in southeast New Mexico are currently classified as marginal, and theoretically

operating at capacity.

Q What is your understanding of the reason that the Division has historically used a category of marginal well classification?

A I really wouldn't know why a marginal and nonmarginal classification was originally set up. I presume that it was to separate the good wells from the bad wells and to allow the bad wells to produce 100 percent of the time and to allow the pipelines to swing on the good wells.

Q Are you aware of any conservation reason why you would want a low capacity, low volume, marginal wells to produce at their full capacity?

A Oh, some of them there might be some reason; others, there's no reason why they should produce at capacity at all times.

Q Well, would not allowing those marginal wells to produce at capacity prolong the economic life of those marginal wells?

A Allowing any well to produce at its capacity at the end of its life is going to prolong the life of the well.

Q And that would avoid the premature abandonment of marginal wells and avoid losing gas that would otherwise be recoverable from the reservoir, would it not?

A If you averted the premature abandonment of wells, you would probably avert a certain amount of waste, yes.

Q And that concept has been used by the Commission since 1954 in giving special consideration, then, to marginal wells so that they're allowed to produce at their capacity.

A They normally have been permitted to produce at capacity; however, under current conditions it's been testified they're not being permitted to produce at capacity any longer.

Q I understand.

A They're being restricted.

Q El Paso, in fact, is restricting those wells, is that correct?

A I believe, so, yes.

Q Now, if I understand Mr. Hartman's proposal, he would take wells that are now currently classified as nonmarginal, those wells that have a high capacity, and reclassify them as marginal wells. In other words, all wells are going to be classified as marginal.

A We've proposed that 5 percent of the wells that are currently classified as nonmarginal would be classified with the other 95 percent that are currently marginal; therefor, you would have 100 percent marginal wells.

Q He would, therefor, eliminate this distinction that the Division has historically made between marginal and nonmarginal wells.

A Yes, to this extent: That marginal wells have never by the Commission been mandated to produce at 100

percent of their capacity. It's a classification by the Commission and there's been no legal requirement under the rules and regulations of the Commission that those wells would be classified -- would be produced at 100 percent of the time.

It may be a pipeline policy, as we've heard it here at this hearing, to produce marginal wells 100 percent of the time. In that event, what you say may be true, that historically those wells have been permitted to produce 100 percent of the time, but the classification, or the reclassification as proposed by Mr. Hartman would not change that in that the pipelines currently are restricting marginal production.

Q Let's look at Mr. Hartman's Exhibit Number Thirty, Mr. Nutter. What you have graphically demonstrated here, Mr. Nutter, is what Mr. Hartman's proposal is to do with regards to the implementation of the allocation or prorationing schedule in a situation where you have a depressed market.

If I understood you correctly, he would propose that the curtailment percentage using your formula is going to be apportioned among all wells by the same percentage.

A That is correct.

Q So when we get down to a well at the far right, a 32 Mcf per day well, now that well currently under the existing practice of the Division would be classified as

a marginal well.

A That well is classified as a marginal well right now.

Q Are you aware of how many wells in the Jalmat currently produce 33 Mcf per day, or less?

A No, I haven't made that calculation.

Q All right, but a well, that, in fact, makes that is a marginal well?

A I believe that I could give you some figure on that. Exhibit Number Twelve was a tabulation of the wells that would remain as marginal wells under El Paso's proposal, and I believe, you may recall that I had gone through December, November, January, production to find wells that would not make a million a month, and then to give them -- if I couldn't find them in those three months, including December, which was the best month of that three month period, then I went to February and March, also, looking for wells that would make a million, and in the Jalmat Pool I found that there were 80 wells, 80.42 acreage factors, which doesn't necessarily mean 80.42 wells, 80.42 acreage factors that would remain marginal under El Paso's scheme.

Q So of those 80+ acreage factors, under existing procedures those wells would not be curtailed. They currently are allowed to --

A I don't know if El Paso is currently producing those wells 100 percent of the time or not. Under

their proposal, you'll recall their original proposal was to reclassify all wells as nonmarginal, and then they amended their proposal later, to say, well, we'll leave wells as nonmarginal that will make a million a month, leave wells marginal, but their proposal originally was to reclassify all wells as nonmarginal, in which case all wells would have been curtailed, and I'm not sure they're not curtailing those wells at this time.

Q Under the examples demonstrated on Exhibit Number Thirty, when we look at a well that produces 32 Mcf per day, under the method of curtailment proposed by Mr. Hartman those wells that were previously allowed to produce at capacity are going to be restricted in the same ratio as all nonmarginal wells are going to be restricted.

A This is correct. All production would share the depressed market.

Q For those wells, then, if it's a 50 percent curtailment, that well will obviously be divided in half and allowed 16 Mcf.

A That is correct.

Q Have you made any determination or study, Mr. Nutter, as to what the adverse impact would be on those marginal wells within those proration units?

A No, I haven't, but when market conditions get such that certain wells can't be produced, maybe they ought to be shut-in and temporarily abandoned until market conditions get better.

I don't think you can tailor the whole market to 1500 wells to half a dozen wells that are down on the fringes of economic abandonment, anyway. What we're trying to do, we're trying to protect correlative rights, which we have found to be a necessary adjunct to prevention of waste, and if it's going to cause some of these very low marginal wells to be shut-in for the time being, until market conditions improve, then so be it; it's just got to happen. You can't -- you can't keep wells on production forever. There comes a time when certain wells must be curtailed or even abandoned.

It's harsh fact of life, but that's the way it is with oil and gas wells.

Q You've talked about the protection of correlative rights, Mr. Nutter. How would a curtailment formula as you propose, that restricts marginal wells, protect the correlative rights of the operators of those marginal wells?

A Well, if he can't -- if he can't produce it economically, the protection of -- the correlative rights means your opportunity to produce your fair share, and if you can no longer produce your fair share because of economics, I don't think correlative rights can be tailored to your well necessarily.

Q Let's go back to your method of calculating this allocation formula, your fair share calculation. I guess it's Twenty-seven, or any of those that

show that --

A Yeah, it's --

Q -- formula.

A Yeah, it's on a number of those exhibits, Mr. Kellahin.

Q Yes, sir. Isn't the effect of what you have proposed here, Mr. Nutter, simply a recognition of deliverability as a factor in the allocation formula?

A It is to this extent, Mr. Kellahin. As I stated before, 95 percent of the wells in southeast New Mexico are currently classified as marginal. 95 percent of the wells that we started out talking about in this hearing.

We've now dismissed the Indian Basin, where the biggest part of the nonmarginal wells are, so now we're talking about maybe 97 or 98 percent of the wells are currently classified as marginal.

And if marginal wells are, in fact, as you were discussing awhile ago, permitted to produce at capacity, you're 98 percent on deliverability right now, and we're not proposing any great change in the -- in the application of any formula. If 98 percent are on deliverability, we put 100 percent on deliverability.

El Paso's program was going to reclassify 98 percent of the wells to nonmarginal and --

Q Well, I think we have some trouble with semantics here, Mr. Nutter. The deliverability you're talking about is tied to the marginal wells. That's an ex-

empt classification. In other words --

A Well, yeah, but the wells for practical purposes are producing on a deliverability basis because, as you stated, they're on the line 100 percent of the time, unless you have a depressed market like you've got today.

So they're on a deliverability delivery factor.

Q For the marginal wells.

A Yes, 98 percent of the wells we're talking about.

Q Under current provisions of Order No. R-1670, a deliverability factor is not permitted in the calculation for the allowble of the nonmarginal wells.

A No, they're all on straight acreage and our __

Q All right, and --

A -- maximum fair share factor is -- which would be the controlling factor on this mini-proration schedule -- is a straight acreage factor.

Q Under your proposal, for the first time, then, there will be deliverability as a portion of the calculation of the allowable for the nonmarginal wells.

A No. No, deliverability doesn't enter into the calculation. A time share basis enters into the calculation. We're saying that if the pipelines say that the market demand is 65 percent of what it was last year, we'll put the wells on the line 65 percent of the time.

empt classification. In other words --

A Well, yeah, but the wells for practical purposes are producing on a deliverability basis because, as you stated, they're on the line 100 percent of the time, unless you have a depressed market like you've got today.

So they're on a deliverability delivery factor.

Q For the marginal wells.

A Yes, 98 percent of the wells we're talking about.

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Q Now, the time share concept is nothing more than a different phrase for deliverability, isn't it, Mr. Nutter?

A It's access to pipeline facilities, is what it is.

Q And whatever that well will produce on that day.

A It's access to pipeline facilities.

Q At its capacity at that day.

A On that day.

Q Yes, sir, so that, in fact, is a deliverability.

A Which is what the wells are doing now, they're on -- 98 percent of the wells are marginal and that's what they're doing now.

Q Yes, sir.

A They're on pipeline delivery basis.

Q Yes, sir, but not for the nonmarginal wells.

A Well, the 2 percent that are still nonmarginal, right.

Q That's right, and for the first time, then, we are going to have a system that includes deliverability for the nonmarginal wells.

A No, it won't, because there won't be any nonmarginal wells.

Q That's a point. Let me ask you what happens under your proposal with regards to the fair share allowable for what I will characterize as a well that's not going to be able to produce that fair share allowable. There was a Conoco well under your mini --

A Right.

Q -- proration schedule.

A Right.

Q One of those Conoco wells, you said, is not going to make its fair share allowable.

A Well, there are two wells on the unit.

Q Yeah, it's not important which ones they are, but there is a type of well that can't make the fair share allowable.

A That is correct.

Q What happens under your proposal to that underproduction, the difference between what the well will make and the fair share allowable?

A The same thing that's happening now.

Q There'd be no change in it.

A There'd be no change in that well's status. That well is -- that unit is not carrying any underproduction because it's classified as marginal. There would be no change in that unit whatsoever.

This is -- this number here, if you'll look at Exhibit Number Twenty-five, for the month of January, you'll see that that Conoco Vaughn B-1 Unit has a

maximum fair share factor for an acreage factor of 2 of 33,000. The well averaged 8,400 in the year 1982.

Now, that well -- that unit was restricted at certain times. I think you'll come down here on our proration schedule and you'll see in the month of December, when the market was pretty good, last December, the well -- the unit made 19,000, which was twice what it made for an average in 1982.

Q I'm not interested in specific numbers, Mr. Nutter --

A Yes, but --

Q I want to have you explain the concept --

A Right.

Q -- of how this works for me.

A The maximum allowable that that well could produce, if it were capable of doing it, in January of 1983 would have been 33,000.

The wells can't make 33,000, I don't believe, so --

Q Let me ask you a question.

A So it's not accumulating any underproduction now; it wouldn't accumulate any underproduction under our proposal.

Q All right. Under current prorationing methods a well that is a marginal well producing at capacity cannot make that allowable assigned to it and it would generate an underproduction. What happens to the underpro-

duction.

Q All right, sir. What happens to those wells that I'll call marginal under your calculation of the fair share allowable? There is a gap there in which it cannot produce enough to meet its fair share.

A If it's due to pipeline curtailment beyond the professed demand for that month, then the producer has a case against the pipeline.

Say that the pipeline deliverability, or the pipeline access, is determined to be 65 percent for a month, average pipeline access, and the pipeline produces the well only 25 percent of the time. If, over a period of time, you said -- you'll recall that we would require the pipelines to balance out with producers over a period of time, and if the pipeline has not balanced out with that producer, then there'd be a case between the producer and the pipeline. Why haven't you produced my well? Over here across the line I see that you've overproduced my neighbor's well, and it's a matter between the pipelines and between the producers, which is the way it is right now with marginal production. The marginal production -- the Commission doesn't do anything to protect the producer with marginal wells at this time. He's on his own, and the producer would continue to be on his own to protect his wells and see that the pipeline takes his production. He's going to have to get a hotline to the pipeline office, maybe.

MR. KELLAHIN: Thank you, Mr.

Chairman, I have nothing further.

MR. RAMEY: Any other questions of Mr. Nutter? Mr. Nance.

MR. NANCE: Mr. Chairman, first of all, I wondered if we might appropriately ask a few questions relating to Mr. Nutter's earlier testimony during -- his direct testimony during the June portion of the hearing?

MR. NUTTER: I don't remember what I said then, so --

MR. NANCE: Well, I'll try to remind you.

MR. NUTTER: I'm sure you will.

CROSS EXAMINATION

BY MR. NANCE:

Q Mr. Nutter, in your being qualified as an expert witness in petroleum engineering, prorationing matters, and also regulatory matters, by your attorney, Mr. Carr, you indicated many years of experience with the New Mexico Oil Conservation Commission and the Oil Conservation Division, is that correct?

A That is correct.

Q In all those years with the -- either the NMOCC or the OCD have you ever proposed such a formula for protecting gas or for prorating gas in any pool in New Mexico as what you are proposing in this particular case?

A No, there's never been a case like this brought before the Commission before.

Q Okay, thank you.

You discussed what can be done to ease the present burden on gas producers in New Mexico, and you suggested that the answer would be to reduce takes ratably, and that's what you are continuing --

A That's the basis of our case.

Q -- to propose this morning.

A Ratable reduction.

Q Could you tell me if another solution would be to permit every producer an equal part of over-production in making making market demand?

A Every producer? No, because every producer doesn't even have the same number of wells.

Q Shall we say an equal -- a portion equal to that producer's interests?

A No, I don't think so. Why should a producer that has ten wells that will make 100 Mcf total get the same amount of production into the pipeline that a producer that has ten wells that will make 1000 Mcf?

Q All right.

A In other words, if you're going to put it on a per well basis -- if every producer had wells, the same number of wells, that every other producer has, and every producer's wells were of equal capacity, then all producers should be cut equally.

Q All right.

A But it has to be all on an equal ratable basis.

Q Okay, assuming, however, that you were using a 100 percent acreage allocation formula, what would your answer be then?

A Well, the maximum acreage -- maximum fair share factors here consider acreage. They consider nominations and previous acreage factors, or top allowable factors, times current or present nominations and acreage factors, and so the wells would have a maximum fair share based on acreage. There's no departure from acreage in this formula that we're proposing.

Q All right, and as far as the existing rules are concerned in the Jalmat Gas Pool, for example, is it not true that each well in the Jalmat is allowed a portion of the market demand according to that well's acres, or acreage factors, and the relationship that that acreage factor -- that those acres then bear to the total acres in the pool?

A No. No, that's not true, because -- because --

Q Are you talking about current rules?

A Yes. Because in the Jalmat Pool we have a total of 355.94 total acreage factors. Of those only 6.25 are nonmarginal, so 349.69 out of 355.94 are marginal factors. So they don't have access solely on the basis of

acreage. They have access on the basis of their deliverability into the pipeline, their marginal wells.

So they're not operated solely on acreage.

Q Now, the distinction you're talking about then, is between nonmarginal and marginal, if all wells were classified as marginal, then the access to the market would be strictly on the basis of 100 percent acreage?

A No, no, it's just the opposite, if they were all nonmarginal would be on the basis of 100 percent acreage. If they're marginal it's on the basis of deliverability, if you will.

Q What is the reason for classification of wells as marginal?

A They can't make the allowable.

Q All right. Let me take you through an example, if we might.

Assume that we have a new pool and that we start proration for that pool on a well by well basis, using 100 percent acreage factor as the basis for the calculation of allowables, could you describe how that would work on a well by well basis?

A Well, normally the way it would always work would be you'd have nominations totaling, say, 1000, you'd have five wells that come in in the pool. You'd divide the -- and they're all of equal capacity -- divide 5000 by 5 and give each one 200.

And then as marginal production develops, this is under the current system --

Q All right.

A As marginal production -- as marginal wells develop they're permitted to produce, if they can't make that 200, they're permitted to produce what they can and the balance is divided among the remaining four wells, if one of them goes marginal.

