

1 STATE OF NEW MEXICO
2 ENERGY, MINERALS AND NATURAL RESOURCES DEPARTMENT
3 OIL CONSERVATION COMMISSION

4 IN THE MATTER OF THE HEARING CALLED
5 BY THE OIL CONSERVATION COMMISSION FOR
6 THE PURPOSE OF CONSIDERING:

COPY

7 REOPENED APPLICATION OF THE NEW Case No. 14255
8 MEXICO OIL CONSERVATION DIVISION, THROUGH
9 ITS ENVIRONMENTAL BUREAU CHIEF, FOR ADOPTION
10 OF AN AMENDMENT TO 19.15.39 NMAC ADDING NEW SECTIONS
11 TO BE CODIFIED AT 19.15.39.9 AND 19.15.39.10 NMAC
12 ADDRESSING SPECIAL PROVISIONS FOR SANTA FE COUNTY
13 AND THE GALISTEO BASIN, SANTA FE, SANDOVAL AND
14 SAN MIGUEL COUNTIES, NEW MEXICO

15 DE NOVO AMENDED APPLICATION OF ENERGEN Case No. 13957
16 RESOURCES CORPORATION TO AMEND THE COST
17 RECOVERY PROVISIONS OF COMPULSORY POOLING ORDER
18 NO. R-1960, TO DETERMINE REASONABLE COSTS, AND FOR
19 AUTHORIZATION TO RECOVER COSTS FROM PRODUCTION OF
20 POOLED MINERAL INTERESTS, RIO ARRIBA COUNTY,
21 NEW MEXICO

22 REPORTER'S TRANSCRIPT OF PROCEEDINGS
23 COMMISSIONER HEARING

24 BEFORE: MARK E. FESMIRE, Chairman
25 JAMI BAILEY, Commissioner
WILLIAM C. OLSON, Commissioner

May 27, 2009

Santa Fe, New Mexico

26 This matter came on for hearing before the New
27 Mexico Oil Conservation Commission; MARK E. FESMIRE,
28 Chairman, on Wednesday, May 27, 2009, at the New Mexico
29 Energy, Minerals and Natural Resources Department, 1220
30 South Saint Francis Drive, Room 102, Santa Fe, New
31 Mexico.

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23 ALSO PRESENT:

24 Florene Davidson

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1 CHAIRMAN FESMIRE: At this point we will
2 call the Wednesday, May 27th regularly-scheduled meeting
3 of the New Mexico Oil Conservation Commission to order.
4 The record should reflect that Commissioners Bailey,
5 Olson and Fesmire are all present. We, therefore, have a
6 quorum. The first order of business before the
7 Commission this morning is the adoption of the minutes of
8 the April 15th, 2009, special Commission meeting. Have
9 the Commissioners had a chance to review those minutes?

10 COMMISSIONER BAILEY: Yes, I have, and I
11 move that we adopt them.

12 COMMISSIONER OLSON: Second.

13 CHAIRMAN FESMIRE: All those in favor
14 signify by saying aye.

15 Let the record reflect that the minutes of the
16 April 15th meeting were unanimously adopted by the
17 Commission, signed by the Chairman and conveyed to the
18 secretary.

19 At this point we probably need to talk about
20 scheduling. The next item on the agenda is Case Number
21 14255, the Galisteo Basin matter. The Commission has
22 decided, in order to facilitate scheduling this morning,
23 that we will address the Galisteo Basin first, then we
24 will address the Energen case, and then we'll go into
25 deliberations on the "Pit Rule". So if you are brave

1 enough to want to venture how long it will take to
2 address those three issues, you can plan your day
3 accordingly.

4 The first item before the Commission this
5 morning is Case Number 14255, the reopened Application of
6 the New Mexico Oil Conservation Division, through its
7 Environmental Bureau Chief, for adoption of an amendment
8 to 19.15.39 NMAC adding new sections to be codified at
9 19.15.39.9 and 19.15.39.10 NMAC addressing special
10 provisions for Santa Fe County and the Galisteo Basin,
11 Santa Fe, Sandoval and San Miguel Counties. May we have
12 the entry of appearance for the attorneys in that case,
13 please?

14 MS. MACQUESTEN: Mr. Commissioner, my name
15 is Gail MacQuesten. I'm here representing the Oil
16 Conservation Division.

17 CHAIRMAN FESMIRE: Ms. MacQuesten, are you
18 the only attorney in this case?

19 MS. MACQUESTEN: Now I am.

20 CHAIRMAN FESMIRE: Are you prepared to
21 begin?

22 MS. MACQUESTEN: Yes, I am. Mr.
23 Commissioner, I have two witnesses, Theresa Duran-Saenz
24 and Daniel Sanchez. Ms. Duran-Saenz is here to provide
25 information on notice. You should have in front of you

1 Exhibit 48, which is our Affidavit of Notice. It was not
2 provided with the prehearing statement but it was
3 provided this morning. I would move for admission of the
4 affidavit. However, if you have questions about notice,
5 Ms. Duran-Saenz is here to testify to answer your
6 questions.

7 CHAIRMAN FESMIRE: Have the Commissioners
8 had a chance to review the --

9 COMMISSIONER BAILEY: Yes, I have, and I
10 have no questions.

11 COMMISSIONER OLSON: I have no questions.

12 CHAIRMAN FESMIRE: Neither do I. We will
13 go ahead and admit OCD Exhibit 48 in Case Number 14255.

14 (Exhibit 48 was admitted.)

15 MS. MACQUESTEN: In that case, I would
16 call Daniel Sanchez.

17 CHAIRMAN FESMIRE: Mr. Sanchez, would you
18 proceed to the stand, please? Would you raise your right
19 hand?

20 (The witness was sworn.)

21 CHAIRMAN FESMIRE: Ms. MacQuesten before
22 we start, can you bring the Commission up to speed of
23 where we are and why we're doing this in this case?

24 MS. MACQUESTEN: Certainly. The Division
25 had proposed special rules for the Galisteo Basin and the

1 remainder of Santa Fe County. After the case was
2 concluded and the Commission entered into its
3 deliberations, it made the determination that the rules
4 should apply only to the Galisteo Basin and not the
5 remainder of Santa Fe County.

6 At that time the Commission asked the OCD to
7 provide a legal description of the Galisteo Basin so that
8 the rule could be limited to just that area. The OCD
9 provided a legal description and also copies of the maps
10 that we used to create that legal description. The
11 information was put out for comment. We did not receive
12 any comments or proposed modifications for the legal
13 description. However, the Commission order indicated
14 that the Commission would like to have this brought to a
15 hearing so that testimony could be taken on the legal
16 description and any comments or questions could be raised
17 at that time.

18 CHAIRMAN FESMIRE: At this point -- and
19 we're not scheduling right now -- is there anyone here
20 who has any comments on the proposed legal description?
21 Ms. MacQuesten, why don't you proceed?