Q Okay. Is this not the historical basis for the proration scheme that has been in effect --

A Yes, this is the way it was adopted in southeast New Mexico and has been until -- until now.

Q Okay, do you know how long this type of calculation has been in effect for the -- well, for the Jalmat Pool, for example?

A Yes, since 1954 in the Jalmat. As I stated to Mr. Kellahin, it's anywhere from '54 to '74 that this gas prorationing was implemented in various pools.

Q All right. Would you say that if wells were properly classified in the Jalmat Pool, as an example, as between marginal and nonmarginal, given the existing rules that the proration scheme would be on an equitable basis, protecting correlative rights, preventing waste?

A It would be if you had flush production. This worked fine when these pools were better pools, but as you'll recall from Exhibit Number One, everyone of these pools has declined. There's only two of these fifteen pools

that's making as much as 50 percent of its maximum production. It ranges from 74 percent down to only 2 percent of its previous high.

So many of these pools are at advanced state of depletion here and a straight acreage formula just isn't that applicable any more as it once was, because so many of the wells have gone marginal and the reclassification now to nonmarginal of everything above this is kind of farfetched, as was shown by another witness in the previous hearing on this matter, the classification as nonmarginal and the curtailment of some of these wells is going to cause gas to migrate from one well to the other. Violations of correlative rights will occur. Subsequent waste will follow, and it just isn't practical in an advanced state of depletion to classify everything as nonmarginal.

Q Could you tell me, does flush production, which you described as what would be required for these -- for these rules to work, does flush production become the factor that requires proration, or is proration needed because market demand is less than producing ability in a gas pool?

A Well, under normal conditions you would expect the market to be able to support wells that -- and support allowables that are fairly realistic, but when we have a depressed market like we have today, those allowables do not become realistic, and what might have been proper for

classification of wells as nonmarginal in previous days is no longer proper. It's hard to say just what flush production is, but it's -- it's good production. It's not stripper production. We're talking about an awful lot of wells that are approaching or are in almost a stripper state.

Q Wouldn't it make sense, then, if the market is at an unrealistically low -- or an unusually low level, that allowables should also be set at a correspondingly low level?

A That's probably right, if it's done on a ratable basis, but not on a non-ratable basis, and we don't feel that the El Paso was ratable, because it's taking away so much from some wells and not taking away anything from other wells, as Exhibits Numbers Twenty-nine and Thirty show.

Here we had this well that was making 450 under the 1000 Mcf per day market and it's cut by 74 percent, and one of these other wells that was become nonmarginal under your proposal is only cut 8.5 percent.

We don't feel this is ratable. We feel that a ratable reduction of market should apply to these, and that all of them should share in this depressed market.

It's unreasonable to expect just a few to bear the burden and the other wells to take the free ride, so to speak.

Q However, the way that the rules are cur-

rently stated, and the rules that have been established by the Commission up to this point on the basis of what the Commission saw as reasonable evidence, said that 100 percent acreage is the appropriate basis for allocating production among wells during periods of proration, is that not correct?

A That is correct, under the existing rule, acreage is the only method that's used to divide the allowable among the wells that can't make -- that can make their allowable.

Marginal wells are not subject to that acreage factor, exept the acreage factor and the assigned allowable are what determine whether the well is classified as marginal.

But under the rules, a well is supposed to come back as nonmarginal if it can make the allowable and you all haven't been willing to wait for the wells to come back to nonmarginal. You come in here and you say let's classify everything down to 1-million as nonmarginal. You haven't waited for the thing to work.

It used to be that wells were reclassified on a more frequent basis back to nonmarginal and El Paso is the one that asked for the rules to be changed to wait one full year before you could get back into a nonmarginal status. El Paso's the one that asked for that change.

Q When was this?

A Oh, I don't remember when. It's a number of years back that that rule was changed, but it was on the application of El Paso.

Q During a significantly different market situation.

A Right, that's right. That's when you wanted to keep things marginal. Now you want to get things nonmarginal.

Q I'd like, if we might, to go back to your Exhibit Number Twenty-five, which you introduced this morning.

A Okay, that's the mini-proration schedule?

Q That's correct, and if you wouldn't mind, please, explaining again, because we, as you started your explanation this morning we hadn't yet gotten copies of the exhibit and it's a little difficult for us to follow the calculation that you've made --

A Okay.

Q -- for determining the difference between what you indicate here as an example as the January fair share and the maximum fair share --

A Okay.

Q -- considering the acreage factor.

A Okay.

Q If you could go through that.

A Okay. Now nominations are not on that; however, we'll take just the month of January, it's the top

of the first page of Exhibit Number Twenty-five.

Now, the average adjusted nominations for this pool in 1982 were 1,044,500.

Q That's the average nominations.

A The average adjusted nominations in 1982.

Q All right.

A The nominations for the month of January totaled 1,409,100. These are rounded off to even 100's.

Now, if you divide the January nominations by the 1982 adjusted nominations, you'll find that the January, 1983 nominations were 134.91 percent of the average adjusted nominations for 1982.

Now --

Q Now, when you say adjust nominations, you're talking about nominations that were made for the month of January and then subsequently --

A No, I'm talking --

Q -- adjusted?

A No, the adjusted nominations were the nominations for each month in 1982 as they were adjusted for underproduction, overproduction, and so forth, in the pool.

Q And that was an adjustment that was made two months or so subsequent to January, is that correct?

A No, no. No, we're not talking about January right now. We're talking about -- the adjusted nominations are the 1982 nominations.

So those totaled 1,044,500.

Q Okay, that's the same figure, then, that you used for all of these months calculations.

A That's correct. That figure enters into everyone of these months.

Now, the individual month's nominations differs for each one of these six months on this mini-proration schedule.

Q Right.

A For the month of January they were 1,409,100. Then I went to each one of these wells that's on the mini-proration schedule and I averaged what its production was for the year 1982, what its average monthly production was.

The Alpha Twenty-one averaged 5,240 Mcf per month.

Q The entire year of '82.

A For the entire year of '82. The Shipley averaged 8.028, and so on.

All right, then you take the ratio of January's nominations to 1982 average adjusted nominations, that 134.91 percent, and you apply that to the 1982 production, and you get fair share based on production and current nominations.

The Alpha Twenty-one, its fair share based on production only, would be 7,069 Mcf.

Now, this is a guide. This would give

the pipeline a guide, and also the producer, as to what he might expect that well to produce during the month of January if 1982 was a typical year's production for the well. Probably isn't. Some of them were curtailed. Some were curtailed more than others.

Q Right.

A Some of them -- in calculating this I found some wells that had zero month's production for two or three months. Others, there was a normal decline in production. So this is not a firm figure at all. This is a tentative guide, this January fair share based on that.

Then you take that same ratio of 1044.5 to 1409, you multiply that times the top unit allowable for 1982, which isn't on here, it's on one of these other exhibits, and for the Jalmat Gas Pool a factor of 1 had 12,259 Mcf average monthly top allowable production.

So you take this ratio of January nominations to '82 adjusted nominations, multiply that by -- times that 12,259 Mcf that was the average top unit allowable for the Jalmat in 1982, times an individual well's acreage factor, which is .5, and you come up with the 7069 for this Alpha Twenty-one Well.

That's its maximum fair share.

Q And all wells, for example, in this pool that have the same acreage factors, for example .5, would have this same top fair share?

A That is correct. You'll see the number

repeated for two wells there. I read that number wrong. I said 7069. I meant 8269. I read the wrong column.

Q Yes.

A But you'll notice that the Shipley Well, which is a nonmarginal well at the present time, of course it's shown here as being marginal, the M over on the left side, but it currently is a nonmarginal well, but it has a maximum fair share of 16,539.

The little Gulf well down here, which is a small marginal well, has an acreage factor of 1, it has a maximum fair share also of 16,539.

If that well could be reworked and its productivity increased, it could produce up to the 16,539.

Now the monthly, in all these months, the monthly nominations are calculated in against the average nominations for 1982, and the average top unit allowable factor for 1982, to arrive at the maximum fair share, and as we stated before, under just applying production, that Hartman Bates Well calculates on production only an allowable of 13,287 for the month of January; however, its maximum fair share is only 12,403, so that would be held to the 12,403. That would be its fair share maximum and it couldn't produce more than that.

Q Is there any type of relationship at all between this maximum fair share that you are proposing here and the current situation with nonmarginal wells versus marginal wells?

Let me rephrase that, if I might.

What you anticipate is that very few, if any, wells would make that maximum fair share.

A That's right, very few of them are going to be subject to that, because take a look at the Gulf Well. It's got 16,539, yet in 1982 it only averaged 1608. I can tell you what its best month was in the year 1982, it wasn't very good. It's best month in the year 1982 was 2640, and that was at the beginning of the year; that was January of 1982. It did have some pretty badly curtailed months. It didn't produce anything in August and September and only 30 in October, but its average was 1608 for the year, so it's not a very good well and it's never, unless something is done with the well, it's never going to approach that 16,539 but if they'd rework the well and put -- and get substantial increase, that would be its maximum fair share ceiling.

Q Well, as things stand now, we have the majority of the wells being classified as marginal. If the market is sufficient and all of those marginal wells, essentially, are being allowed to produce, the only wells that are being cut back are the few, small -- or the small number of good producing wells at the top again that are nonmarginal wells --

A This is the way it was until --

Q -- and this is the way it is operated up through the present, essentially.

A Until -- until the pipeline conditions

got to the point you had to start curtailing those marginal wells.

Q All right, what I'm asking is if you would not have a similar situation again under your proposed scheme where only a handful of the very best wells up at the top end of the scale are going to be subject to this maximum fair share cutoff?

A No, no, because it's up to the pipelines to reduce them all ratably. They're going to produce all those wells ratably, and this, as I stated, the first column is the guide as to what the wells would produce if the '82 production were typical for that well. Now, we realize it's not, so the guide is going to be a flexible guide, but that would be the amount you more or less would expect from the wells; you wouldn't expect the maximum fair share, but they would all be curtailed on the basis of time access to pipeline facilities.

Q Well, the maximum fair share, though, you are stating, is a level beyond which a well could not produce without some type of penalty --

A No, no, this is the guide that the producer uses in going to the pipeline if he sees a well across the line producing in excess of that maximum fair share, he's got a case against the pipeline. You're producing my well at fifty percent; you're producing that well in excess of the maximum fair share, how come?

And the fair share is flexible for each

month. At the end of a year, or some period of time, the total maximum fair shares will be calculated, the production would be shown, and any operator could tell whether another producer was getting an advantage over him or not by the production.

Q Now, overall the role of the Commission in a scheme that you're proposing becomes a much more passive, is that correct?

A It's the same as it is currently for 98 percent of the wells, listing the production and listing -- they call it now an allowable for marginal wells. It's not an allowable, as I stated before, because if a well doesn't produce one month -- the marginal allowable is always shown to be the production from two months back in a proration schedule. All right, if a well didn't produce anything two months back it shows zero allowable this month. That doesn't mean that the well can't produce gas if it's a marginal well.

So allowable is a misnomer there. But it's, what the Commission does at the present time for marginal production, it reports its production.

Now, the Commission would be less passive than that because they're giving guidelines here now; maybe zero production, or maybe showing production for marginal wells is a guideline. In that case they would be the same amount of passivity that they are now.

But they really don't do anything about

marginal wells at the current time, and they wouldn't be doing anything about marginal wells in the future.

Q And what your proposal is then, is to correct -- well, let me -- let me ask again.

Do you see the problem as being one where only those 2 percent of the wells, then, are treated unfairly, and that correcting the situation as far as those 2 percent of the wells is concerned, then it will solve the overall problem? Is that what your proposal is?

A No, no. Our proposal is not to correct the problem for 2 percent of the wells. Our proposal is to correct the problem for 98 percent of the wells, becaue you all filed the first application and you wanted to make everything nonmarginal. That, to us, was the problem. We didn't see any problem the way things were, but when you all filed your application to classify everything as nonmarginal we saw a problem developing then.

So we're not complaining about the 2 percent right now. We're complaining about your proposed 100 percent.

Q Is it essentially true that what you are asking for is to do away with proration rules as they currently exist?

A No more than your case is.

Q But would you say that El Paso's proposal is one to reinstate existing proration rules?

A No, I don't think so. I don't think it

is.

Q Where they are not working because of the market situation?

A No, I don't think you're reinstating the rules here. You're modifying the rules by reclassifying marginal production as nonmarginal.

Q And what is the impact of your proposal on the existing rules?

A You're reclassifying 98 percent; we're reclassifying 2 percent.

Q And your reclassification of that 2 percent leaves what effect as far as the rules are concerned?

A Everything marginal.

Q And the rules, then, are -- are able to operate how?

A The burden is made clear to the producer and to the pipeline that it's up to them to ratably produce the wells subject to the market demand.

Q And the Commission's enforcement, then, becomes one merely of responding to complaints between producers and pipelines.

A I would think so.

Q And not of establishing specific guidelines for the pipelines and producers to follow.

A We had our specific guidelines, which I read into the record, points one, two, three, and four.

Q Would you mind repeating those so that we

might be sure that we have them down correctly.

A Okay. One, all southeast prorated wells be classified as marginal.

Two, each gas purchaser to implement any necessary production cutbacks by, as equally as practicable, restricting on a time basis each prorated well's access to that purchaser's gathering system.

Three, any southeast prorted well that is truly nonmarginal, which has excess producing capacity, shall be further restricted in its production by being assigned a monthly production ceiling, which shall be calculated by the formula.

I won't go into the formula again.

Four, for a given prorated well each pipeline purchaser to balance out with all other wells in the pool over a specified period of time the access that that well has to the pipeline system.

The ultimate responsibility for policing the actual time access to the pipeline shall be left to each individual operator.

Q What you're saying is that the operator, then, has the responsibility for making sure that that's the case and he is the one who needs to monitor the production of his -- of his offset property.

A And his own, also. He's got to monitor his own production. He's got to monitor his pipeline. He's got to keep an eye on his neighbor's production, and any

wise operator that's one of these 98 percent marginal wells today is doing that.

Q And what should the extent of the Commission's involvement be?

A The Commission's involvement is the same as it is now for marginal wells, and also establishing the maximum fair share allocations.

Q But as you see it, that maximum fair share has not a great practical effect.

A It wouldn't to some wells; it would to other wells. It's a maximum that is there and up to the pipeline and the producers to observe.

Q But as long as wells were cut back on a ratable time basis, then you don't see that --

A I don't see it as being a problem, right. That's right.

MR. NUTTER: Mr. Chairman, may I get a drink of water?

MR. NANCE: We could break right now. We only have a couple more questions.

(Thereupon a recess was taken.)

MR. RAMEY: The hearing will come to order.

Mr. Nance, you may proceed.

Q Mr. Nutter, one final explanation. I

wondered if you could -- could go through an example.

Let us assume, as I have mentioned before, that we are starting proration in a new field with a 100 percent acreage allocation formula and a situation of increasing market demand to start with.

What could you -- will you agree that as wells are added and as market demand increases, under a 100 percent acreage allocation formula, that all wells would be allowed to produce up to a certain level, say, a level of 1, before any well was allowed to produce to a level of 2?

A Well, I think I understand what you're saying, and I think the answer is yes.

Q All right. Still the increasing market demand, still the increasing production, you have wells that have gone to a level of 2 and some wells have not been able to reach that level of 2.

A Okay, those become the marginal wells.

Q Those become the marginal wells. The same situation applies as market demand increases and wells are allowed to produce up to a level of 3, there are those wells which cannot make that level, they in turn become marginal wells, and ones that can produce 3 are allowed to produce 3, and so on, is that correct?

A That's historically the way this has worked.

Q Then you have a peak in demand, for example, and demand begins to decrease. With a 100 percent

allocation formula, what type of cutback in production do you have? Describe that, please.

A Well, I don't know what kind of a cutback in production you've got. I don't know.