22 DANIEL SANCHEZ

23 Having been first duly sworn, testified as follows:

24 DIRECT EXAMINATION

25

1 BY MS. MACQUESTEN:

2 Q. Would you please state your name for the
3 record?

4 A. Daniel Sanchez.

5 Q. And what is your title?

6 A. I am the Compliance and Enforcement Manager
7 for the OCD.

8 Q. Are you here to introduce and explain the
9 exhibits pertaining to the legal description for the
10 Galisteo Basin?

11 A. Yes, I am.

12 Q. Could you turn to what's been marked as
13 Exhibit 45?

14 A. Okay.

15 Q. What is this exhibit?

16 A. This is an exhibit of the Galisteo Basin and
17 watershed as defined by the State Engineer's office.

18 Q. Where did you obtain this map?

19 A. From the State Engineer's office. Darrio
20 Rodriguez, who is now retired from the State Engineer's
21 office, put together the database that came up with these
22 coordinates, and Manuel Pasquel from the State Engineer's
23 office put together the maps and provided those maps to
24 us.

25 Q. Is this map pulled from the database of the

1 State Engineer's office?

2 A. Yes, it is.

3 Q. The map has a dotted line boundary. What does
4 that indicate?

5 A. That is the boundary of the Galisteo Basin
6 watershed.

7 Q. Is the State Engineer the entity that defines
8 the Galisteo Basin watershed?

9 A. Yes, they are.

10 Q. What are the small squares on the map?

11 A. Those are the sections within that area.

12 Q. And what are the numbers within each section?

13 A. They indicate the range within each section.

14 Q. What are the blank areas that are marked,
15 "MS"?

16 A. Those are areas that have not been surveyed
17 and in this case, they're land grants.

18 Q. Could you turn to what's been marked as
19 Exhibit 46, please?

20 A. Okay.

21 Q. What is this exhibit?

22 A. This, as well, is a blown-up version of that
23 map, and this shows the sections. The sections are
24 penciled in for the entire area.

25 Q. Could you turn to what's been marked as

1 Exhibit 47, please?

2 A. Okay. Exhibit 47 is the legal description of
3 the entire basin, both sides.

4 Q. And this is by section, township and range?

5 A. Yes, it is.

6 Q. How were the unsurveyed areas described?

7 A. They were described by the surveyed sections
8 around those areas that were not surveyed.

9 Q. Why not just name the land grants involved?

10 A. Some of the land grants were only partly
11 within the Galisteo Basin.

12 Q. Now, in paragraph A(1) and A(2), some of the
13 section numbers are highlighted. Why is that?

14 A. Those highlighted numbers are additional areas
15 or descriptions of additional areas within Sandoval and
16 San Miguel Counties that we originally didn't see in our
17 version of the original map. When the State Engineer
18 gave us the coordinates for the new map, those little
19 sections, those areas, actually came out, so we decided
20 to put those in, every single piece that we could, within
21 that map -- within the boundaries of the watershed.

22 Q. To be clear, those highlighted sections were
23 not included in the original description that was
24 provided with the application?

25 A. No, they were not.

1 Q. Did the OCD receive any comments on the
2 proposed legal description?

3 A. No, we did not.

4 Q. Did the OCD receive any proposed
5 modifications?

6 A. No.

7 MS. MACQUESTEN: I would move for
8 admission of Exhibits 45 through 47.

9 CHAIRMAN FESMIRE: Is there any objection
10 to the admission of Exhibits 45 through 47? They'll be
11 so admitted.

12 (Exhibits 45 through 47 were admitted.)

13 MS. MACQUESTEN: That concludes the OCD's
14 presentation.

15 CHAIRMAN FESMIRE: Thank you. Do you have
16 anything to add?

17 MS. MACQUESTEN: Just that the reason we
18 provided this level of detail on the map for you and in
19 the legal description was so that we could give you the
20 raw data to fashion the legal description however you see
21 fit to fashion it.

22 And, also, I wanted to point out that you can
23 put the legal description of the Galisteo Basin in
24 several different locations within the proposed rule.
25 Again, we're leaving it to the Commission to decide how

1 to do it. But the NMAC structure would allow you to take
2 this description and put it in subsection 7, which is the
3 area of Part 39 that's reserved for definitions, because
4 it is a very lengthy legal description. So it would be
5 possible that you can either build it into the rule or
6 you could put it in the definition section of that part.

7 CHAIRMAN FESMIRE: Ms. MacQuesten, thank
8 you very much. At this time the Commission will take
9 Case Number 14255 under consideration with the intention
10 of deliberating at the end of the -- towards the end of
11 the meeting today. Is that acceptable? Thank you very
12 much. Thank you, Mr. Sanchez.

13 The next case before the Commission is Case
14 Number 13957, the amended application of Energen
15 Resources Corporation to amend the cost recovery
16 provision of Compulsory Pooling Order No. R-1960, to
17 determine reasonable costs, and for the authorization to
18 recover costs from production of pooled mineral interests
19 in Rio Arriba County, New Mexico. Are the attorneys
20 present for that case?

21 MR. HALL: Yes, sir.

22 MR. BRUCE: Yes, sir.

23 CHAIRMAN FESMIRE: May we have an entry of
24 appearance?

25 MR. HALL: Mr. Chairman, Commissioners,

1 Scott Hall, Montgomery & Andrews law firm, Santa Fe,
2 appearing on behalf of Energen Resources Corporation, and
3 I have one witness this morning.

4 MR. BRUCE: Mr. Chairman, Jim Bruce of
5 Santa Fe appearing in association with Candice Lee of the
6 Sommer, Udall law firm, and we are representing the
7 Estate of Joseph A. Sommer, the Joseph A. Sommer
8 Revocable Trust and JAS Oil and Gas Company, LLC. We'll
9 refer to these during the hearing. And I have one
10 witness.

11 CHAIRMAN FESMIRE: Will the witnesses
12 please stand? Would you raise your right hands?

13 (The witnesses were sworn.)

14 CHAIRMAN FESMIRE: Mr. Hall, do you have
15 an opening statement?

16 MR. HALL: Very briefly, Mr. Chairman.
17 This case involves a well that was acquired by Energen
18 Resources in 1997. The well was originally drilled in
19 1961 and was the subject of a compulsory pooling order
20 issued by the Commission then.

21 CHAIRMAN FESMIRE: And signed by Governor
22 Mechem, I saw.

23 MR. HALL: Yes. It was the full
24 Commission, so very authoritative. As you will see in
25 our exhibits, we have a copy of the order. It is

1 something of a bare-bones order and does not contain the
2 modern-day provisions that the Division uses now in its
3 compulsory pooling orders.

4 When the pooling order was issued in 1960 --
5 1961, rather, among the interest owners was Joseph
6 Sommer, who's a local attorney in town. The well was
7 produced for a number of years by Energen's predecessors.
8 It was drilled by Southern Union Production Company,
9 taken over by Union Texas, Unicon, acquired by Meridian,
10 eventually went to Burlington, and Energen Taurus at the
11 time acquired this well as part of a package of wells
12 from Burlington in 1997.

13 Production of the well, as we'll demonstrate
14 to you, we find the well is long paid out. With the
15 decline in the gas market in the 1990s, interest owners
16 in the well were advised that the operator at the time,
17 Meridian, would discontinue sales on behalf of those
18 other interest owners and revise to make arrangements for
19 the disposition of their own shares of gas. Some did,
20 some did not. That led to the well getting out of
21 balance. Some interest owners were over-produced, others
22 were under-produced.

23 That led to the situation we have today. It
24 led to a dispute with Mr. Sommer over how gas was to be
25 accounted for and disposed of and at what price. The

1 dispute went on for a number of years, and I think
2 Energen did the right thing in a situation like that. I
3 think any operator is obliged to try to take reasonable
4 efforts to work out their differences with their
5 nonoperator well partners. Energen did that. It simply
6 didn't succeed. So Energen has availed itself of the
7 administrative processes of the Division and now the
8 Commission.

9 What Energen is asking this Commission to do
10 is, as I said, one, provide us with a modern-day
11 compulsory pooling order which allows for the recovery of
12 costs, including overhead and supervision costs, and we
13 are also asking for authorization to market the gas on
14 behalf of the nonmarketing owner so that those costs can
15 be recovered out of that owner's share. If you do not do
16 that, Mr. Commissioners and Ms. Bailey, it is our view
17 that the operation of the Compulsory Pooling Order is
18 thwarted. The operator is bearing the expenses for all
19 of the other interest owners and does not have the
20 opportunity to recover those costs.

21 That's our situation today. We'll provide you
22 with proof of the dispute, and I think we can show you a
23 way out of this dispute, as well, as the testimony
24 progresses. Thank you.

25 CHAIRMAN FESMIRE: Mr. Bruce, would you

1 like to make an opening statement or would you like to
2 reserve it?

3 MR. BRUCE: Just very briefly, Mr.
4 Chairman. As Mr. Hall noted, this well was drilled
5 almost 50 years ago, and for decades, about three and a
6 half decades, the operator or successor operator sold the
7 gas and accounted to the interest owners and paid the
8 interest owners, the force pooled interest owners.
9 Energen ceased paying Sommer and has kept a gas balancing
10 account since then.

11 Energen did advise the owners to market their
12 own gas. However, we'll have testimony that, in the
13 past, when Sommer has asked to take the gas, Energen
14 refused, and so we're at a dilemma. We certainly think
15 that since -- under the orders Energen is selling 100
16 percent of the gas, and out of that, it has to pay
17 Sommer's one-eighth royalty interest as an unleased
18 mineral interest owner, and it also has to take out of
19 those proceeds the operating costs. What is the issue
20 with simply accounting to Sommer and paying that same
21 interest, their working interest?

22 Certainly the Division under the pooling
23 statute has the authority to make an order that will
24 afford to the owner or owners of each interest in the
25 unit the opportunity to recover or to receive, without

1 unnecessary expense, his just and fair share of the oil
2 and gas. And we think that merely making Energen under
3 the order -- since it is already selling 100 percent of
4 the gas and accounting and paying all interest owners is
5 fair and reasonable.

6 And as I pointed out in my prehearing
7 statement, certainly if the Sommer interest was
8 unlocateable, Energen would have to do that under the
9 current form of pooling orders. They are required to put
10 the unlocateable owners' share of revenues in a bank
11 account. And I don't think that gas balancing accounts
12 or gas balancing credits suffice as putting money in a
13 bank account.

14 And nowadays, when there's many changes -- it
15 used to be one thing 40 years ago when you had a few big
16 operators in the San Juan Basin who were there for
17 decades, you could always find those operators. And
18 Energen is a big company, but there's always changes of
19 operators. What if the well goes dry? Who is liable for
20 all that stuff?

21 Some of the under-production that Sommer is
22 accounted for might have been under the last operator. I
23 don't know. But under a force pooling order, I think the
24 Division should make the operator sell that gas and
25 account to the force pooled interest owners. Thank you.

1 CHAIRMAN FESMIRE: Thank you, Mr. Bruce.

2 Mr. Hall, would you like to call your first witness?

3 MR. HALL: Yes, sir. At this time, Mr.

4 Chairman, we would call Paul Rote to the stand.

5 CHAIRMAN FESMIRE: Mr. Rote, please spell
6 your last name for us.

7 THE WITNESS: R-o-t-e.

8 CHAIRMAN FESMIRE: And you've been
9 previously sworn in this case?

10 THE WITNESS: Yes, sir.

11 PAUL ROTE

12 Having been first duly sworn, testified as follows:

13 DIRECT EXAMINATION

14 BY MR. HALL:

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

16 A. Paul Rote.

17 Q. Mr. Rote, where do you live and by whom are
18 you employed?

19 A. I live in Birmingham, Alabama, and I'm
20 employed by Energen Resources Corporation.

21 Q. What do you do for Energen?

22 A. I'm the general manager of land.

23 Q. Have you previously testified before the
24 Commission and had your credentials accepted as a matter
25 of record?

1 A. Yes, I have.

2 Q. Would you briefly give these Commissioners a
3 summary of your educational background?

4 A. I have a BS in psychology, MBA in finance, and
5 I've worked as an oil and gas landman for the past 26 or
6 seven years.

7 Q. Does your area of responsibility include the
8 San Juan Basin?

9 A. Yes, it does.

10 Q. Are you familiar with the lands and the well
11 that are the subject of this application?

12 A. Yes.

13 MR. HALL: At this point, Mr. Chairman, we
14 would offer Mr. Rote as a qualified expert petroleum
15 landman.

16 CHAIRMAN FESMIRE: Is there any objection?

17 MR. BRUCE: No.

18 CHAIRMAN FESMIRE: Mr. Rote is so
19 accepted.

20 Q. (By Mr. Hall) Mr. Rote, would you provide a
21 brief explanation of what it is Energen is seeking by its
22 application today?

23 A. We're asking the Commission to clarify the
24 cost recovery provisions under the old 1961 pooling order
25 to allow us to deduct both the costs and expenses

1 associated with the production and sale of that
2 production attributable to a nonmarketing working
3 interest owner. Basically, we're asking for an update of
4 the 1961 pooling order.

5 Q. Why don't you give the Commissioners the
6 background on the drilling and the operation of the
7 Martinez #1 Well?

8 A. This well was drilled, as Mr. Hall mentioned,
9 in 1961 by Supron. It was completed as a producer.
10 Supron operated this well for some period of time from
11 1961 to 1982, and they sold the property to Union Texas.
12 Union Texas thereafter operated it. In 1990, the well
13 was acquired by Meridian. Meridian was acquired by
14 Burlington. We acquired, as Taurus, our previous
15 operator name, in 1997, this well amongst many others in
16 a large property acquisition from Burlington. In 1998,
17 we changed our name from Taurus Exploration to Energen
18 Resources Corporation.

19 Q. We should establish for the record, this well
20 was drilled --

21 A. Pictured Cliffs.

22 Q. -- the Pictured Cliffs Formation, in the
23 southwest quarter of Section 2, Township 25 North, Range
24 3 West as dedicated to the well?