Q Can you describe the mechanism? Are all wells that are top producers cut back to a certain level of production before wells that are on a lower level of production are cut back at all under a 100 percent acreage allocation formula?

A Under Commission rules the top allowable wells would be reduced and under Commission rules, I don't know, the marginal wells may or may not be. It's apparently some pipeline policy that they wouldn't affect the marginal wells, although that's not a provision of Order R-1670, but theoretically, the nonmarginal wells, the top allowable for the nonmarginal wells would be lowered as the market is depressed. The marginal wells, theoretically, would be producing at 100 capacity; the nonmarginal wells producing less. And then as the allowables came down, the mechanics of reclassification would work and some of those marginal wells would be reclassified as nonmarginal.

Q All right, correct. The other point that I would like you to discuss, if you would, just briefly, is to define what you mean as ratable taking among wells in a pool.

A As I mentioned in the testimony the first time around, ratable does not mean equal. Ratable means

proportionate. This is a basic legal definition of ratable and ratable taking means that wells are going to share in -- ratable, the legal definition of ratable is that various components share on a non-equal but a proportionate basis, and that's what the wells are doing at this time, they're sharing the total market on a proportionate basis. 98 percent of the wells are sharing this market on a basis of their capacity to deliver into the pipeline.

Now, the pipeline demand is going on. We're proposing that they continue to produce on a proportionate share and that the reductions would be proportionate.

And we'll say the market is depressed by 50 percent, as shown on Exhibit Twenty-nine and Thirty. The reduction is on an equal basis percentagewise, but it's on a ratable basis volumewise. It's proportionate to their capacity to produce under the Case 1 as compared to Case 2 on Exhibit Number Thirty.

Now, --

Q Are you equating --

A -- Exhibit Twenty-nine, nothing here is ratable. Nothing here is proportionate.

Exhibit Number Thirty is proportionate or ratable.

Q Would you not say that on your Exhibit Twenty-nine it certainly is something proportionate among all of the wells 1 through 4 if they have -- if they all

have the same acreage factor?

A Yeah, the acreage factor is the same but the allowable is not a ratable allowable. The allowable is an equal allowable.

Q If we are talking about 100 percent acreage allocation as the basis for establishing the allowable as ratable and not equal.

A The acreage factors are equal. The acreage factors are equal.

Q Then therefor, the allowables also should be equal.

A The top allowable would be equal but we're not talking -- this -- this is an extreme case here where market demand has been cut in half, and rather than allow wells to assume their classic reclassification position, we're trying to hasten things by saying let's classify everything down to nonmarginal; put everything on an equal footing here, and we're not allowing the system to work.

So what we're proposing would simply say instead of reclassifying everything as nonmarginal, let's classify everything as marginal and have ratable reductions during this depressed market.

We're not asking for this to be a permanent thing. The application was until further order of the Commission. If this doesn't work, or if the market demand improved in the next few years, it won't make any differ-

ence. We think this is an extreme market situation right now and where you asked me before had a case like this ever come -- had I ever testified in a case, had I heard of a case like this, no, I haven't, because I haven't seen the market like it is today, and I haven't seen a pipeline come in before, except in February when they asked that everything be classified as nonmarginal. It's never happened before, so I guess we've never had a market like this before.

Q But as far as you can see, ratable means --

A Ratable means proportionate to me.

Q -- proportionate to deliverability?

A The wells today are taking a proportionate share of the market, the 98 percent marginal wells are taking a proportionate share of the market.

Q Because the rules are not operating on those wells.

A Well, the rules have operated on the wells to the extent that they were classified as marginal wells, and now they're sharing a proportionate market and while the rules say acreage is the factor, the practicality dictates that deliverability is the factor for 98 percent of the wells today.

Q The practicality being the pipeline's interpretation of what seems to be appropriate?

A No, the -- no, the practicality of the

matter is that the wells are not permitted to make top allowable. They can't make top allowable, and so they're classified as marginal and they're delivering at capacity.

Now, I presume that you are cutting those wells back. I think Mr. Kendrick testified previously that you were cutting those wells back. So you're reducing the takes based on deliverability or some factor, I don't know what it is.

But the fact of the matter is that 98 percent of the wells are on a deliverability or pipeline capacity basis today under the allocation formula.

Q And your proposal is to make it 100 percent.

A Right, change the classification for two or three percent of the wells.

Q And to make deliverability, then, the basis for determining what is a ratable take?

A Up to a ceiling; up to a maximum ceiling; to a maximum fair share.

Q Do you not see this as a significant departure from the existing rules?

A No, I don't see it as a significant departure because you're reclassifying two percent of the wells and letting things operate just the way they are.

Q Where in actual operation, though, the 100 percent acreage allocation formula does not have any opportunity to operate.

A The 100 percent allocation based on acreage hasn't operated for the majority of the wells for years.

I think I had an exhibit going back to 1980, I believe it was; might not have gone back that far; no, I guess it didn't, that showed the number of marginal versus nonmarginal wells for years back, but it's been years since most of these pools had the majority of their wells classified as nonmarginal.

This only compared -- Exhibits Four and Five compared the number of marginal wells in the May proration schedule to the -- of '82, to the May schedule of '83 and 91 percent were marginal in '82; 95 percent are marginal in '83.

During a period of depressed market more wells became marginal. Explain that. It's because of the decline in productivity of the wells, not the decline in market. The decline in market should have made things nonmarginal.

Q If allowables were established.

A Well, allowables have been established but still more wells were becoming nonmarginal -- more wells were becoming marginal all the time when this market was going down. Just like I said, you had 91 percent of the total wells, or proration units, in 1982 were marginal. 95 percent are marginal in 1983.

Now, with the dismissal of the Indian

Basin Upper Penn this figure is going to be something like 98 percent. I don't know exactly how many. 33 percent of the wells in the Indian Basin were nonmarginal.

Q Mr. Nutter, thank you.

MR. NANCE: Mr. Chairman, we no further questions at this time.

MR. RAMEY: Mr. Stamets.

QUESTIONS BY MR. STAMETS:

Q Mr. Nutter, I may say you periodically in the cross examination, but certainly I mean Mr. Hartman since it's his application.

Why didn't you ask for de-proration of these pools?

A That would be a major departure from what we've got and we're not seeking a major departure. We're just seeking a minor departure by the reclassification of a handful of wells as marginal.

Q I'm not sure that I agree with that response but that's -- that's all right.

Let's talk about ratable in prorationing. It would seem, Mr. Nutter, that if we look at the appropriate statutes, being 70-2-16C, relative to prorationing, and 70-2-19D, relative to ratable take, that many of the factors that go into those are the same, except that I notice in 70-2-16C on prorationing it talks about the system and it says shall prevent drainage from producing

tracts in a pool which is not equalized by counter drainage. Now, I believe that once we examine these statutes, that that phrase is not common to the two; it applies only as far as prorationing goes.

How does the system that you propose here today act to prevent this drainage which is not offset by counter-drainage better than prorationing system and straight acreage as El Paso proposes to modify?

A Well, without getting into a dissertation on reserves and deliverability, I think it was shown by Mr. Aycock in the first hearing that there are variations in reserves under various tracts, and these reserves are reflected to a great extent by the deliverability of these wells on those tracts, and if wells are curtailed to a common level regardless of the reserves under the tract, that some of these wells are going to produce reserves from under their tract as well as under adjoining tracts, and this would result in drainage that is not conteracted by counter-drainage or offset by counter-drainage.

Q How many wells did Mr. Aycock look at?

A He looked at an area that just had three or four wells in it in the depth, but it's a common thing throughout the pool, where you have old wells and you have new wells being drilled, that you will have these variations in ability to produce and probably in reserves under the tracts.

Now, we know that -- we know that the

Jalmat case, the Supreme Court said that a prorationing formula is supposed to determine the reserves under each tract and determine the reserves under the entire pool, and that wells would be permitted to produce their fair share of those total reserves. The Supreme Court did not go on to say that when a well had produced its calculated fair share of reserves it had to be plugged and abandoned.

So I think that the Supreme Court probably recognized this is not in all cases feasible to determine exactly what the reserves are, so that you wouldn't have to plug wells that could still produce, but I don't know -- I don't know just how the application of the statutes in this case would apply.

It seems that reduction on takes or productivity of the well is at this time indicative of the reserves, probably, a great extent, anyway, and that reduction on a ratable basis would mean a recognition of a proportionate difference in reserves under the tracts.

Q Did Mr. Aycock look at a dozen wells?

A No, he didn't look at a dozen, I don't believe.

Q Less than a dozen?

A Yes.

Q How many wells are in these prorated pools, exclusive of the Indian Basin?

A Well, I can give you the total for all the pools and you'll have to subtract Indian Basin.

Q That was what, fifty wells, or so?

A No. In December of 1982 there were 1259 prorated gas wells in southeast New Mexico, and I don't know how many -- I don't know how many were marginal or how many were nonmarginal.

Q Indian Basin probably has fifty or sixty wells in it?

A Yeah, I can tell you exactly what it has. lYou kind of get into a difference sometimes when you look at these numbers. One place it says wells and in another place it says proration units, but Indian Basin in the May 1983 proration schedule had 54.6 total acreage factors. So we'll say, probably 55 wells, I think, somewhere in that neighborhood. And we had a total of 1259 prorated wells at the end of 1982.

So we had approximately 1200 wells outside of Indian Basin that we're talking about now, as opposed to 1980 nonprorated gas wells in southeast New Mexico.

Q Just for round figures, let's say at Mr. Aycock looked at twelve wells.

A Okay.

Q And there are 1200 wells.

A Yeah, 1 percent.

Q He's looked at 1 percent of the total wells?

A Yeah, as an example of what can happen

when you have nonratable take.

Q Okay, do you think looking at 1 percent of the total prorated wells is -- and looking at those only in one pool -- is sufficient number or sufficient sample upon which to draw a major conclusion that the straight acreage proration system that's been in effect for -- well, since 1954 is wrong everywhere and it should be superseded by a more or less deliverability type formula in all of these prorated pools?

A No, it's probably not the basis for making such a statement at all. A 1 percent analysis is not rally indicative of -- of conditions throughout the -- such a vast area as southeast New Mexico, but it was intended to show what can happen, not what was happening all over, but what can happen.

And I'm sure if there was time to do it and the facilities to do it, we could make a study of more wells than that and find similar conditions in more reservoirs than just the one that he studied.

Q Now, Mr. Nutter, under your proposed system, all wells -- well, let's say that the allowable was 50 percent at this point, or that nominations were 50 percent, and all wells would be shut-in half the time. What about those wells that are subject to damage when they're shut-in?

A That's one of those things that's going to have to be ironed out. It's just like today, you know,

we have operators come in -- we -- you have operators come in that all the time are saying don't curtail my well; it's going to be damaged, and he's got to prove this. Then if he can substantially prove that his well is going to be seriously damaged by being curtailed in any way, shape, or form, and his evidence is solid, he's been given an exception by you.

Q It seems to me, that under the current system, though, he does not get an allowable bonus. He doesn't get the authorization to produce more than his share of the allowable under those conditions. He gets to keep his well on but if he's overproduced eventually he'd have to shut it in.

A Well, most of the time these problem wells are -- are not capable of large amounts of production. Usually they're water wells, something like that.

Q That's certainly, true in the periods of high demand. It may or may not be true under periods of low demand.

A Well, I think that the Commission doors are always open for anybody that's got a problem with a well to come in and make his case, that his well should not be curtailed, but it's been that way and it should remain that way in the future.

Q Let's take a for instance. We have two wells and they're both producing at 50 percent. My well has water problems, so I come in to the Commission and I ask for

special dispensation to keep my well on every day, and this results in my producing half again as much as my neighbor, who's shut in half the time.

Assuming everything else is equal, isn't that going to mean I'm drawing some of my gas away from my neighbor?

A Yeah, but why is this different from what's going on today? We're not asking for any departure from the present rules in that regard.

Q In doing that, wouldn't the Commission be establishing a procedure which clearly is not even designed or intended to prevent this drainage which is not offset by counter-drainage?

A Well, what is -- what are the Commission's rules today that prohibit what you're talking about from happening today under the existing rules?

Q Well, I'm assuming, Mr. Nutter, that in essence what you're saying by this system that you're proposing, that we're authorizing prorationing by days on. That's the proration system.

A You establish a percentage of -- of '82 allowables that would be applicable and then this would be implemented by the pipeline on a days on/days off basis, yes.

Q But that in essence authorizes proration on days on/days off.

A I believe you're correct.

Q In our other, the existing system, we are prorating by volume, is that correct?

A Yeah, and you've got volume ceilings here.

Q Okay, but let's not confuse the two systems, so that if we have a problem well that is a non-marginal well, under our current system, where everything's on straight acreage and it's prorated on volume, if the Commission administratively authorized that well to be produced, eventually that well would become overproduced, is that right?

A Yeah.

Q Okay, and eventually that well would have to be shut-in.

A Yeah, and then the operator is going to be -- if it's a problem well, then the operator is going to be in your lap telling you about how he can't shut it in.

Q In any event, the system is designed to see that that operator doesn't get more than he's allowed.

A He would, yes, he would -- under the system if he had a nonmarginal well and it would get six times overproduced, he's supposed to curtail his production until he's less than six times overproduced.

Q Okay, if we go to prorationing on days on/days off, have a problem well, then after his ten days on that well's got to be shut-in or get an exception.

A Well, there's a period of time, now. Our proposal would be after a -- that they would balance out over a specified period of time. Now that period of time hasn't been set forth. I would imagine it would be either on a calendar year basis or on a proration year basis. I believe El Paso stated in their direct testimony that they were trying to take -- equalize takes between states, between pools, and between wells within a pool, on a one year basis. I believe that was correct.

And so over a period of time you'd balance these up, and perhaps this well would be producing in excess of some sort of a maximum fair share during a period of time, but then would be subject to the shut-in, just as it would acquire six times overproduced status if it were classified as nonmarginal, and then be subject to a period of shut-in.

So you're not changing that aspect of it at all. The well wouldn't produce ten days on and ten days off; ten days on and ten days off, necessarily.

Q Moving away from that subject, wouldn't it be possible under your proposed system that all wells or all proration units in a pool produced up to their maximum fair share?

A It's theoretically possible but I'm sure it's physically impossible. There's no way that you're going to be able to get all the wells to be able to make all that allowable.

Q So we are talking about an allowable which is the sum of all the fair shares.

A We're talking about an allowable that's really going to be in the vicinity of the first column --

Q On the --

A -- on the mini-proration schedule.

That's -- that's what you're really expecting to be produced; somewhere in that neighborhood; not the maximum fair share. The maximum fair share is going to be the maximum that the better wells are going to be subject to, but the wells that are presently marginal are probably going to be over here in this January fair share at 134.91 percent column.

Q But every proration unit would be assigned its maximum fair share allowable.

A That would be the maximum fair share it could not exceed, but it would take a vast amount of workovers to be able to get all the wells up to that capacity, and some wells you'ld never be able to get up to that capacity.

Q In essence, we'd be assigning an allowable which is greater than (inaudible).

A No, no, the total allowable is based on the proportion of the current nominations to the previous nominations times top allowable.

Now that's the maximum fair share.

The other column is the proportion of

current nominations to average nominations previously times the well's production previously.

So this gives you an idea of what the wells will produce in the first column. The second is simply the maximum above which they would not be produced.

Q But nevertheless, if they could produce it, they could produce that amount.

A They could go up to that amount.

Q So we would be talking about assigning an allowable on the maximum fair share allowable.

A Right, right.

Q If you add up the maximum fair share --

A It's the same as it is today, Mr. Stamets. A marginal well can produce what it produced last month or it can produce any other amount, but then there's that ceiling that's over there, that top allowable ceiling, and you've seen wells that were marginal that were producing more than nonmarginal wells. When they finally get caught up with, they turn out to be overproduced. That's what would happen to these wells if they -- if they were producing more than their ceiling over here, they'd be subject to action because they've overproduced the top allowable. We can call that the top allowable; we can call it the ceiling; we can call it the maximum fair share, or the Max FSW/AF.

Q Let's go to the last page of Exhibit Twenty-five.

A The last page of Twenty-five?

Q Yes. And take the third well from the bottom, that's the Gulf Shanda?

A Yes, that's the little, small well on there.

Q Right. What allowable would the Commission assign that well for the month of June?

A That well has a basic allowable there based on its 1982 production of 515. That's what you could expect from the well.

Now, actually, the well had an average production in 1982 of 1608. Now it's best month wast January of 1982 in which it produced 2640, so the well can actually make about 80 Mcf or 90 Mcf, someplace in between 80 and 90. That's the capacity of the well.

Now, the market demand is 32 percent here for the month of June, so you'd expect it to produce about 32 percent of its maximum, which would be about 30 Mcf, and its -- its fair share, based on that 1982 production is only 515. The well can actually make more than that, so on a fair time on/time off basis, producing at 80 Mcf, it would make 32 percent of 80, which is 24, something like that, and it might come up to about 700 Mcf for that month, but it's not in any danger of exceeding its ceiling because it's really a marginal well; it's a poor well, and its ceiling is 3922 for that month.

So it could produce its 70 or whatever

Mcf, or 40, 50 Mcf, without exceeding its ceiling.

Q Mr. Nutter, under your proposal here, would the Commission really be prorating wells or simply blessing ratable takes in prorated pools?

A They would be prorating to the extent that they're prorating 98 percent of the wells today. That's what I said before time and time again.

98 percent of the wells are classified as marginal and the effect -- the Commission's effect on those wells in the future would be exactly the same as it is today.

Q It seems to me, if I can remember it correctly, that in the El Paso order for northwest New Mexico, that there was a finding that marginal wells should remain on all the time. Of course this has not been -- this is a Commission order and there's a de novo in that case so that finding might not ultimately appear.

It would certainly seem that what you're proposing here is in conflict with the finding in that case, that marginal wells should be on all the time.

A Well, yes, the ultimate finding we're seeking here would be 180 degree opposition to what was found in that case, in which El Paso got its application approved to reclassify all the wells down to almost zero level as nonmarginal, and we're in opposition to that basic order right now for southeast New Mexico, so we wouldn't

want that finding.

Q Moving right along, isn't what we have today just a difference in the matter of scale of what we were looking at in 1954? Let me expand on that.

In 1954 we had a relatively small number of wells. They had higher capacities. Today we have more wells, lower capacities, but in both case don't we have more productive capacity from the wells than we have market demand?

A Oh, yeah, we have productive capacity, I believe; however, I wonder, basically whether we have except during this immediate emergency, because if you will review the Exhibit Number -- I know you weren't at the first hearing, Mr. Stamets, but you probably looked at the exhibits, but if you'll review Exhibit Number Nine, you'll see that nominations have been coming down in these pools for years, and also, that allowables have been coming down, and productivity, as demonstrated by Exhibit Number One, has been coming down, so -- and the number of marginal wells has been going up. So there's been a drastic decline in productivity.

Now, top allowables have been coming down in conjunction with the decrease in nominations, so the number of marginal wells has also been increasing, so I believe the decline in productivity has been greater than the decline in market.

So we don't -- the situation -- at that

time we had an increase in productivity occurring and now we've got a decrease in productivity occurring. It's different in that respect than it was in 1954.

Q Nevertheless, we still have more capacity today than we have demand.

A We obviously have more capacity than we have demand.

MR. STAMETS: I believe that's all the questions I have.

MR. RAMEY: Any other questions of Mr. Nutter?

CROSS EXAMINATION

BY MR. RAMEY:

Q Mr. Nutter, you've made the statements today that pools are in an advanced state of depletion. Wouldn't it follow that some wells are in an advanced state of depletion also?

A Yes, they are.

Q Don't you think something should be done to protect these wells that are in an advanced state of depletion?

A Well, what do you mean protect them, Mr. Ramey?

Q Keep them producing as long as possible.

A Perhaps so. You might ought to put a floor under some of these wells. I don't know. I don't

have any recommendation to make as to a floor. I don't think it ought to be a high floor, but to avoid premature -- you know on our -- on our -- on the statute that relates to -- I'm not sure if it's a statute or just a rule -- that relates to pipeline prorationing to avoid -- on oil -- to avoid premature abandonment, it set a minimum floor below which wells could not be curtailed, and it might be that some sort of minimum allowable, or minimum cuts should be imposed on wells. I don't know.

Q But then your -- under your formula any well would have to be cut.

A This is correct, and we're -- our basic application is for all wells to share ratably. Now, if you have to impose some kind of a floor to protect wells from premature abandonment that's all right, but I think that you have to be very careful in this because, as I stated before, I don't believe that -- the market is going to improve some day, and these wells could be brought back on production, and it may be that the best thing for some of these wells during high -- during periods of high cost of operation would be -- and low takes from the well, it might be better to just shut them in and let them rest. Maybe they'll come back as better wells than they were when they were shut in. This has happened many times.

Q Well, perhaps they will be plugged as a result of this.

A Yeah, somebody may want the pipe more

than they want the future production.

Q What makes you think that today's conditions are not normal conditions?

A Well, let's hope that they're not. The predictions are that this gas bubble will dissipate by 1985.

Q Well, last year it was going to dissipate by 1984.

A Uh-huh.

Q Next year it may be 1990.

A And I remember a prediction several years ago when they said that by 1985 the price of oil would be up to $12.00 a barrel, so predictions are often in error.

Q But any well that's -- any small well that's operating now at its economic limit, say it's making a dollar day profit, you would cut that -- you would cut that, maybe, up to 50 percent or up to 68 percent.

A 50 cent --

Q Under your Exhibit Thirty you would cut it -- you would cut it up to 50 percent, which would make it an uneconomical venture.

A Right. I think maybe you ought to impose a floor, then.

Q But you have no -- you have no --

A I don't have any --

Q -- suggestion for a floor.

A I don't have a recommendation for a floor.

Q What makes you think I'm capable of setting a floor?

A Well, in your wisdom I'm sure you could pick a floor.

Q I think in your evidence on June the 8th you stated that there are gross violations of correlative rights at the present and have been for many years, and I wish you'd elaborate on that a little bit. I always -- I always get a little concerned when somebody says that, you know, I'm running a system that violates correlative rights.

A Well, I don't recall exactly that statement or what predicated it. I'd have to have the background as to what preceded that statement. I must have had some example in mind, Mr. Ramey.

Q I think you stated that, as I remember, you stated that the present system was and had been for years violating correlative rights.

A Well, like I say, I don't recall the exact statement. I'd have to see what it was based on before I could elaborate.

Q Is there any system that would actually be guaranteed no violation of correlative rights?

A No, there isn't. Like I mentioned before, when the Supreme Court said that you determine the total reserves under the pool and the total reserves under the tract and devise a formula that's going to allow the production of a proportionate share, they didn't say you

had to plug the well then, so they were anticipating there would be violations of correlative rights, I'm sure, because there's no law that could be imposed, I don't believe, that would say you have to plug the well when you've produced your calculated fair share of the reserves in the pool.

So I think that the whole basic conception of prorationing recognizes that there are going to be certain violations of correlative rights.

Now, when I said that there had been gross violations, I don't recall the statement. I don't recall exactly what it was predicated on, as I said, and I can't elaborate on it any further at this point.

I apologize if it's in error.

Q But basically the idea behind proration is to --

A It's to try to protect correlative rights.

Q But any -- any well that your formula has caused to be prematurely abandoned would be waste, would it not?

Or any formula that --

A Any formula that would -- that would cause premature abandonment would cause gas to be left in the ground if the wells were still capable of producing and they were abandoned.

Q Now, under your system, Mr. Nutter, I'm

having a little trouble. I see myself as a mediator numerous times, maybe every day for the rest of my life with your system. An operator does not produce his fair share. He goes to the gas transporter. All right, if the gas transporter says well, your well was on the number of days that was called for. Does that satisfy the operator?

A Well, if the pipeline could show him that they were operating the pipeline at the contract pressure and that the well was on those days and the well wouldn't produce, the producer should be satisfied. I mean, if the pipeline can show him they made a bonafide effort to produce his well the fair share time, he should be satisfied. If he's not, he's --

Q What does he do then, if he's not satisifed?

A I don't know if he would have to go directly to Court or if he'd have to come here first, if he wanted to take a case against the pipeline.

Q Well, if he came to us, then we would have to check, I would assume, his production figures.

A Right.

Q We would have to contact the pipeline, get certain information from them, and then probably have a mediation meeting between the two parties, or a hearing.

A I don't know if he'd have to come here first or not. It's a contractual thing and we're trying to

leave the responsibility for policing the actual time access to the pipeline system and the individual operator, and I don't know if the courts would say you have not exhausted your administrative remedy if you didn't come to the Commission first, or not. If there was a gross violation by the pipeline and you took a case to court, they may refer it back to the Commission. I don't know.

Q Well, I visualize a lot -- a lot of personnel would be -- additional personnel would be needed and I'm sure, considering the economy of the state, I don't think Representative Coll is going to give us any more, any more people.

So I'm having a little trouble with this.

A Well --

Q I don't know -- I don't know that --

A Has there been a problem with the 95 percent or 98 percent of the marginal wells to date? I don't believe there has been, and so we're reclassifying another 2 or 3 percent of the wells and I don't visualize that these marginal wells that are marginal today are going to present any more of a problem in the future than they have in the past.

So the most wells that you could have difficulty with would be the 2 or 3 percent that you're reclassifying, if they got into difficulties with them.

If the pipelines say that they're --

Q I believe under your proposal, Mr.

Nutter, though, that all wells would now be prorated.

A Well --

Q To some extent. So we would have --

A No, they're not -- they're not -- they're really not prorated. They're really not prorated. They're put -- they're put on a marginal basis and the pipelines would continue doing what they say they're doing now, is reducing their takes ratably among all of the wells.

Now, under the proposal that El Paso has before you, they would not reduce the takes ratably. They would increase the burden to the Commission because the Commission would be classifying all of the wells as nonmarginal and then policing the production from all of the wells.

This relieves the Commission of a lot of the burden. It puts the burden where it belongs, on the pipelines to impose ratable take, and the application of El Paso here is predicated on pipeline convenience, I believe, and they're passing their burden to the Commission by reclassifying everything as nonmarginal.

And we're easing the Commission's burden by a marginal reclassification.

MR. RAMEY: Any other questions of Mr. Nutter? Mr. Pearce?

MR. PEARCE: If I may, Mr. Chairman, just a few.

CROSS EXAMINATION

BY MR. PEARCE:

Q Mr. Nutter, for my clarification, if for, for instance, the Jalmat Pool, and let's look at your Exhibit Number Twenty-five --

A Okay, that's the mini-proration schedule.

Q -- let's assume that that was complete.

A Okay.

Q If we were to total the maximu fair share with acreage factor column for any month, how would that number relate to the pipeline nominations from that pool for the month?

A That would be in excess of the pipeline nominations, because it's the monthly -- it's the monthly ratio of nominations, the average nominations previous year, times top allowable the previous year, so this would be in excess of the total nominations, but we know that the wells are not going to make that maximum fair share. We know that because many wells are marginal and have been marginal for years and are going to continue to remain marginal, and they can only make a breathe of gas.

Q Okay, let us assume for the moment that pipeline nominations for any given month are exactly what that pipeline eventually takes.

A Okay.

Q From the pool. If the difference between the pipeline nomination and the total maximum fair share

is a number that is less than the amount that the cumulative total of wells in that pool fail to make their maximum fair share with acreage factor, are we not forcing some producer into a situation of producing more than his fair share or in the alternative, are we not failing to allow the pipeline to take what it needs from the pool?

A I don't know if I understand the question.

Q All right, let's go through it, then.

Let's assume that for the month of January of 1983 all of the pipelines taking from the Jalmat Pool nominated exactly the amount of gas that they wanted --

A Okay.

Q -- and they were exactly correct.

A Okay.

Q Now, you tell me that the maximum fair share with acreage factor numbers, if I totaled them for all acreage factors in the pool, is greater than that nominated amount of gas.

A That, it would be far in excess.

Q All right. You also tell me that a substantial portion, if not a majority, if not a substantial majority of the wells in that pool will be unable to produce that maximum fair share with acreage factor.

A Right.

Q All right. If you subtract the pipeline nominations from the maximum fair share totals and you sub-

tract the producing ability numbers for each of those wells from the maximum fair share with acreage factor numbers, if the producing ability shortfall is greater, won't you have a pipeline trying -- needing, having a market for gas and wanting to take gas out of the Jalmat Pool and putting producers and/or pipelines in a situation of producing more gas from some wells than is allowed under the maximum fair share with acreage factor system, in violation of the system which you propose?

A Well, it could occur in a given month, but this would be extended and balanced out over a one year period.

Q Now, let's look again at your Exhibit Number Twenty-five.

Let us assume, and I understand that this is not correct, but let us assume that this is a fully historical record, that your system was in effect in January through, say, May of 1983.

Let us look at the Alpha Twenty-one Production Company Well. In the month of January the maximum fair share with acreage factor number for that well, as I read your exhibit, is 8269.

A That's right.

Q If I go down towards the bottom of the page where I finally get some production numbers for the month of January, I find that in fact that Alpha Twenty-one Well produced 9155.

A Right.

Q Short of some offsetting producer bringing suite against Alpha Twenty-one for having produced more than its maximum fair share with acreage factor, there is no penalty to Alpha Twenty-one for producing that extra amount of gas, is there?

A No, no, because pipeline is going to balance out its takes from that well and while it may have produced 9155 in January, opposed to a maximum fair share of 8269, at some months down the road it would produce less than its fair share.

Q That is dependent upon the ability of the New Mexico Oil Conservation Division ordering an interstate pipeline to do something, is that correct?

A No, this is dependent upon the producer and the pipeline to police this.

Q All right, and the same situation exists, as I read your exhibit, with regard to the Doyle Hartman Husky Woolworth Well, is that correct?

A Well, let's see, it's fair share in January was 8269 and in January it produced 9458, that's correct.

Q And that situation continues in your exhibit --

A You have some wells that over --

Q -- through the month of June. You have some wells that are producing more than this maximum fair

share --

A And some producing substantailly less.

Q -- and the ultimate remedy for that is the courthouse, whether or not there is an initial step at the Oil Conservation Commission, as I understand your position.

A Unless it can be amicably worked out between the producer and the pipeline.

Q And that results because there is now no accumulation of over or under production, is that correct, since these are all now marginal wells?

A That's correct.

Q All right. Now, turning to your responses to some of Mr. Ramey's questions.

Let us refer to a category of very poor wells which need to be left on in order to prevent premature abandonment as super-marginal.

A Okay.

Q (inaudible due to tape change) was developed, would you not in fact have instituted the prorationing system we presently have but for the fact that you have replaced 100 percent acreage allowable calculation with a deliverability allowable calculation?

Would you not have two classifications of wells, one which is to remain on all the time and one of which is by some system, either acreage or deliverability, regulated in the amount of gas it can produce?

A I don't know if there's -- if the system would say that you'd have to remain on the line all the time or not. What it would do, it would assign, as it does at the present time, a minimum allowable. Now that minimum allowable, I don't believe, Harold can correct me if I'm wrong, is applicable in all pools, but it would assign a minimum allowable. If the well could produce it in one day, it would produce it in one day. If it takes thirty days to produce it, it would produce it in thirty days.

Q But as you understand it, that's just a renaming of our present marginal system. We don't require that the wells remain on all the time. We simply say that it's allowable is whatever it can produce. That, it would be the same system.