25 A. Yes, sir.

1 Q. Let's look at Exhibit Number 1. Can you
2 identify that for us, please?

3 A. Exhibit Number 1 is a copy of the original
4 1960 pooling order covering this well.

5 Q. Is Exhibit Number 2 a copy of Order Number
6 R-1960-A which was issued by the Division in this matter
7 last year?

8 A. Yes, sir, it is.

9 Q. Let's look at Exhibit 3. What does that show
10 us?

11 A. Exhibit 3 is from our accounting systems. It
12 shows the ownership of the well and it shows two types of
13 wells called decks. First, on the top of the page, is a
14 hundred percent revenue deck which shows the total 100
15 percent interest of all the parties involved, what type
16 of interest they have, what their decimal fraction in the
17 well is. The deck that is below is called a revenue
18 deck. What that is, it's an inflated deck which allows
19 us -- it's a mechanism that accounting uses, oil and gas
20 accountants use, to inflate the decimals in those cases
21 where the operator is not selling -- does not own 100
22 percent of the gas that's being marketed.

23 It's a mechanism to make sure that the
24 proceeds that are received by the purchasers are applied
25 properly to make sure that all the owners are paid

1 appropriately. So there will be some difference between
2 100 percent revenue deck and an inflated decimal deck,
3 and that's what this exhibit shows.

4 Q. For the benefit of the Commissioners, when we
5 refer to the Sommer interest, is that interest now owned
6 under the name of JAS Oil & Gas Company?

7 A. Yes, it is.

8 Q. That is reflected on the revenue deck?

9 A. Yes.

10 Q. On Exhibit Number 3, except for the JAS
11 interest, are all of the other interest owners under
12 lease or an operating agreement?

13 A. All owners are either leased or have signed a
14 Joint Operating Agreement, with the exception of JAS.

15 Q. When the 160 acres was originally pooled,
16 which unleased mineral interest owners were the subject
17 of that pooling order?

18 A. It was Josie Gallegos and Amadito Valdez and
19 the Estate of Luis Martinez and Joseph Sommer.

20 Q. Was the Thomas F. McKenna interest pooled, as
21 well?

22 A. Yes, it was.

23 Q. Since that time have the Josie Gallegos,
24 Amadito Valdez and Luis Martinez interests been made
25 subject to an operating agreement?

1 A. Yes. Josie Gallegos, Amadito Valdez and Luis
2 Martinez all signed a Joint Operating Agreement.

3 Q. When Taurus acquired this property in 1997,
4 did it acquire the file materials for the well from the
5 predecessor operators?

6 A. Yes, it did.

7 Q. Are some of those file materials included as
8 exhibits today?

9 A. Yes, they are.

10 Q. When Taurus and Energen assumed operations of
11 the well in 1997, were the takes and entitlements of all
12 the interest owners in the well in balance at that time?

13 A. No, they were not.

14 Q. With respect to the Sommer's JAS interest, was
15 it over-produced or under-produced?

16 A. Their interest was over-produced according to
17 the information we received by the amount of 1,031 MCF,
18 over-produced.

19 CHAIRMAN FESMIRE: May I ask a question?
20 How did it get over-produced?

21 THE WITNESS: I don't know. And I can
22 speculate, but I really can't answer that question with
23 certainty. It may have been -- I'm just speculating
24 here -- that the operator, Burlington, was itself
25 over-produced and accounted for the Sommer interest in

1 the same manner that they accounted for their own
2 over-production and attributed his working interest
3 percentage to the over-produced volumes, but I'm just
4 speculating here.

5 CHAIRMAN FESMIRE: Could you say that
6 again? The Commissioner didn't hear everything.

7 THE WITNESS: I'll try. As I said, I
8 don't know for sure. We just have that old gas balance
9 and statement that arrived with the rest of the files.
10 The fact that Mr. Sommer was over-produced at that time,
11 I can only speculate without certainty, and that
12 speculation would include the possibility that Burlington
13 itself was over-produced as the operator and attributed
14 Mr. Sommer's interest in that same over-produced account
15 and gave him some share of their over-production.

16 CHAIRMAN FESMIRE: Mr. Hall, proceed. I'm
17 sorry.

18 Q. (By Mr. Hall) Mr. Rote, are you familiar
19 with the customs and practices of the industry in
20 producing and operating wells generally?

21 A. Yes.

22 Q. Is it the custom and practice of the industry
23 to implement gas balancing where takes and
24 entitlements -- I'm sorry -- where less than all the
25 interest owners in a well have not sold their gas?

1 A. Yes.

2 Q. Can you give the Commissioners a brief
3 explanation of how balancing works? How is that
4 implemented?

5 A. If a party is not selling their gas, it has to
6 be accounted for. A hundred percent of the production
7 out of the wellbore has to be accounted for. The only
8 way to do that is to credit those proceeds or debit those
9 proceeds against the gas imbalance account. So that if I
10 had not sold my gas, I would be subject to a gas
11 balancing account which would credit me for the gas that
12 I had not sold, and that will build up over time for the
13 period of time that I am not selling.

14 At some point down the road you would settle
15 out that account, typically under a gas balancing
16 agreement, which would account for that imbalance, and
17 typically the under-produced party would be paid proceeds
18 based on historical prices at completion of the well or
19 some time previous to that if they would negotiate that
20 issue.

21 CHAIRMAN FESMIRE: So the balancing occurs
22 on the historical price they would have sold if they had
23 an agreement?

24 THE WITNESS: Typically you'd see that in
25 gas balancing statements. It's quite common.

1 CHAIRMAN FESMIRE: It doesn't just
2 occur -- "We owe you X MCF at this price"?

3 THE WITNESS: Well, you have to assume
4 that that owner has never sold their share of the gas or
5 that share of the gas was never sold. So the only option
6 you have is at depletion of the well, then to cash settle
7 the account. And that cash settlement will typically be
8 based on the actual prices received by the selling party,
9 historical prices, and you pay the under-balanced owner
10 that amount at that time.

11 Q. We will hear the terms today "takes" and
12 "entitlements" and "makeup." Does entitlement reflect an
13 interest owner's ownership in a share of gas?

14 A. Yes. That's the share he's entitled to.
15 That's his ownership share, yes.

16 Q. "Takes" reflects actual movement of gas
17 attributable to an account; is that right?

18 A. Yes.

19 Q. Now, when an under-produced party, someone who
20 hasn't been selling its gas, comes to sell its gas in
21 order to make up its under-produced position, is it
22 common for that interest owner's account to be -- his
23 entitlement to be inflated?

24 A. By inflated --

25 Q. Increased.

1 A. Yes, it is. Typically, what you would see in
2 our gas balancing agreement would be to give the
3 under-produced party the ability to sell his share plus
4 the additional percentage, inflated number. Typically
5 that would be on the order of say 25 to another 50
6 percent. So, for instance, if I had a 10 percent
7 interest in a well and I was under-balanced and under a
8 gas balancing agreement, I told the operator I wanted to
9 sell my share, I could invoke the gas balance agreement
10 and say I want an additional 50 percent over my 10
11 percent. Therefore, I would now be entitled to 12 and a
12 half percent -- my math is not very good -- of -- 15
13 percent -- I'm sorry -- I'd be entitled to 15 percent --

14 CHAIRMAN FESMIRE: I thought lawyers were
15 bad mathematicians.

16 A. So I'm entitled to take an additional amount
17 attributable to my interest until that gas imbalance is
18 built back down to zero.