A For the -- for the bulk of the wells. The allowable, or the fair share would be -- two fair shares here, one based on '82 production; the other based on maximums, and the wells would be permitted to produce up to that subject to the curtailment that developed each month.

Then this little group of super-marginal wells would be allowed to produce a given volume of Mcf, whatever that might be, 500 Mcf for the month, or whatever.

Q But they would essentially have a minimum allowable assigned to them.

A They'd have a minimum allowable assigned.

Q Thank you, sir.

Looking at your Exhibit Number Twenty-

Seven, which is the explanation of your calculation of the production ceiling.

A Okay.

Q As I understand that calculation, the present system of adjusting nominations would be abandoned, is that correct?

A That's correct, because at the present time the nominations are adjusted for a number of factors, overproduction, underproduction, and various other factors that go into deriving the allowable, and you wouldn't have overproduction in the picture any more, so you wouldn't use adjustments on the nominations any more.

Q Whatever reasons existed at that time, which I believe you explained in your prior testimony for establishment of that adjustment system, you believe would no longer be required.

A They wouldn't be required any more, because, now, like, for instance, today under the existing system, you take the pipeline nominations, that reflects what they want for next month.

All right, you've got a whole bunch of underproduction that's in the picture. You subtract that from the nominations because that's already in the allowable formula, the underproduction is, so that's deducted from the nominations to get adjusted nominations.

If you've got overproduction, you have to add some more on to the nominations to cover the overpro-

duction that's in the pool.

So you wouldn't have this over and under status to deal with any longer, and you wouldn't have to adjust nominations.

Take the pipelines at their word: This is the amount of gas we want for next month.

Q Looking now at your Exhibits Numbers Twenty-nine and Thirty, Exhibit Number Twenty-nine representing the El Paso proposal as you believe that would develop.

A Yes.

Q Now, Well No. 1, which has the producing capability of 450 and is allowed to produce only 117 because of currently depressed market conditions, under the present system does that well accrue underproduction?

A Yes, it's the -- it's the one well -- it's the one well on here that is nonmarginal. The other wells are all marginal.

Q And if, as you said in response, I believe to one of Mr. Ramey's questions, if the market were to turn around, that well would be able to make up that underproduction, is that correct?

A No, there wouldn't be any underproduction under this allowable formula, because, you see, under the formula the demand is now 500 Mcf a day, so it would be permitted to produce 117 Mcf. It wouldn't accrue any underproduction. It would be producing its allowable.

Q I thought you responded to my first question by saying that it did.

A No, I didn't understand it, then.

Q Thank you.

MR. PEARCE: I have nothing further.

MR. RAMEY: Any other questions of Mr. Nutter?

MR. STAMETS: I have three short ones.

QUESTIONS BY MR. STAMETS:

Q Mr. Nutter, would you agree that the ratable take statute does not apply when the Commission has prorated a pool?

A That the ratable take statute --

Well now, you were reading, weren't you reading ratable take in two different places awhile ago in the statute; one was regarding proration, one wasn't?

Q No, I was reading some of the factors that went into prorationing and then ratable take. Perhaps I -- well -- well, do you agree --

A I couldn't tell you because I don't have the statute in front of me, Mr. Stamets. I don't whether it applies.

Q I presume the Commission could read it and see whether or not they thought that when prorationing

was adopted the ratable take statute did or did not apply, I presume.

A I guess. I don't know.

Q All right.

A I don't have the statutes in front of me so I don't know.

Q Would you agree that prorationing in southeast New Mexico has always been on straight acreage?

A Absolutely.

Q And would you agree that --

A Except to the extent that the marginal wells are really not on straight acreage, and they account for 95 percent actual count now and 98 percent of the wells we're talking about in the hearing today. They're not on straight acreage any more.

Q That's not related to the formula.

A The formula -- the formula does not include the word deliverability.

Q Okay, and what you're proposing then is conversion to deliverability with a cap and a cap that applies only to, say, two or three percent of the wells.

A I don't know that I'd say it's a conversion to deliverability. It's putting everything on a marginal basis and if marginal means deliverability, then you're right.

Q Okay, thank you.

MR. STAMETS: That's all the questions I have.

MR. RAMEY: Any other questions of Mr. Nutter? He may be excused.

We will recess until 1:30.

(Thereupon the noon recess was taken.)

MR. RAMEY: The hearing will come to order.

Did you have anything further, Mr. Carr?

MR. CARR: Nothing further on direct.

We might have a rebuttal witness, and we might not.

MR. RAMEY: Anyone else? Is there any more direct testimony to offer?

Do you want to put your witness back on, Mr. Nance?

MR. NANCE: Yes, sir, Mr. Chairman. What El Paso has is something in the nature of rebuttal testimony to the Hartman Case.

We'd certainly be willing to wait until any other direct testimony is put on, but we do have his testimony plus two exhibits that we would like to introduce.

MR. RAMEY: Anyone else have testimony to put on? Okay, Mr. Nance, if you're ready,

Mr. Nance, I think you're back on the line.

MR. NANCE: Thank you, Mr. Chairman. Let me hand out, if I may, what El Paso has designated its Exhibit Number Eighteen.

H. L. KENDRICK,

being recalled as a witness and having been previously sworn upon his oath, testified as follows, to-wit:

DIRECT EXAMINATION

BY MR. NANCE:

Q Mr. Kendrick, if you would, please, explain what the two sheets designated El Paso's Exhibit Number Eighteen are designed to show.

A To explain the use of Exhibit Eighteen, I need to tell you how the data is derived to plot the curve that is shown.

I went to the April, 1982 gas proration schedule for the Jalmat Pool and copied the New Mexico State Gas Proration Schedule for that pool to get a listing of wells and acre factors for every well that was a producing well at that time.

I then looked at the New Mexico Oil and Gas Engineering Committee Report for the year 1982 and looked for each well that was listed on the Jalmat Gas Proration Schedule for the highest producing day -- highest producing month from April '82 through December, 1982, and

used that figure regardless of what month it was from as the high or the producing ability for each well, or for a multiple well unit for the producing ability of that unit.

Now, if a well -- if several wells are completed on one multiple well unit, the data I took was not the highest per well from different months, I looked for the highest unit production for a month, and used that as the producing capability of that proration unit.

I did that for the matter of -- to calculate an allowable on 100 percent acreage allocation for the Jalmat Gas Pool for every well in the pool, and in doing so the first page of this is a calculation of what would have happend in October, 1982 had the nominations been exactly what the total production of the pool for October, 1982 was.

And there remember we've got the assumption that April of 1982 Gas Proration Schedule had all the wells that were produced in October, on the line at that time and their acre factors were the same, and with that set of assumptions I took the October, 1982 gas production was 398,431 Mcf for the month. This being the lowest month that we had shown on our previous exhibit for the Jalmat Gas Pool in the period when this exhibit was submitted earlier.

Q Do you -- could you tell us what exhibit that is, Mr. Kendrick, if people wish to refer to the exhibit?

A Right now I can't. The exhibit I'm referring to is one that was -- showed the gas production for

ferring to is the one that was -- showed the gas production for a 12-month period in the Jalmat Pool. I think it was Exhibit Number Eight.

Q Exhibit Number Nine.

A Exhibit Number Nine was a 2-page exhibit, one page being the data showing the amount of gas produced, the amount of gas that was considered marginal gas, the amount of gas that was considered nonmarginal gas, and this 398,431 Mcf was the production, total production for October, 1982.

From the Gas Proration Schedule I came up with a figure of total acre factors for that pool.

Also, in the manipulation of data, and I don't mean manipulation in a way of trying to arrange it in such a way as to tell you a story that's not there, I took another list and I listed the producing ability of every well in the pool in an ascending order of production, and I've got seven pages of that.

Then I made a comparison by dividing the acre factors for the Jalmat Pool into the total production for October, 1982. I should have gotten an answer that would say this is the top allowable for any well in the Jalmat Pool for that month; however, in using that value I would some wells assigned an allowable that they could not produce.

So looking at the record of the producing ability of every well and of the acre factor of each well, I

subtracted the actual producing ability from the total production. I subtracted the acres factors from the total production, reduced now the total production by the amount of gas that would be marginal on this first time through, first time calculation, and reduced the acre factors that amount, by the amount of what was represented by each of the wells, and I made the division again, dividing acre factor into the now new number of amount of gas we're going to produce.

I continued in that process, it's just a reiterative type calculation, until finally you calculate again and no other well comes up marginal, comes up with an allowable greater than it can produce. And at that point I reached a number that said that at a value of 1355 Mcf per month would be a dividing line for the month of October, 1982, so that anything that produced less than that would be a marginal well; anything that produced greater than that would be a nonmarginal.

Now, this gives you an idea of what we're looking at and the minuteness of a producing ability that has to be considered as a nonmarginal well.

I plotted that on Exhibit Nineteen, which is the companion page to Exhibit Eight, is that what we decided?

Q That's right.

A Exhibit Eight, well, where is it?

Q You want to get into this exhibit, as well?

A Yes, sir, I'll get into that and then I'll come right back to this other one in just a second.

All right, excuse me, I'll stay with the Exhibit Eighteen.

When I finally reached a calculation of 1355 Mcf per month, that's the top allowable for an acre factor of 1 for any well in the Jalmat Pool, considering the assumptions that I made, the production had to equal nominations, we've set allowables for every well on exactly what happened in that month.

This graph is drawn with the idea the producing ability of all wells would be incorporated on the horizontal axis, the allowable on the vertical axis, in Mcf per month.

As the line begins from a O-0 intercept, it goes up a ways and it is at a 45 degree angle, which says that whatever its producing ability is is what its allowable is, and that was true for all the wells that became marginal.

And then at a point, the dividing point between marginal and nonmarginal wells, the line becomes horizontal. Every well that produces greater than 1355 has an allowable of 1355 for the month. That's its acreage allo-cation.

Now, to convert 1355 Mcf per month for the month of October, I divided by 31 and I got a figure of 43.7 Mcf per day for each acre factor of 1.

Now, this being the lowest month that we experience in 1982, I did this for the purpose of showing we must keep the number of marginal wells at a minimum, I took the month of December, which was the highest month of production in 1982 from my Exhibit Eight, took the total --

Q Nine, Exhibit Nine.

A Exhibit Nine, second page of -- is Jalmat Exhibit Nine?

Q Yes, sir.

A I'm sorry. Took the total production for the month of December, 1982, and went through the same process in that as I did for October, 1982, and calculated allowables, subtracting out the wells that would be assigned an allowable greater than its ability to produce, as a marginal well, took that from the total amount of production, took their acre factors away from the total acre factors of the pool, and made another calculation and went through it seven times, and finally I reached the point 7 times 12 that no other well was going to drop out as a marginal well, and said, well, perhaps I've gone far enough.

That data then is plotted on the second page of Exhibit Eighteen. This is made to the same scale the first page is made and the first part of the line as it comes from 0-0 intercept is a 45 degree line. Any well that has a producing ability of 2000 per month would have an allowable of 2000 per month, 3000 per month, the same way, until we reach a point near the top where the line turns

horizontal. That value at the top I calculated to be 6724 Mcf per month. For the month of December, that's 31 days, that's 217 Mcf per day for any well with an acre factor of 1.

Now, those two bits of data were resolved back to the graph shown on -- introduced as Exhibit Nine.

Q At this point, we'd like to go ahead and introduce Exhibit Nineteen, which is based essentially on Exhibit Nine, with some additional information placed on it as well.

Mr. Kendrick, at this point, if you would, please explain the relationship between the information on Exhibit Eighteen and that on Exhibit Nineteen.

A The data shown on Exhibit Nineteen, that came from Exhibit Eighteen shows only the month of October for the first graph on Exhibit Eighteen, and shows in the month of December for the second graph in Exhibit Eighteen.

All of the exhibits are not colored, so if you recall what happened a month ago when we entered this exhibit, the top boxes across the page were painted green, the top of each column was green, representing nonmarginal gas production. The bottom part of those boxes was painted red, which represented marginal gas production.

Now, in the month of October, I have a little box at the very bottom, and on mine I have it cross-hatched in blue, and that represents the figure that I calculated through the schedule for the month of October, where

the breaking point should have been in calculating allowables for the month of October, 1982, assuming production and nomination were the same.

That would have a breaking point of 43 Mcf per day.

The second graph in Exhibit Eighteen, which has the higher value, shows in the month of December, and on mine I show it as cross-hatched up about halfway, of the marginal production that was in the month of December.

Now, all of this is done to show you that El Paso is asking for all wells to be classified as nonmarginal, and if not all wells classified as nonmarginal, then let's set a figure that is low enough that in the production of wells on a daily basis, day in and day out, high month demand, low month demand, we will have only those wells classified as marginal that will not need to be shut in by any pipeline company.

This mode of calculation is the means by which the Commission goes through in calculating allowables for pools in their normal process, and this was not doctored by any data of previous production versus previous nominations. This is just trying to put fact against fact, because we had October's production and the October wells to work with.

Q Mr. Kendrick, do you have, or could you get the Commission an indication of the relative impact of El Paso's proposal versus the Hartman proposal in this case,

in some sort of graphic manner?

A I will try to do that, and I do not have that as an exhibit, but I'll try to draw one on the board, if I'm permitted to do so.

I've got to have a starting point. Suppose we start with a scale the same as we did with Exhibit Eighteen. We'll call this daily producing ability or well producing ability, well potential, well deliverability, whatever you want to name it, I don't care; call this factor allowable.

Starting with a zero and a zero, and the calculation as I understand has been submitted by Hartman, says we have a -- may I ask Dan to help me -- maximum producing -- maximum permitted rate?

MR. CARR: Fair share.

MR. NUTTER: No, fair share.

A Maximum fair share, that is a calculated fact.

MR. CARR: With acreage factor.

A With acreage factor, let's say it's an acreage factor of 1, and we'll draw maximum fair share. We said that at any point beyond where this starts, whatever the deliverability of the well might be, its allowable will be cut off here.

Now, let me draw a line then at a 45 degree angle. It just happened I nearly hit that, boy; I don't care whether I did or didn't, but now I must maneuver

every well that falls in this category from here back to zero, from the intercept to where that point is. But wait a minute, now I'll go look at October, 1982 again. I'm going to take the total production for October, 1982, and compare that to the average of 1982, that Mr. Nutter has prepared. Using that comparison I came up with a figure that -- I've got to do it by figures -- of approximately 38 percent, October production was 38 percent of the average for the year.

According to that plan that's presented by Mr. Nutter, we would control the production from all other wells by that 38 percent amount. Okay, now I have to reduce this from a 1-to-1 ratio to 38 percent, so that every well is reduced in this area by an allowable of that amount.

So when you start looking at this from this zero point on up, see, I've got deliverability allocation until I reach this point; then I've got a maximum and that's the way I understand it.

Q And can you compare El Paso's proposal to that? Would it be the --

A El Paso's proposal, and not bending the proration rules of the pool, says that we'll continue with acreage allocation, and El Paso's line went along this line until we reached a point of cutoff, and -- I've got to find Dan's figures.

Q Is it Exhibit Twenty-one?

A The figure that I have calculated for

October, 1982, for this line is a figure of 4675 Mcf per month.

On mine for straight acreage allocation I came up with 1355. So the difference in allowable, while our plan is made up by the amount of gas in this area from these smaller producing wells and to the larger producing wells in the Hartman plan, this cutoff is 43 Mcf per day on our plan and I do not have that figure calculated there.

Q Would you summarize, Mr. Kendrick, why you feel El Paso's approach, then, to be a more correct one?

A I feel if we have field rules, or pool rules, in any pool, whatever those rules are, we should prorate by those rules, if the rules are made for proration, and we feel that these are.

We feel that the Commission has a responsibility to set allowables according to the nominations that are submitted by the pipelines. We feel that the pipelines should have an opportunity to produce the gas as it's needed to meet their market demand, and we do not feel that it's the pipeline's responsibility to calculate the allowable for each individual well on their linel. We don't think it's our police action to look after every producer on the line. We don't think it's necessarily their job of policing every well on the line.

So we really feel that the Commission has its job to do of calculating allowables, assigning them, and doing it, and we say that we can do that with a minor

adaptaton of gas well classification, or reclassification, if you please, to change marginal wells to nonmarginal wells, and then you have wells that you can work with is assigning the allowable.

If we play with numbers and say we have 95 percent or 98 percent of the wells classified marginal now, my reaction to that is okay, how did they get there? They got there because the market was strong. We were approaching a limit of whether we would be able to take all the gas that was available in every pool.

But all of a sudden we didn't reach that limit and now we're taking possibly 60 percent of the gas or 70 percent or 50 percent of the gas from the pools, and to cause those same wells to be properly reclassified, the automation that's built into the rules that apply under Order 1670 on how to classify wells will not work and it will not work solely because we shut off marginal production.

Had El Paso and other pipeline companies been able in a month of low production to shut off only nonmarginal wells and reduce their takes from the pool to what actually became market demand, and would have been able to do that from April, 1982, through March of 1983, the wells would have automatically reclassified themselves to nonmarginal and we would not be here today.

But because the pipeline companies did not have time, they had to cut their loads more drastically,

then we did shut off marginal wells. Whether we shut them off in a proper sequence I think is not the issue. El Paso very certainly could have erred in that. I make no excuses for it today. But it's something that has happened. But wells need to be reclassified to nonmarginal and the system works.

Q And it is your opinion, then, Mr. Kendrick, that this is the manner in which correlative rights may best be protected and waste might best be prevented?

A Yes, sir.

Q Is there anything further that you have to add at this time?

A No, sir, I believe not.

MR. NANCE: That concludes El Paso's rebuttal testimony, Mr. Chairman, and the witness is tendered for cross examination.

MR. RAMEY: Thank you, Mr. Nance. Any questions of the witness? Mr. Carr.

CROSS EXAMINATION

BY MR. CARR:

Q Mr. Kendrick, if I understand your Exhibit Number Eighteen, this shows how El Paso's proposal would work, is that correct?

A Yes, sir.

Q And on the first page of Exhibit Eighteen

only wells with a capacity or that are able to produce less than 1355 Mcf per month would be able to be what you call marginal wells, able to produce all they could produce into the pipeline.

A Yes, sir.

Q And everything that would fall above 1355 Mcf per month would be cut back to that level, that would be their allowable. Is that what this shows?

A Yes, sir.

Q So if I had a well that produced 1356 per month, I would be cut back 1 Mcf per month.

A Yes, sir.

Q And if I had a well that produced 2-million a month, I would still be cut back to 1355.

A Yes, sir.

Q And we would all be treated the same above 1355.

A Yes, sir.

Q And we would not be -- curtailment would not be proportional but we would be treated as if we were equal.

A They would be -- the curtailment would be according to the rules that exist in the pool today.

Q And under those rules and under your proposal it would mean that all wells above 1355 would be permitted to produce only that and no more.

A Yes, sir. Excuse me, just a little bit

of elaboration.

1355 is the allowable for that month. Of course the wells could be overproduced or underproduced but that is the allowable.

Q That is what their allowable would be.

A Yes, sir.

Q Now, if we go to the second page, this is similar.

A Yes, sir.

Q And all the wells that would fall below, and I didn't get that figure, 6500 plus or minus -- 6724, all that produced below 6724 Mcf per month would be able to produce into the pipeline all they could produce.

A Yes, sir.

Q And we treat everyone above that as if -- I mean that would be the allowable for all wells that had a capacity of in excess of 6724. Is there any reason that you cut this off at 9000 Mcf per month and 300 per day?

A No, sir, it was only due to the size of the paper.

Q And if there are wells in the Jalmat that produced 2-million a day -- I mean, yes, 2-million a month -- is it a day?

A 2-million a month would be back on --

Q Okay, I'm sorry, 2-million a day.

A Anything larger than the 9000 Mcf per month would be on that same line.

Q But to make this graph truly give an accurate picture of what goes on in that pool, you would have to extend this line that sets the allowable out to the right some distance so it would pick up even those wells that produced 2-million a day, is that correct?

A Yes, sir.

Q So, what in effect you'r doing with this allowable, is you're bringing all wells above those that are classified marginal to the same level.

A That's what the rules provide for.

Q And you're treating them the same.

A Yes, sir. Each of these are considered with an acre factor of 1.

Q And you anticipate a fluctuation of over almost 80 percent between October and December, is that the kind of fluctuation you actually think you would anticipate?

A I used this to show the extremes that did happen in 1982, and those extremes on a per month basis may be even more exaggerated on a per daily basis -- per day basis.

Q Mr. Kendrick, the reduction that would be bringing all the wells, say, in October down to 1355, in your opinion is that a ratable reduction?

A It's in accordance with the rules of the pool.

Q Well, but is that ratable?

A Do you want me to give you Kendrick defi-

nition of ratable?

Q No, what I'd just like to -- maybe I could just ask the question this way. Is that a proportional deduction?

A I don't know that it would be a proportional if you're saying everything is reduced by the same percentage. I would say, no, it is not a percentage deduction.

Q Now, the proposal that you set out on Exhibit Eighteen is for southeastern New Mexico.

A Yes, sir.

Q And under your proposal we're looking at straight acreage allowables.

A Yes, sir.

Q We have no deliverability that figures into this whatsoever.

A That is correct.

Q And unlike the northwest, the better wells are not entitled to produce more than a poorer if they're above this cutoff between marginal and nonmarginal.

A That is correct.

Q And would you accept that some wells would be cut back by as much as 90 percent under this proposal in a month like October?

A I would not be surprised.

Q And others, of course, would not be cut back at all.

A Yes, sir.

Q And as this proposal works, would you consider that affording equitable market access to the producers of all the wells in each pool?

A I'm not sure that I can answer that question in the sense of a pipeline company trying to produce gas from prorated wells in accordance with the rules of the pool, which we were trying to do, and as we assume other pipeline companies were trying to do.

But that's what we were trying to match is our takes according to allowables.

Q And you could not comment on whether or not it is fair and reasonable to operators in the pool to curtail one 90 percent and others not at all?

A If the State of New Mexico permits 100 percent acreage allocation and accepts that as a just and equitable means of prorating gas pools and prorating oil pools, then I'd say, yes, it is just and equitable and fair.

Q And a guy who is producing well that makes 1000 a day has certain correlative rights which should be protected, is that not true?

A He's producing how much?

Q 1000 Mcf a month.

A All right, yes, sir.

Q And you have an operator who's producing 2-million a day, he also has correlative rights, does he not?

A Yes, sir.

Q But if he isn't able to sell what he has under his tract and can produce, is it your testimony that his correlative rights are protected?

A Again, the proration formula as adapted to the pools in southeast New Mexico was based, supposedly, upon correlative rights, and under that basis that that formula was established.

Q And your testimony is in terms of correlative rights is conditioned upon the effectiveness of the individual pool rules.

A Yes, because there are pools prorated on 100 percent acreage in some areas and some pools prorated on 100 percent deliverability.

Q Now in this proposal you -- well, let's -- if we look at page one in Exhibit Number Eighteen, you would let all wells that produce less than 1355 a month produce all they can produce into the pipeline. That's correct, is it not?

A With a little bit of overriding data. I'm not saying that because October, 1982 was the lowest month we produced in '82 that 43 should be the lowest point that we have to consider as a breaking point between marginal and nonmarginal wells.

I would say we have to have a figure below 43 and then that would be 33, anything above 33 would be considered nonmarginal wells; anything below 33,

marginal.

Q The purpose for having that cutoff is to protect the operators of the poorer wells, is that not true?

A It is to -- under the application of the rules of pools in calculating allowables for wells, it says that if these wells are incapable of producing their allowable, then what they produce becomes their allowable.

Q And as you understand those rules, the reason you don't shut them in, is it not to protect the interest owners in poorer wells?

A We see that it is not our plight in life to take a well that's considered a marginal well that could neither accrue underage or overage and cause that well to be shut in when other wells as nonmarginal classification do accrue underage and overage and if they become underproduced have the opportunity to make up that underproduction where a marginal well does not have that opportunity.

Q But is it your testimony that in not curtailing marginal production you do not -- are not concerned about attempting to keep the poorer wells on line?

A Do that once more, please?

Q Is it your testimony that in not shutting in marginal wells it is -- have to get all my negatives out of this question -- is it your testimony that El Paso's policy not to shut in marginal wells doesn't take into consideration the fact that certain of them might be pushed beyond their economic limits?

A We cannot consider economic limits for everyone's well. That's where the proration formulas as applied depict allowables that can be produced from various wells, and economics for one operator are definitely different to another operator, and we cannot look at them. We take the figures as prescribed in gas proration schedules and try to produce those allowables.

Q Why did you pick 33 Mcf?

A Okay.

Q That's the thrust of my -- I'm trying to find out. Is it entirely arbitrary or is there some reason for that?

A I'd say it is semi-arbitrary, but on the first page of this Exhibit Eighteen I have indicted that the lowest month of production in 1982 said the breaking point could be at 43 for the month. During that month we may have had fluctuation, both up and down, in the daily takes of gas from that pool.

And in doing so, if the rate goes up we can turn on more wells, and if the rate goes down, we have to turn off wells.

If we turn off down to 43 we may not have enough gas turned off, so turn off down to 40, to 37, and we picked a figure of 33 which represents a million a month as a semi-arbitrary figure.

Q Doesn't that tend to protect poorer wells in the pool?

A The wells that have an allowable assigned as what they produce, and we're given the opportunity to produce them as much as they will produce.

Q Mr. Kendrick, didn't last year you cut back on occasion to 25 Mcf per month?

A Yes, sir, we did.

Q What would you do in that situation?

A Since the time of last year -- we cut back in steps last year. In fact, we started cutting off only nonmarginal wells. Then it became evident we had to shut off more than nonmarginal wells so we picked a figure of 100 Mcf a day and said we will cut off any well that produces greater than 100 Mcf per day. And then we got to the point where that's not enough, we've got to cut off more, and we went to a figure of 25. That's a magic number picked out of the air or off of a Burlington Northern boxcar as it went by, but 25 was just a figure to start. We figured we could leave the rest of them on that produced less than that.

Q As I understood your comparison on the board of El Paso's proposal as opposed to Mr. Hartman's, you stated that with Mr. Hartman's proposal you would have to maneuver more wells than you would with your proposal. Is that a correct statement?

A I don't understand what I said as maneuver.

Q Maybe you could tell us what --

A Let me back into this way and say if we're talking about the difference of having now 95 or 98 percent of the wells as marginal and the remaining few to 100 percent as nonmarginal, and the question comes up, what are we going to change, the fewer number of wells or the greater number of wells, I have no problem in changing the classification of the greater number of wells because one stroke of the pen, I have made a marginal well to a non-marginal well, and the computer, if I think I understand the system that's in operation by the Division Office here in Santa Fe, has a program already in operation that would take those wells by that classification and calculate them allowables for every well in the pool on the basis of the formula that now exists for that pool.

Q Now would there be such a program in effect if Mr. Hartman's proposal was granted?

A A little intelligence is dangerous, but from what I know about computers and program writing, nothing exists in Santa Fe, according to my idea, that would handle Mr. Hartman's proposal at this time. Computer programs would have to be written and a different procedure of calculation have to be made to handle the proposal by Mr. Hartman.

Q So is it fair to say that it would be more convenient to take your proposal than that of Mr. Hartman's?

A Absolutely.

Q Now, when you talk about having to reduce production in a month by 38 percent, for an example, isn't that really partially because the nominations are down?

A No, sir.

Q Is it not. So if you cut your nominations back that is not going to reduce the allowable.

A Mr. Carr, it may reduce the calculated allowable that is printed in the gas proration schedule but the pipeline company is going to produce wells to meet its current market demand day by day, if at all possible.

Q So maybe this is where we've misunderstood each other before. When a reduced nomination can reduce an allowable but it doesn't reduce what the pipeline will take because they'll be taking their demand and there are other things that will work that out.

A Yes, sir.

Hopefully, this was one of the stipulations that El Paso tried to make early in the game, that whatever we do in this, we are in no way trying to reduce takes from any pool in the State of New Mexico; that whatever happens on this, we'll still be taking exactly the amount of gas we can sell at the other end.

Q The takes will be the same, but as your market falls off, your nominations will come down.

A Yes, sir.

Q And the allowables will therefor be lower.

A Or if we nominated the same every month and takes got lower, then the adjustments to nominations would lower the allowable.

Q Now I've asked you this before, but your proposal is based on what -- you are asking that your proposal be adopted and that in effect the Commission stand behind the pool rules on an individual pool basis.

A Yes, sir.

Q Now, if we stood behind these pool rules, wouldn't there automatically be a reclassification of wells back to nonmarginal?

A Yes, sir.

Q Isn't it true that your problem is that you're just unwilling or unable to wait till these rules work?

A No, sir.

Q What is your reason?

A The reason is, as I said a few minutes ago, by virtue of the fact that El Paso shut in marginal wells during 1982, from April 1st, 1982 till March 31st, 1983, we caused the system to fail to work to reclassify wells from marginal to nonmarginal that should in effect truly be nonmarginal wells.

Q But if you did wait the system would work to correct this problem, would it not?

A No, sir.

Q It woudn't ever?

A If a reduction in takes due to our market demand are as drastic as happened in '82, so that we have to shut off a marginal well, when we shut it off it shows then, when you're making your annual comparison, or quarterly comparison, that that well did not produce greater than its calculated allowable, so it stays marginal.

The reason it stays marginal is because we shut it in and we say we should not be shutting in that marginal well, any marginal well.

Q Now, I think you have stated that El Paso's proposal would result in a minimum reclassification of wells. Is that what you mean?

A The minimum amount of work could be applied and reclassifying 99 percent of the wells and the system would be on a go and would be ready to run and ready to conduct our business the remainder of the year.

Q So you weren't talking in terms of reclassification of a minimum number of wells, but a minimum amount of work involved in getting there.

A Yes, sir, I think you're correct in that.

Q Your testimony is that El Paso's proposal is more convenient than Mr. Hartman's in that regard.

A Yes, sir.

Q And is it more convenient to El Paso Natural Gas?

A I would say very definitely our proposal is more convenient to El Paso Natural Gas than Mr. Hartman's

proposal because we have a system in our company that we check the allowables calculated by the Commission. We compare the status of wells that have statuses because they're nonmarginal, and we can calculate the allowables side by side with them.

For us to change to Mr. Hartman's system and using in-house programming, I would hate to think how many months it would take for us to get a computer system running that would do that.

Q Did you consider the inconvenience to someone like Mr. Hartman of having his wells cut back 90 percent?

A There are pains in all of them. No one said it would be easy on anyone, but it is a problem that exists across the industry and we're all suffering because of it.

Q I understand it would be painful to get, perhaps Mr. Hartman's proposal, in your opinion, off and running, and it would take, as I understand your testimony, perhaps many months to do that, is that correct?

A Partly. The programming people in the El Paso organization to establish a program for us to work with would take, and I'll dare say, months, because they figure things on a daily basis and then when we add up these days, they are very long days.

Q Well, how have you been able to do it during this periods of demand when you were called upon to

curtail the marginal wells? Has that taken months?

A No, sir, we have a system whereby we can curtail right now under any basis provided by any rule of the Commission. Now, I say any, any that we have heard of or thought of that would be in use by the Commission.

Q And that would include the deliverability based approach?

A We can control it by deliverability for wells in the San Juan Basin, where deliverability has been part of it.

We can control production of wells being on the line the same number of days or being shut in the same number of days.

We can control wells by the volume they produce where that they're producing at equal volume.