19 Q. As we work our way through the exhibits today
20 that came from the predecessor operator's files, can we
21 get an idea of how those previous operators began to
22 implement gas balancing as the life of the well
23 progressed?

24 A. I'm sorry. Run that by me again.

25 Q. When we go through some of the documents that

1 came from the predecessor operator's files, can we gain
2 an understanding of how balancing was implemented for
3 this well?

4 A. Yes, I think so.

5 Q. From your review of some of those documents,
6 does it appear that the operators up through the time
7 Meridian operated the well were selling gas on behalf of
8 the other joint working interest owners who had not made
9 arrangements to dispose of their share?

10 A. Yes, it appears so.

11 Q. Look at Exhibit 4. Can you identify this for
12 us?

13 A. Exhibit 4 is a letter from Meridian to the
14 joint working interest owners dated 1992, where they are
15 letting the nonoperators know that Meridian would no
16 longer be selling their gas on their behalf and it's
17 asking them to take responsibility for selling their own
18 gas.

19 Q. So Meridian was telling its nonoperators to
20 make arrangements to sell their own gas after that point?

21 A. Yes.

22 Q. Let's look at Exhibit 5. Could you identify
23 that, please?

24 A. Another letter from Meridian dated September
25 28, 1995, where they are again telling the nonoperators

1 that Meridian will cease taking their gas as of December
2 1st of that year, and that after that date, Meridian will
3 no longer allocate any gas to their working interest
4 shares.

5 Q. And by that same letter, did Meridian ask to
6 be advised by its nonoperators of their plans for
7 disposing of their gas by November 1st, 1995?

8 CHAIRMAN FESMIRE: Mr. Hall, before he
9 answers that, Mr. Rote, is there any way to know how Mr.
10 Bruce's client elected under the March 1992 letter?

11 THE WITNESS: No, sir, nothing comes to
12 mind.

13 CHAIRMAN FESMIRE: From the accounting, we
14 can assume that they elected not to participate in the
15 Meridian sales?

16 THE WITNESS: I'd have to say yes, that
17 they -- I don't believe Meridian continued to sell its
18 gas.

19 MR. HALL: Mr. Chairman, we'll be able to
20 connect up in subsequent exhibits to address that.

21 CHAIRMAN FESMIRE: Okay. I apologize.

22 Q. (By Mr. Hall) Again, did Meridian ask to be
23 notified by November 1st, 1995, of the nonoperators'
24 plans for disposing of their share of production?

25 A. Yes.

1 Q. Did the letter also indicate that if the
2 nonoperators had not made arrangements to sell their gas,
3 they would be made subject to gas balancing?

4 A. That's correct.

5 Q. Did the files that Energen acquired for the
6 Martinez Well also include copies of Division orders?

7 A. Yes, it did.

8 Q. Let's look at Exhibit 6. Is Exhibit 6 a copy
9 of the Division order for the Pictured Cliffs Formation
10 in Martinez #1 Well?

11 A. Yes, it is.

12 Q. This particular one is signed at the bottom by
13 Joseph A. Sommer; is that correct?

14 A. Yes, sir.

15 Q. Page 2 of that reflects percentage interest
16 for his ownership; is that right?

17 A. Yes.

18 MR. HALL: May I approach, Mr. Chairman?

19 CHAIRMAN FESMIRE: You may, sir.

20 Q. (By Mr. Hall) I've handed out what is a
21 highlighted version of Exhibit 6, but, Mr. Rote, if we
22 could direct our attention to page 1, the second full
23 paragraph on that page, if we bear in mind the March 17,
24 1992 and September 28, 1995 market election notices from
25 Meridian for Exhibits 4 and 5, does -- look at the

1 language on the Division order. Does it provide for the
2 operator to make payment until written notice of
3 termination is received?

4 A. Yes, it does.

5 Q. Let's look at Exhibit 7. Can you identify
6 that?

7 A. Exhibit 7 is a transfer order under which Mr.
8 Sommer transferred his interest to the Joseph A. Sommer
9 Revocable Trust.

10 Q. If we turn to page 2 of that transfer order --
11 we've provided the Commissioners with highlighted copies
12 of that -- like the original Division order, if we look
13 at the top paragraph on page 2, does that transfer order
14 also authorize payment for production proceeds until one
15 party provides written notice to the other?

16 A. Yes.

17 Q. That language is in there. Let me ask you,
18 Mr. Rote, is the Sommer royalty interest on pay status
19 now?

20 A. Yes, it is.

21 Q. Let's look at Exhibit Number 8. Would you
22 identify that, please?

23 A. This is a letter sent from Taurus dated
24 February 13, 1998, from our Manager-Joint Interest
25 Accounting to all working interest owners, telling them

1 that, if they prefer, we would JIB net them, basically
2 account for their share by sending them a net check after
3 expenses were deducted on a monthly basis, rather than
4 sending them an invoice for those expenses and a separate
5 revenue check.

6 Q. Let's explain to the Commissioners what JIB
7 net means.

8 A. JIB stands for Joint Interest Billing, and JIB
9 net means that I would send one check, which would be
10 proceeds minus their share of operating expenses. I'm
11 netting out their joint interest billings.

12 Q. So is it accurate to say by this letter Taurus
13 Energen was notifying its nonoperators that they had an
14 option to be netted out for their expenses; is that
15 right?

16 A. Yes. It was sent to many small owners.

17 Q. And the alternative is what, if they are not
18 to be netted out?

19 A. The alternative is that we would send them a
20 bill each month and we'd also send them a revenue check.
21 The bill would be for their share of the joint interest
22 billings, the lease operating expenses. We'd send that
23 out and wait for them to send us back their check for
24 their share of those operating costs.

25 Q. Now, do monthly lease operating expenses

1 continue to accrue for all of the working interest owners
2 of a well even in those instances where a working
3 interest owner is not marketing its gas?

4 A. Yes.

5 Q. Those costs don't go away, do they?

6 A. No, they do not.

7 Q. Is it Energen's practice to continue to
8 invoice working interest owners for their proportionate
9 share of lease operating expenses whether they market or
10 not?

11 A. Yes.

12 Q. And has the Martinez #1 Well paid out?

13 A. Yes. I believe it paid out in November 1968.

14 Q. Can you tell the Commissioners generally what
15 comprise monthly lease operating expenses, just
16 generally?

17 A. Generally, it would be electricity, vehicle
18 expense, supervision, labor, chemicals, overhead, et
19 cetera.

20 Q. Let's turn to Exhibit 9. Would you identify
21 that? What does that tell us?

22 A. This was a letter sent October 26, 1998, from
23 one of our joint interest accountants to Mr. Sommer
24 directly, letting him know that we had not been receiving
25 his JIB payments. We also offer, if he doesn't want --

1 we wanted to purchase his ownership in the well if he
2 cared to have us do an evaluation of the value of that
3 well.