So we can set our program to operate on either one of those bases, yes, sir.

Q And isn't in fact what Mr. Hartman is seeking merely curtailment on a daily basis?

A I believe there's more to it than that.

MR. CARR: No further questions.

MR. RAMEY: Any other questions of Mr. Kendrick? Mr. Kellahin.

CROSS EXAMINATION

BY MR. KELLAHIN:

Q Mr. Kendrick, I think I've lost track about your drawing on the board here. Refresh my memory as to what is the -- well, first of all, this is your understanding of Mr. Hartman's proposal, is that not true?

A Yes, sir, part of it is.

Q Yes, sir. I'm concerned about the shaded area, the hatched line area in the drawing. What does that signify to you?

A Well, first of all, let's take this line off. Remember this line is a 45 degree line so that anywhere up to this line from the producing ability to here, across, the allowable would be equal to the producing ability.

The first thing that we can do under Mr. Hartman's proposal is calculate a maximum fair share, and that is this line. It would extend to the highest producing well in the basin.

Then, since for other wells, as Mr. Nutter presented testimony last month, he said that would be a marginal category, not making this amount, they would be reduced proportionately, just comparing that well, that well's allowable would be reduced in the percent that its 1982 average production compared to the nominations of '82. I think that's what -- if that well's producing ability were only 38 percent, then you've got a line of 38 percent that you would have to reduce this amount, and that is kind of how -- from wells that could be producing gas that's

enclosed in the cross hatched area.

Q The shaded area then is the shut in time for each well for each --

A It would be shut in time because their allowable is now reduced to this level, to this line, the lower line.

MR. NUTTER: It's shut in volume, not time.

A Well, time equals volume if you're producing gas, and we're working here with volumes, and you work with shut in time, then you are cutting off gas, so gas and time is volume.

This amount of gas would be displaced here and actually picked up with the other --

Q My point is, the shaded area doesn't have anything to do with the straight acreage allocation.

A No, sir, it doesn't. It's a difference between straight acreage and what might -- I would consider that as deliverability.

Q Thank you. Mr. Kendrick, I was interested in what your definition is of prorationing and ratable take. You about offered us one awhile ago and didn't.

If I attend the Kendrick school of gas prorationing and ratable take in New Mexico, and as a college freshman I know nothing about most everything, and you are a guest lecturer that day and you're going to tell

us about conservation practices in New Mexico, and you've told me that there are two basic concepts under gas prorationing is implemented for given pools in New Mexico, one concept is under straight acreage factor, and the other is based upon some deliverability factor. Would you first of all tell me, in a pool that is prorated under a straight 100 percent acreage factor, how will the well -- the pool be produced so that each of the proration units within that pool are going to be produced in a fair, equitable manner to all the operators of the wells?

A For rules to be established for a pool to have 100 percent acreage allocation within that pool, the operators and the Commission would -- the operators would agree and convince the Commission that this is a means of controlling the production from the many wells in the pool to the many wells collecting gas from the pool on a basis that the amount of gas owned by each operator under each tract he drills is proportional to the acreage that is dedicated to that well. That is a premise that has to be in there for the operator to agree to begin with.

And after they do that, then they say, well, we will find out in New Mexico what the market demand for gas is, and the pipeline companies would submit their nominations of market demand, and that total market demand, then, would be divided up to the wells according to the acreage that each well had, and as we start out, we say every

well is permitted to produce 1 Mcf. Now does that give enough gas to make the market demand. And no, we'll give every well 2 Mcf, and you continue it that way until you get an allowable high enough that that will meet the market demand.

Now in going that high you will find some wells that fail to produce the next high Mcf and that's drops off as marginal for that month, anyway.

Until you reach a level that says, well, with what few wells have fallen out as marginal now, all the rest of the wells can produce a common figure of 396 or 891, whatever that common figure is for that month, and make the allowable that the pipeline company has told us is their demand for this month.

If the demand goes down next month, due to reduced nominations, the figure from 891 might be reduced down to 700. Some of the wells that might have been between 700 and 891 as classified as marginal, would be nonmarginal in this category because they produce greater than 700, and this did, every well would be limited at the top at 700 Mcf for that month.

That would be straight acreage.

Q What if I am told that there is a scheme of gas prorationing that can be based upon something other than straight acreage; perhaps deliverability.

If you had a pool that you wanted to prorate based upon deliverability, what do you do then?

A The same thing exists that the operators with wells in those pools through their decisions and through their -- through the decision of the group of operators they say that the reserves that each of us have under the tracts that we operate is proportional to the deliverability of the well, and if the reserves are proportional to the deliverability, then we should take from each well according to its deliverability.

Q Do we have any pools in southeastern New Mexico that are prorated based upon deliverability?

A Not to my knowledge.

Q How are all those pools in southeastern New Mexico prorated?

A The majority of pools are prorated on 100 percent acreage basis. There are a few pools, and they're not in the discussion of this hearing, that were assigned an allowable not to exceed a certain figure because they were retrograde reservoirs and they think that would be a top figure for any of the wells to produce.

Q For example, I think the Burton Flats Wolfcamp is a fixed allowable retrograde condensate reservoir, and that's not the subject of the hearing.

A I believe you're right, but I can neither confirm nor deny it.

Q What El Paso is proposing to do with the application does not alter the prorationing concept that the pools in southeastern New Mexico that are the subject of

this hearing are prorated on a straight acreage factor?

A We in no way at this hearing intend to change that mode of calculating allowables, no, sir.

Q All right, sir. Give me your definition, Mr. Kendrick, of what ratable take is.

A To me for ratable take to be used in any discussion that must defined to the type of proration formula that you are working with.

Q Would I have a different concept involved if I'm talking about ratable take from a prorated gas pool that is prorated on acreage as opposed to ratable take from a prorated gas pool that's prorated on deliverability?

A I would have a different concept, yes, sir.

Q All right, sir, tell me what the different concepts are.

A The concept on 100 percent acreage allocation means that every well gets to produce the same volume of gas, provided they are all nonmarginal wells.

For wells on deliverability allocation, every well gets to produce the same percentage of its allocation, percentage of its deliverability.

MR. KELLAHIN: I have no further questions of Mr. Kendrick.

MR. RAMEY: Any other questions of Mr. Kendrick?

QUESTIONS BY MR. STAMETS:

Q Mr. Kendrick, I presume you recall that the Commission made a short excursion with a deliverability formula in the Jalmat Pool in the late fifties?

A I think I recall that, yes, sir.

Q And you'd probably also recall that that didn't last very long.

A I know that it is now not on deliverability allocation, yes, sir.

Q So the formula for the allocation for the individual wells that you are talking about here today is basically the same formula that has been in effect since 1954, is that correct?

A Yes, sir.

Q And under this formula haven't there always been wells with widely varying potentials being prorated by straight acreage?

A Yes, sir.

Q So that's not any different.

A No, sir.

Q So you're simply saying let's go ahead with what we've got, you just need minor corrections.

A Yes, sir.

MR. STAMETS: That's all.

MR. RAMEY: Any other questions of Mr. Kendrick? He may be excused.

Do you have anything further, Mr. Nance?

MR. NANCE: Nothing further, Mr. Chairman, thank you.

MR. RAMEY: Do you have anything further, Mr. Carr?

MR. CARR: Nothing further, Mr. Ramey. I do have a closing statement.

MR. RAMEY: Okay, I think we'll accept statements at this time. I'll ask Mr. Carr and Mr. Nance to go last.

If there is anyone in the audience who's ready to make a statement at this time, why he may do so.

MR. ADAMS: Mr. Ramey, I'm Mark Adams. I represent Southern Union Exploration Company.

I think there are several points that need to be made here.

First of all, as Mr. Stamets has indicated, the New Mexico Supreme Court in the Jalmat decision in 1962 imposed rather severe limitations on the Commission's power to change a prorationing system.

The only way, as I read that case, the Commission can change a system is on the basis of findings that the total amount of gas reserves in a pool and the total amount of gas reserves under each producer's tract in the pool.

I think there's been no evidence at this hearing directed toward those two critical questions.

The second point is that, as I read the New Mexico statutes, again one that Mr. Stamets referred to this morning, they impose upon the Commission a duty to prorate effectively.

I think that the proceedings in this case and in the northwest New Mexico proration case earlier in the spring indicate that prorationing, because of changes in the market demand, is not working very well in New Mexico right now, and probably, as a result there is not effective prorationing.

The third point is that I think these two proceedings have indicated that is a very difficult way to try to develop a comprehensive, workable prorationing system. This is probably one case where the adversary system doesn't lend itself to the development of something that's going to work very well.

What we would propose in an effort to get around this stumbling block and meet the limitations imposed by statute and by the Jalmat decision, is a joint cooperative effort by industry and by the Commission, perhaps similar to that used by the New Mexico Oil and Gas Engineering Committee, to arrive at a prorationing system that everybody is more or less happy with and that will meet the legal requirements in that it will work.

I think the Engineering Committee pro-

vides some guidance in how this type of structure might be set up. I think that under the existing statutory framework the structure could work with the Commission reviewing, adopting, and then if finding it satisfactory, ratifying a proposal adopted by the industry-Commission group, and I would urge that the Commission and the other representatives of pipelines and producers here today give serious thought to such a group and perhaps how such discussion might be implemented.

MR. RAMEY: Thank you, Mr. Adams.

Any other statements? Mr. Mote.

MR. MOTE: Mr. Chairman and Commissioner.

I'm Clyde Mote from Amoco Production Company.

We believe that the existing proration rules with minor modifications should be adequate to handle the gas over-supply problem which exists in southeast New Mexico.

Failures in the system appear to have arisen from two facts. Number one, the overly optimistic nominations by the pipeline companies; two, a breakdown in the proration system where there are rapid swings in gas demand such as we had in 1982.

Specifically, there's too long a lag

period for a marginal well to be reclassified as nonmarginal.

We support the El Paso Natural Gas application for reclassification of all wells as nonmarginal to restart the prortion system in southeast New Mexico; however, in conjunction with the implementation of El Paso's application, pipeline companies must in some manner be held accountable for their future gas nominations in these fields.

In addition, we feel that Rule 18 of Order No. R-1670 should be revised to allow a marginal well to be reclassified as nonmarginal at the end of every three month classification period instead of the current twelve month proration period.

Also, we can sympathize with alleged instances of potential damages to drainage brought forward by Mr. Hartman's representative.

Neither El Paso's nor Hartman's notice of hearing gave notice of any potential changes to the individual pool rules and the allocation formula. The Hartman proposal does in fact constitute a collateral attack on Order R-1670.

Those fields in which an operator feels the allocation formula is not adequately protecting correlative rights should be addressed after legal notice at a hearing which will allow each affected party in that field to thoroughly analyze the ratable taking.

There are over 1000 wells, I believe the testimony said some 12,000 wells -- 1200 wells, in the 15 fields involved in today's hearing. We cannot remotely pretend to have adequately considered all the detailed reservoir data necessary to change the field rules in all prorated fields and allocation formulas in southeast New Mexico.

We concede there may be fields in which deliverability might have some relationship to the gas reserve distribution, but it is just as possible that more detailed studies of those and other fields would indicate acreage factors, or some combination of the two, might be more appropriate.

Now, Hartman, Mr. Hartman had the burden of proof in here to prove that his proposal would avoid waste and protect correlative rights. We would submit that the evidence clearly shows that waste would happen by virtue of it. Mr. Nutter admitted as much on the stand, that waste would occur in the shutting in of the low producing marginal wells. He also admitted, I think, very clearly that it would fail to protect the correlative rights. In fact, it appears that the only correlative rights which would be protected would be Mr. Hartman's wells.

Under cross examination by Mr. Ramey, Mr. Kendrick stated that in spite of pool rules which specified 100 percent acreage allocation formulas, El Paso was forced to take from prorted wells on a deliverability basis.

Mr. Kendrick also stated that in his opinion granting of El Paso's application would more nearly prorate these pools according to the existing pool rules.

The only logical ruling on these applications would be for the Commission to rule in favor of the El Paso application, allow operators to pursue changes to the allocation formulas on a field by field basis at a later hearing.

MR. RAMEY: Thank you, Mr. Mote.

MR. PICKENS: Bob Pickens, with Marathon Oil Company, and most of my statement was taken care of by the dismissal of the Indian Basin-Upper Penn this morning.

But I would like to say that it is Marathon's opinion that the recommendations by El Paso and Hartman in this hearing are only two of the methods dealing with gas prorationing problems caused largely by unusually low demands for gas.

We believe that the existing special rules for prorating gas contain the mechanism with which the Commission can affect these changes.

It is our suggestion that as a long range solution to the problems resulting from future low gas demand, prevent interim orders, such as the one proposed by El Paso here, possibly may consider it as a permanent solution to this problem, that the Comission attempt to speed up its

procedure for reclassification of marginal wells so that marginal wells can be more promptly reclassified as nonmarginal when the demands for gas is low.

We would support the position of Amoco that perhaps a three month period, or even shorter, if possible, would certainly help solve this problem.

Also, until a more rapid system of reclassification of marginal wells is operational, in the event the application of El Paso, or perhaps of Hartman, is approved on an interim basis in this instance, Marathon recommends that a proviso be made to such an order that would in effect say that any producer, I think this exists under the local field rules, with a well in a prorated pool subject to this order, shall be afforded an opportunity after notice of hearing, to show that such pool or such well, as the case may be, should be excluded from the operation of this order and that another basis for the allocation of gas production or for the protection of correlative rights should be made applicable to said pool or well.

We request something like that, a protective order, then people would feel free to come in and show specific instances where any rule that was adopted could be changed. Thank you.

MR. RAMEY: Thank you. Mr. Lyon?

MR. LYON: Members of the Commission, I'm Victor T. Lyon with Conoco in Houston.

Conoco is a substantial producer in four of the prorated gas pools under consideration today. We have studied those four fields in relation to the two proposals being offered at this hearing, as well as a continuation of the status quo.

Our conclusions for those four pools, Blinebry, Eumont, Jalmat, and Tubb, may or may not be applicable to the other eleven pools.

Conoco participated in the continuing development of rules for gas prortion embodies in Order No. R-1670. During the past several years increasing gas demand and declining deliverability has caused a very high percentage of the wells to be unable to produce their allocated share of the gas demand for the pool and thus be reclassified to marginal status.

This situation has progressed to the extent that there may have begun to be questions whether continued proration was needed.

We believe it is fortuitous that the system continued to work during this period, because it is now obvious that the system is needed. We would point out that during the past few years of high markets the process has gradually approached the situation where acreage allocation has necessarily given way to deliverability allocation, which is the inevitable result of all-out production conditions.

In a curtailment situation the reclassi-

fication should move in the other direction where curtailment operates on an acreage basis and the number of wells classified as nonmarginal should increase to accommodate the curtailment situation.

Our conclusion is that there are manyl wells in each of the four pools which in this curtailment period should be reclassified as nonmarginal so that curtailment can be accomplished under the established proration formula or 100 percent acreage.

In evaluating the two proposals before the Commission, El Paso's proposal, as modified to exempt a certain level of low capacity wells, will accomplish the objective described above, and would preserve the existing system and implement it as it was designed to operate.

On the other hand, the Hartman proposal completely abdicates Order No. R1670 and reverts the entire system to a deliverability allocation. This can be construed as nothing less than a collateral attack on Order R-1670 and as such, should not be countananced under this case as advertised.

If it is desirable to change the proration formula, an application to do so should be filed and argued on that basis. The attempt to accomplish this under a disguised proposal of fair share allocation should not be given any consideration.

Furthermore, Hartman's proposal to curtail all wells, even those very small wells which are barely

economic, flies in the face of universal conservation ethics, which promote protection of such wells so as to maximize recovery of natural gas, which is the prevention of waste, as required under the law.