4 Q. Did it appear that this accounts receivable
5 letter in October of 1998 triggered a series of
6 correspondence between Mr. Sommer and Energen?

7 A. Yes, it did.

8 Q. Let's look at Exhibit 10. Can you identify
9 this, please?

10 A. It's a letter from Mr. Sommer, January 5th,
11 1998, and he's basically asking why he's being charged
12 expenses for a well he thought was shut in, apparently.
13 We have evidence to show that it was not being shut in.

14 Q. Among other things, was Mr. Sommer objecting
15 to supervision and overhead charges?

16 A. Yes, he was, such items as company labor,
17 supervision and vehicle expenses.

18 Q. Let's turn to Exhibit 11. Could you identify
19 this, please?

20 A. Another letter from Mr. Sommer dated June 15th
21 of '01. He had received a gas balancing statement from
22 us and was responding to the receipt of that statement
23 and responding to JIB bills. He continues to object
24 being charged for overhead and joint interest billing
25 expenses.

1 Q. If we turn to page 2 of that letter, does the
2 highlighted language reflect his objection to being
3 charged for overhead?

4 A. Yes, it does.

5 Q. Look at Exhibit 12. Identify that, please.

6 A. A subsequent letter from Mr. Sommer dated
7 February 13, 2002. Basically, it's another letter
8 further objecting to joint interest billing statements
9 and, in particular, COPAS overhead charges. He asked for
10 information of gas and balances in that letter.

11 CHAIRMAN FESMIRE: Could you elaborate on
12 COPAS?

13 THE WITNESS: Yes, sir. COPAS is a
14 standard industry petroleum accounting society
15 organization that is responsible for formulating
16 accounting policies and procedures for the industry.

17 CHAIRMAN FESMIRE: So that will be on the
18 record. That description will be on the record.

19 THE WITNESS: Okay.

20 Q. (By Mr. Hall) In view of the ongoing efforts
21 of Mr. Sommer to obtain an explanation for balancing
22 statements and the joint interest billings, did Energen
23 make any effort to try to communicate with him?

24 A. Yes, we did.

25 Q. Let's look at Exhibit 13. Would you identify

1 that and explain that?

2 A. Thirteen is a letter dated March 11, 2002,
3 from Energen authored by Mr. Kirk Flowers, who's the
4 Director of Joint Interest Accounting Department. He's
5 responding to Mr. Sommer's previous February 13th letter
6 and tries to -- attempts to explain gas balancing, how it
7 works and what happens if an owner does not market their
8 share of the gas.

9 Q. And did he also try to explain Energen's joint
10 interest billings for monthly lease operating expenses
11 and producing well overhead charges?

12 A. Yes, he did.

13 Q. Basically, what did he say in that regard?

14 A. That a nonmarketing interest owner -- that the
15 joint interest billings continue to accrue even though
16 that owner is not selling their gas.

17 Q. Did Mr. Flowers try to explain that the
18 imbalance position for the Sommer interest was a
19 situation that was inherited from Burlington when you
20 acquired the well?

21 A. I believe so.

22 Q. Did Energen also offer to correct any errors
23 in the gas balancing statement?

24 A. Yes, we did.

25 Q. Let's turn to Exhibit 14. Can you identify

1 this, please?

2 A. Another letter from Mr. Sommer dated August
3 16, 2002.

4 Q. Was he responding to Mr. Flowers' earlier
5 letter?

6 A. Yes, he was.

7 Q. If you look at the first paragraph on page 5
8 of the August 16, 2002 letter, was it Energen's
9 understanding that Mr. Sommer was asserting that as of
10 December 1, 1995, when Meridian gave its notice to
11 nonoperators, that the operator was without any further
12 authority to sell his gas?

13 A. That's apparently what it says, that we
14 would -- our interpretation was that Mr. Sommer claimed
15 that we did not have the authority to assume title of
16 that gas and sell it.

17 Q. And would termination of that authority be
18 consistent with the provisions of the Division order and
19 the transfer order that we showed the Commission earlier?

20 A. Yes, it was.

21 Q. In the second and third paragraphs also on
22 page 5 of that same letter, did it appear that Mr. Sommer
23 was asserting that pursuant to the pooling order, Energen
24 had the authority to sell only those volumes attributable
25 to the Sommer interest that were sufficient to cover the

1 real costs of production?

2 A. Yes, that's what he said.

3 Q. Did it also appear that Mr. Sommer was not
4 only objecting to lease operating expenses, but he was
5 also objecting to bearing his share of fixed production
6 overhead, as he says it?

7 A. Yes.

8 Q. If we turn to page 6 of that letter, I
9 highlighted some language there. What is it that you
10 understand that Mr. Sommer was contending? Was he simply
11 reasserting that the operator was without authority to
12 sell gas on behalf of the other interest owners?

13 A. Yes, that's right.

14 Q. Did you understand him to say that Energen
15 could not sell its own gas, and his own gas was being
16 marketed?

17 A. Yes. Throughout this Mr. Sommer asserted that
18 we do not have the right to sell his gas. We -- I'm
19 stuck here.

20 Q. Was he also disputing the operator's authority
21 to try to recover operating costs in a balancing
22 situation from a nonmarketing interest owner whose
23 interest was being balanced?

24 A. Yes, it appeared so.

25 Q. He was having a problem with that concept?

1 A. (Witness nods head.)

2 Q. Overall, Energen's communications with Mr.
3 Sommer, was it Energen's understanding that Mr. Sommer
4 was asserting that Energen had no authority to sell the
5 Sommer Trust working interest share of the gas to balance
6 its production?

7 A. That was our interpretation, yes.

8 Q. Let's look at Exhibit 15. Could you identify
9 that, please?

10 A. Another letter from Mr. Sommer dated September
11 3rd, 2002, which is where he's apparently threatening
12 legal action on a class action basis over these issues.

13 Q. If we look at page 4 of Exhibit 15, we've
14 highlighted some language there, the third full
15 paragraph. Does this passage summarize the position
16 which Energen understood Mr. Sommer was taking?

17 A. Yes, it does.

18 Q. And he was interpreting the operation of the
19 Compulsory Pooling Order; is that right?

20 A. Yes, it appeared so.

21 Q. And, again, he was asserting that the order
22 did not allow for the production and sale of gas over and
23 above what was necessary to reimburse the operator for
24 the expense of producing the gas?

25 A. Yes. The understanding here was that he was

1 saying that we would only be allowed to sell that small
2 portion of the gas that would only cover his share of
3 joint operating expenses and nothing more.

4 Q. Let's address that concept for a minute. Is
5 it practicable or even possible for Energen or any
6 operator to market only a large enough share to recoup
7 lease operating expenses on a month-to-month basis?

8 A. I don't think it would be practicable to do
9 nor possible to do. I cannot estimate what the upcoming
10 expenses are going to be and sell just that specific
11 portion of gas from the wellbore to account for that
12 share of those expenses.

13 Q. This concept would require an operator to know
14 in advance what the next month's expenses would be and
15 then schedule that much gas accordingly?

16 A. I would think so, yes.

17 Q. Is it often the case that an operator will
18 experience unanticipated expenses, variable costs?

19 A. Certainly, workovers, et cetera.

20 Q. Let's look at Exhibit 16. Would you identify
21 that, please?

22 A. It's a letter dated September 25th, 2002. I
23 was the author to it. This was an attempt to respond to
24 Mr. Sommer's concerns and try to reach some sort of
25 accomodation that would be acceptable to he and Energen.

1 Q. So you continued to try to work with Mr.
2 Sommer; is that right?

3 A. Yes.

4 Q. Can you summarize for the Commission what you
5 were proposing to do in this case?

6 A. We offered to sell his share of the gas,
7 market his share of the gas. We would allow him to
8 increase his percentage under a gas balancing type
9 arrangement whereby his interest would increase by
10 another 40 percent over his 8.33 percent. I offered to
11 settle out his gas imbalance for a negotiated price. I
12 offered to withhold or deduct his COPAS overhead charges
13 for previous gas -- account for his previous outstanding
14 JIB invoices. We also offered to buy him out under an
15 industry-accepted economic evaluation of the value of the
16 well.

17 Q. In your view did you make clear that Energen
18 expected that Mr. Sommer would be required to pay his
19 share of monthly lease operating expenses and overhead
20 charges going forward?

21 A. For future flows, yes, and he would still be
22 responsible for his share of the joint interest billings,
23 including COPAS overhead rates.

24 Q. Is Exhibit 17 the response you received to
25 your letter?

1 A. Yes, it is.

2 Q. And is that a letter from Mr. Sommer dated
3 October 15, 2002?

4 A. Yes, it is.

5 Q. And I believe we could address this quickly by
6 looking at page 5. Was it clear -- was it made clear by
7 Mr. Sommer that he was rejecting your offer?

8 A. Very clear.

9 CHAIRMAN FESMIRE: Mr. Hall, under Exhibit
10 16, there are two letters on consecutive days.

11 MR. HALL: It should be Exhibit 17.

12 THE WITNESS: That second letter is a gas
13 marketing agreement that we offered for him to sign if he
14 elected to allow us to sell his gas. It was an
15 attachment to the first letter.

16 CHAIRMAN FESMIRE: Okay.

17 Q. (By Mr. Hall) Let's address that since the
18 Chairman raised that. Mr. Sommer did not execute your
19 gas marketing letter agreement?

20 A. No, he did not.

21 Q. Again, back to the response to your letter
22 from Mr. Sommer, he made clear that he was rejecting your
23 proposal; correct?

24 A. Yes.

25 Q. Was he disputing any authority for Energen to

1 undertake gas balancing at all?

2 A. Yes, he did.

3 Q. Based on your experience and understanding of
4 industry custom and practices, what is the practical
5 effect of that position where someone asserts an absence
6 of authority to implement gas balancing when one or more
7 interest owners in a well have failed or refused to
8 market their share of production?

9 A. Well, it would -- I would have to shut the
10 well in, because I would not be allowed -- if I'm not
11 able to sell a small working interest owner's share of
12 gas, I cannot flow that well. It would result in having
13 to shut it in, because I wouldn't be able to segregate
14 his share of the gas out of that well flow.

15 Q. And would shutting in the well be consistent
16 with the custom and practice of the industry?

17 A. No.

18 Q. Balancing is; is that correct?

19 A. Yes, it is.

20 Q. In your opinion, would the correlative rights
21 of the other interest owners in the well be violated if
22 the well were forced to be shut in in such a situation?

23 A. Yes, it would.

24 Q. Let's turn to Exhibit 26. Skip forward to
25 that. Would you identify that for us, please?

1 A. This is a geological map that shows the
2 Pictured Cliffs producing wells with the Martinez well
3 centered with a one-mile radius around it.

4 Q. Does the Martinez #1 Well compete with other
5 offsetting Pictured Cliffs wells?

6 A. Yes, it does.

7 Q. Turn back to Exhibit 18.

8 CHAIRMAN FESMIRE: Back to 18?

9 MR. HALL: Back to 18. I'm sorry to skip
10 around.

11 Q. (By Mr. Hall) Would you identify Exhibit 18
12 for us?

13 A. Yes. Exhibit 18 is a front page of a Joint
14 Operating Agreement between Energen's operator and covers
15 the McCroden Well, the McCroden C #1 Well, which has also
16 been executed by -- I don't have the execution.

17 Q. For the record, is Exhibit 18 simply the cover
18 page from that operating agreement for the McCroden C #1
19 Well?

20 A. Yes, it is.

21 Q. And coincidentally, does it cover the west
22 half of the same section we're talking about here?

23 A. Yes, it does.

24 Q. What formation is the McCroden C 1?

25 A. I believe that's Mesaverde.

1 Q. Now, attached to that cover page is Exhibit E.
2 What is Exhibit E?

3 A. Exhibit E is a form of gas balancing agreement
4 that is more or less standardized, used in the industry.
5 This is a particular agreement that our company prefers
6 to use.

7 Q. So parties participating in wells under Joint
8 Operating Agreements, is the custom and practice of the
9 industry to implement gas balancing embodied in Exhibit
10 E?

11 A. Yes, it is.

12 Q. It's largely reflected by the terms of Exhibit
13 E?

14 A. Yes, that's correct. I'll add that most every
15 Joint Operating Agreement will have a gas balancing
16 agreement attached as part of the contract by and between
17 the operator and the nonoperating parties.

18 Q. Now, by the way, are the Sommer interests
19 committed to the McCroden C #1 Well?

20 A. Yes, they are.

21 Q. Is that by virtue of this operating agreement?

22 A. Yes, it is.

23 Q. Let's turn to Exhibit 24. Skip forward to
24 Exhibit 24. Can you identify this for the record?

25 A. Yes, sir. This is a copy of our January 2009

1 gas balance statement that Energen sends to the balancing
2 parties on a regular basis. It shows that the Sommer gas
3 imbalance as of January 2009 was minus 8,378 MCFs.

4 Q. Now, that 8,378 MCF under-produced position,
5 is that net of any royalty interests that would have been
6 paid to the Sommer interest?

7 A. That is a gross figure that would -- needs to
8 be deducted by the one-eighth royalty share. So it is
9 not a net figure. It is a gross figure.

10 Q. If we applied a one-eighth factor to that
11 8,378 MCF, would that yield approximately 7,331 MCF?

12 A. Yes.

13 Q. That's the current imbalance attributable
14 to --

15 A. Current net imbalance.

16 Q. -- attributable to the Sommer --

17 A. Attributable to the Sommer interest, yes.

18 Q. Could you explain to the Commissioners what is
19 the most administratively-efficient means for Energen as
20 operator of this well to administer the under-produced
21 volumes attributable to the Sommer interest?