MR. RAMEY: Thank you, Mr. Lyon.

Any other statements? Mr. Kellahin?

MR. KELLAHIN: Mr. Chairman, on behalf of those clients which have been identified in the record whom I represent, I would adopt Mr. Mote's closing statement. With regard to his observations and comments, we stand in opposition to Mr. Hartman's proposal. I think it undercuts the very fundamental conservation concepts that have been implemented by the Division over a course of many years.

We support the proposal submitted, as modified by El Paso, and we urge the Commission to adopt an order granting the El Paso application.

MR. RAMEY: Thank you, Mr. Kellahin. Representative Coll.

REPRESENTATIVE COLL: Mr. Chairman, my name is Max Coll.

I own a very small working interest and some small royalties from gas production in southeast New Mexico.

I'm trying to dispose of my

fair share of a working interest at a fair price,walked into what I consider to be an illegal and oppressive condition in trying to deal with pipeline companies in disposing of these interests.

Mr. Chairman, I favor Mr. Hartman's proposal because it allows production based upon deliverability. Texas Railroad Commission for years and years set oil allowables on number of days and I think that that system has been tried and tested and it works, and I would like to see gas proration in New Mexico go to that system. I think it would be much more fair, be easier to keep track of in the long run, be easier to set the number of days to allow a well to deliver whatever they will deliver.

And, Mr. Chairman, I think that the truly poor wells, the ones that are close to their economic limit, the ones that need to be produced all the time, could be allowed to do so, and I think that this system would lend itself to that, and I would heartily indorse it.

MR. RAMEY: Thank you.

MR. SORRENTINO: Mr. Chairman, I'm Tony Sorrentino for Gulf.

We'd just like to adopt the closing statement of Mr. Mote. We think it expresses our views, also. Thank you.

MR. RAMEY: Thank you. Mr. Lopez.

MR. LOPEZ: Mr. Chairman, Owen Lopez of the Hinkle Firm, representing Mesa and Bass.

We'd like for the record to show our opposition to the application -- the granting of El Paso's application on the basis we think it's a well disguised attempt to abrogate existing gas purchase contracts, specifically the take or pay provisions.

We feel that it is a major departure with one stroke of the pen to reduce the allowables so drastically and to convert such a great percentage of the marginal wells in New Mexico to a classification of nonmarginal.

The net result is that we believe the Commission should do nothing; should deny both applications and should let the system continue as it is.

I might add that we intend to, I'm sure El Paso's aware of this, enforce our prior contracts with them.

MR. RAMEY: Thank you, Mr. Lopez. Any other statements?

MR. CARR: May it please the Commission, you have before you today two proposals designed to deal with a problem which results from decline of the gas market in New Mexico.

El Paso proposes the reclassificatin of all wells in certain pools in southeastern New Mexico as nonmarginal, a test period, and then a reclassification,

whereby there will be many more nonmarginal wells and they will be able to avoid shutting in marginal wells in times of low demand.

What they propose will result in a substantial change for a limited number of wells and no change at all for many.

Doyle Hartman is proposing the classification of all wells are marginal on a temporary basis. This will let the purchasers take gas from all wells connected in these pools to their system under New Mexico statutes, under Oil Conservation Commission rules and regulation, which require ratable take. This will result in little change to the system.

The testimony today shows that somewhere between 95 and 98 percent of the wells will be affected by the application of El Paso and only 5 to 2 percent of the wells affected by Mr. Hartman's proposal.

El Paso's proposal to this Commission raises a very fundamental question: Can you, the Commission, grant an application that will cause major changes in the State's system for prorationing gas in the face of evidence that correlative rights will be impaired.

As we all know, correlative rights mean affording to each interest owner the opportunity to produce his just and fair share of the reserves in the pool. This is a concept that applies to each property and to each interest owner in each property. In the case before you,

the record discloses nothing on correlative rights advanced by El Paso except some general conclusions that correlative rights will be protected by their proposal. They run behind the special pool rules as the basis for the general conclusions, but they admit that they did not look at the wells in the individual pools to determine the effect of their proposal on correlative rights.

When asked about correlative rights they simply state, we assume the special pool rules will protect these rights.

They also state they didn't take the time to look into this on a pool by pool basis.

When asked about access to the marketplace and about affording operators an opportunity to produce into the pipeline, again they ran behind the special pool rules, and at the hearing in June, Mr. Kendrick even stated, and I quote: If there something in the pool rules that do not protect correlative rights, then that's not an issue with us today.

I submit that's one of the places where El Paso is wrong. Correlative rights is in issue here today. It's your statutory duty to protect these rights. If it is not an issue, then you cannot enter an order in this case.

If El Paso Natural Gas Company has not, and we submit they have not, shown that their proposal will protect correlative rights, then they, in pushing and ad-

vancing their application have failed to carry the burden of proof. Based on the record, we submit you cannot find that their proposal will protect correlative rights, and without this finding you do not have jurisdiction to enter a valid order.

But then they would have you believe that because these pools are prorated, this changes ratable taking and it changes correlative rights, and the requirements that are imposed on you to act to protect these rights. It isn't that easy a proposition.

Rules to prorate pools will stand. Ratable taking in various degrees can be superseded by prorationing orders, as long as the prorationing orders protect correlative rights and prevent waste. If they don't protect correlative rights and if they don't prevent waste, then a prorationing order is void and can be set aside because it fails to carry forward and meet statutory requirements, which are the prepared basis for your jurisdiction.

On this record we believe on the correlative rights issue alone you have no choice but to deny the application of El Paso Natural Gas.

And not only did El Paso fail to carry the burden as to correlative rights, there is evidence in this record which shows correlative rights in fact will be impaired by the El Paso application. Operators of nonmarginal wells will be discriminated. They will be cut back to the same level, and Mr. Kendrick testified that they will

bear the brunt of the curtailment.

Doyle Hartman did not just come forward in this proceeding and make general allegations about protection of correlative rights and prevention of waste. He presented specific examples which show what will happen in isolated situations.

Admittedly, he did not look at every well. There are certain time restraints and resource restraints on an operator like Mr. Hartman, but no evidence was presented to the contrary that would show the very problems outlined by Mr. Aycock in his testimony early in June are not indicative of what can and will happen on a broad and spread scale throughout southeastern New Mexico if you grant El Paso's application.

El Paso has admitted they didn't look at the impact on individual interest owners, but I think the evidence when you review the record will clearly show, based on the testimony of Mr. Aycock that drainage will occur from the best wells offsetting tracts if El Paso's application is granted and a reallocation of reserves will result.

Now let's look at ratable taking for a minute. Ratable simply does not mean equal. This term has no meaning unless it is referrable to some standard. It never means equal division.

El Paso proposes an equal division among nonmarginal wells of the gas that is to be produced above that volume produced by marginal wells. This simply is non-

ratable taking and it results in impairment of correlative rights.

El Paso has used two definitions of ratable taking in their presentation before you today. When they reduce demands, when they cut back between states, Mr. Kendrick stated they do it ratable. How do they do it? They cut back proportionly. So when they cut back the demand between the producing states they do it proportionately.

Mr. Kendrick testified they do it proportionately when they do it between pools. He testified they do it proportionately when they are curtailing production between wells in nonprorated pools. They do it proportionately when they are dealing with wildcat wells. They even have done it proportionately when dealing with marginal wells in the prorated pools at times that demands fall below the ability of the marginal wells to produce.

Yet they come forward with a proposal in which ratable take means cutting some wells by 90 percent and cutting an offsetting well not at all.

A few are asked under their proposal to bear the curtailment and approval of their application would simply be an act by this Commission approving nonratable taking and impairment of correlative rights.

When questioned about this, again they ran behind the special pool rules, and elsewhere in the case Mr. Kendrick testified, our proposal today does not have any

correlation to whether or not the pool rules in existance are protecting correlative rights.

I submit you can't run behind the pool rules and then testify that you haven't -- it doesn't even relate to correlative rights and expect you to accept that as sufficient evidence for a finding that correlative rights will be protected by the order you are being called upon to enter.

El Paso's application simply does deny equal access to the marketplace. It states over and over again, some wells can produce 90 to 100 percent of what they can deliver; others will be curtailed by 90 percent.

Next week you will be testifying before the Federal Regulatory Energy Commission and in that testimony this Commission will state that historically states have promoted conservation objectives and equitable market access by requiring production, or takes, on a ratable basis.

We submit you can't say that up in Washington next Wednesday and then turn around and deny the application -- I mean and grant the application of El Paso on the record that has been made in this case.

We further submit that the evidence in this record shows that El Paso's proposal will result in waste. It shows it will be-- we have shown and Mr. Aycock testified that reserves will be lost due to drainage from shut-in wells that when the demand comes back, assuming it

comes back, the market may not be there and reserves could be left in the ground, but in any event, the drainage away from wells that have capability of producing them and are artificially cut back because of El Paso's system, will result in waste.

Unfortunately, there are other problems with El Paso's proposal. In this case we've heard testimony about the evils of pipeline prorationing and yet after raising this red flag, no one was ever able to show what those problems might be, or how El Paso's proposal would act to resolve any of them.

Mr. Kendrick admitted on cross examination that their proposal will not equalize takes between wells and we will remain in the situation where the wells connected to the system with the greatest demand will in fact be the wells that produce more gas.

The evidence in this case shows that no matter if you grant El Paso's application, they will still purchase the same amount of gas in New Mexico; that they will be producing from wells and be able to obtain it at a lower price, and the result of their application will be lower proceeds to interest owners in New Mexico, including the State Of New Mexico.

Today Mr. Kendrick testified that reducing nominations of El Paso will reduce allowables. We have a situation here where if you grant this application El Paso will be able to reduce allowables in the State of New

Mexico.

He also has testified that he was aware of no other similar matter pending in any other jurisdiction. I would warn you that if you grant the application there is a potential that should other states act to require certain levels of purchasing of gas from wells connected to their system, not necessarily El Paso but any purchaser would be in a position where they could use New Mexico as a swing factor in their overall market, because there's one question that hangs over this whole case, and that is simply why is it that a pipeline cannot curtail or shut in or cut back a marginal well?

We've heard it's the policy of El Paso Natural Gas. We've also heard it's not based anywhere on statute.

I submit to you a month ago Mr. Aycock answered that question. He noted that El Paso had contract obligations that required it take allowables, the allowable, from certain wells connected to its system. If El Paso does not take the allowable connected to its system, then they still pay, and they, we submit, need relief under these contracts because of the decline recently in the gas market.

They are asking you to give this relief to them, even though it conflicts with your duties, your statutory duty to protect correlative rights.

They talk about concern for too many marginal wells and their proposal will result in lower allow-

able, and this in turn will result in relief to El Paso in the take or pay provisions of its contracts.

That evidence has been sitting on the table for a month. It hasn't been reputed. The reason it has not been reputed is it is correct and it is the reason we are here today.

Now Mr. Hartman is proposing a temporary change. We submit the change is realistic. It recognizes the realities of the current gas market and the state of depletion of the reservoirs in the State of New Mexico.

We submit that this proposal does not ask you to enter unwarranted, improper orders, and will not involve you in private contractual matters. It will be easy to administer. There will be some individual disputes. But El Paso's system will also require Commission attention and simply the ease of implementing one program or the other should not be the controlling matter when there is a clear cut issue of correlative rights standing before you.

It will not result in a new series of hearings to exempt wells from the 33 cutoff and either system is going to simply require that you -- either change is simply going to require that you devote some time to this matter and work the problem out. The extent of the volume of additional work cannot be anticipated, quantified by us any more than it can be by El Paso, but I think it is fair to say there is an additional work load coming, no matter which direction you elect to go.

We simply submit that El Paso -- that Hartman's proposal lets interest owners take ratably, it protects correlativer rights, and prevents waste. We believe it's feasible. Right now El Paso is balancing on a time basis, on a days on/days off wherever appropriate. We submit that Mr. Hartman's system could easily be worked into a computer program and that if the market turns around, it could be rescinded and go back to another market situation.

El Paso is proposing to reinstate the system which got us in the problem in the first place. You are asked by El Paso to let them do that which is convenient for the pipelines and provide relief to El Paso for certain contractual problems.

We ask you to deny that application and protect the correlative rights of Mr. Hartman and the interest owners, other people in the prorated pools in southeastern New Mexico.

If you grant El Paso's application on this record, we submit the decision is arbitrary; it's capricious, it's unreasonable, it's contrary to the evidence, and it's inconsistent with your statutory authority.

If, on the other hand, you grant Mr. Hartman's application, correlativer rights will be protected, waste will be prevented, and you will have entered an order which on this record can be defended; that is consistent with your statutory duty.

Mr. Hartman stands willing to work with

this Commission or with anyone who, in the future, who is concerned about trying to establish a system whereby curtailment of gas can be affected on an equitable basis in southeastern New Mexico.

If you enter an order in this case and decide to go with the Hartman proposal, we'd have no objection to 500 Mcf per month floor being set to protect certain minimum -- certain low capacity wells, but what we believe we have done with limited resources compared to other people here, is attempted to come forward, we have attempted to come forward and present to you an alternative whereby you can act within your statutory authority and at the same time can address the current gas market situation.

Thank you.

MR. RAMEY: Thank you, Mr. Carr. Mr. Nance.

MR. NANCE: Mr. Chairman, I think it's fairly clear that we have essentially a choice of philosophy in reaching a decision in this case. One is that the existing situation is not all that bad and a minor change to it will correct any problems that do exist, and that is, as we see it, the proposal that Hartman is making, the minor change being that of reclassification of a handful of wells.

The major change which underlies that is what El Paso takes issue with and El Paso feels is the part of Hartman's proposal which causes it to be invalid as a

collateral attack on the existing proration rules in R-1670.

We feel that El Paso's proposal is a reasonable one. We did not set it forth as the only answer to the problem, but one that we felt would appropriately address the problem. We feel that it is not correct and not protection of correlative rights to be curtailing marginal wells. We feel that reclassification of most wells, if not all wells, the nonmarginal, will allow this problem to be alleviated, and that the system, if started again on this basis, is the one that has been proven over the years to be the correct one, the one based historically on the best evidence, and for which there is no -- no substantial evidence to justify changing the rules, particularly in this circumstance.

We feel that the notice of the hearing did not contemplate abbrogation of the existing rules, which we see is what Hartman is essentially proposing.

We recognize the distinct difference between philosophies of having acreage allocation and deliverability allocation for establishing allowables. We did not propose that one is better than the other; that one is fairer than the other. What we do propose is that the existing rules provide 100 percent acreage allocation and that there has been no correct means of attempting to change that proration formula, and that El Paso's proposal is, in this particular circumstance, is the most appropriate way, if not perfect, at least the best way to address the problem

at this point.

That's all. That's all I have.

MR. RAMEY: Thank you. Mr. Nance, did you ever offer Exhibits Eighteen and Nineteen?

MR. NANCE: I may not have, and El Paso would like to offer those exhibits.

MR. RAMEY: They will be accepted.

MR. PEARCE: And in addition to that, Mr. Chairman, for clarification of the record, which, gee, it would be nice if nobody ever used again, I would ask that the representative of El Paso diagram the material on the blackboard and mark that as Exhibit Number Twenty and submit that subsequent to the hearing and provide one to all counsel of record in this proceeding, please.

MR. RAMEY: I would request that at least Mr. Carr and Mr. Nance prepare suggested orders for the Commission, and anyone else who desires to do, why, they may do so.

Does anyone else have anything further to add in Cases 7858 and 7905?

If not, the Commission will take the cases under advisement and this hearing is adjourned.

(Hearing concluded.)

C E R T I F I C A T E

I, SALLY W. BOYD, C.S.R., DO HEREBY CERTIFY that the foregoing Transcript of Hearing before the Oil Conservation Division was reported by me; that the said transcript is a full, true, and correct record of the hearing, prepared by me to the best of my ability.

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