22 A. Through gas balancing.

23 Q. How will you specifically implement gas
24 balancing for the Sommer interest?

25 A. Each month that -- they have an entitlement

1 amount and a sales amount. And, for instance, their
2 January statement shows that their entitled share of the
3 flow for that month was 57 MCFs. There were no sales
4 because we are not marketing their gas and, therefore,
5 their imbalance grew by an additional 57 MCF.

6 Q. Does Energen ask the Commission to enter an
7 order authorizing Energen to sell all of the working
8 interest share of production attributable to the
9 under-produced interest and to seek appropriate
10 reimbursement for lease operating expenses and
11 supervision charges?

12 A. Yes, we do.

13 Q. You're not asking for authorization to sell
14 only a portion of the Sommer working interest necessary
15 to cover expenses?

16 A. No. No, we are not.

17 Q. Is it more administratively efficient for
18 Energen to sell all of it?

19 A. Yes. It's more administratively efficient for
20 us to sell the entire flow of gas from the wellbore.

21 Q. So if authorized to do so, the Sommer interest
22 will be placed in what's called makeup status; is that
23 correct?

24 A. Yes, that's correct. If --

25 Q. And will the -- go ahead.

1 A. If we sell the Sommer interest, we would sell
2 his share, his working interest share, and that share
3 would then be increased by some percentage and that would
4 work off the gas imbalance until it got down to zero.

5 CHAIRMAN FESMIRE: Without an operating
6 agreement or gas balancing agreement, what should that
7 increased percentage be?

8 Q. Earlier you had proposed 40 percent in your
9 Exhibit 16. Are you proposing to inflate the Sommer
10 entitlement by 40 percent?

11 A. We are more than willing to increase it by 40
12 percent, yes.

13 Q. Let's look at Exhibit 23. Can you identify
14 this and then tell us what this shows the Commission?

15 A. This is a detail of account activity
16 pertaining to the Joseph Sommer/JAS interest which
17 represents what their share of monthly joint interest
18 billings were from the date of our acquisition to
19 current. So this is what their share of LOE expenses,
20 JIB expenses, on a monthly basis would be attributable to
21 their working interest share.

22 Q. For what period of time does this cover?

23 A. It covers August of 1997 through April of
24 2009.

25 Q. So that's the period Energen acquired the

1 well?

2 A. Yes, it is.

3 Q. If we turn to the last page of that exhibit,
4 does it show us a grand total of outstanding lease
5 operating expenses and charges due from the Sommer
6 interest?

7 A. Yes. It's in the amount of \$8,975.35.

8 Q. Let's turn back now to Exhibit 22. Could you
9 identify that for the Commissioners, please?

10 A. This is a copy of the monthly joint interest
11 billings that are sent to the JAS Oil and Gas Company for
12 the Martinez Well. For instance, this first one of April
13 2009 shows that the gross LOE expenses for that month
14 were \$1,057.78. The JAS share of that was \$88.14.
15 Behind that is a detail page which lays out -- lists in
16 more detail what those specific lease operating expenses
17 entail.

18 Q. Now, for all of the detail that comprises
19 Exhibit 22, what period of time is covered?

20 A. It runs from April 2009 back to September
21 2008.

22 Q. Now, among other things, is Energen asking the
23 Commission to amend the Compulsory Pooling Order to allow
24 it to charge the current prevailing producing well
25 supervision overhead rate?

1 A. Yes, we are.

2 Q. Let's turn to the second page of Exhibit 22.
3 Is the overhead rate, the current overhead rate,
4 reflected on there?

5 A. Yes, it is.

6 Q. What is that rate?

7 A. It's \$866.16.

8 Q. What portion of that is attributable to the
9 Sommer interest?

10 A. \$72.18.

11 Q. And is this rate in line with the permissible
12 COPAS bulletin rates and adjustments?

13 A. Yes.

14 Q. Does Energen also ask the Commission to have
15 the order reflect that the supervision rate may be
16 adjusted periodically in accordance with the COPAS
17 bulletin?

18 A. Yes, we do.

19 Q. Let's look at Exhibit 21. Could you identify
20 this, please?

21 A. Yes. This is a matrix that is published by
22 COPAS on a yearly basis which shows how to escalate the
23 COPAS overhead charges. What it does is -- for instance,
24 in this case, the Joint Operating Agreement in question
25 was dated in 1984. If you look to the right-hand side of

1 that page under 1984 and carry it all the way down to the
2 year 2009, you would see the number 247.36. What that
3 is, is that allows you to escalate the original 1984
4 COPAS overhead rate in the Joint Operating Agreement of
5 \$350 by a factor of 247.36 percent, which would take you
6 to the current COPAS overhaed charge of \$866 and some-odd
7 cents.

8 Q. What is the significance of the 1984 date?

9 A. That is the date of the Joint Operating
10 Agreement covering the Martinez Well in which the
11 accounting procedure allowed for a \$350 per month COPAS
12 overhead rate in 1984.

13 CHAIRMAN FESMIRE: Was Sommer a party to
14 that?

15 THE WITNESS: No.

16 Q. (By Mr. Hall) Let's look at Exhibit 20 very
17 briefly. First of all, can you identify Exhibit 20?

18 A. Exhibit 20 is a report that was run out of
19 Energen's accounting system. What it represents was to
20 see in those cases where Energen is not the operator,
21 where Energen is the nonoperating party, what other
22 operators are charging us for monthly COPAS overhead
23 rates. So the column to the far right would be COPAS
24 overhead rates that we are being charged by other
25 operators. What it attempted to do was establish that

1 the current COPAS rates that we are charging under the
2 Martinez Well are within the upper and lower limits of
3 these common charges.

4 Q. So the Commissioners can go through this
5 exhibit and get an idea of what other operators are
6 charging for, for instance, Pictured Cliffs wells in the
7 area?

8 A. That's right.

9 Q. It would help them understand whether the
10 overhead rate that Energen is requesting is in line with
11 prevailing rates in the area?

12 A. That's the intent. Yes.

13 Q. And a couple of examples, if you look at the
14 very first entry on page 1, it seems to show a PC Well
15 operated by Black Hills, and what's the overhead rate for
16 that well?

17 A. \$514.27.

18 Q. If you turn to the third page -- I'm sorry.
19 Let's turn to what's marked as page 12. At the very
20 bottom there is a Starr #1 PC Well operated by Dugan.
21 Does that show an overhead rate of \$852 per month?

22 A. Yes, it does.

23 Q. If we turn, as an example, to page 19, one
24 more example, at the bottom of that page there's a
25 reference to the ConocoPhillips State Com C 5 PC Well,

1 and it shows an \$1,800 overhead rate; is that right?

2 A. Yes, that's what it shows. Yes.

3 Q. Let's turn briefly to Exhibit 19. Can you
4 identify this for us?

5 A. This is a more detailed level breakdown of
6 various lease operating expenses associated with this
7 particular well. For instance, page 1 would show that
8 that was a charge to the Sommer interest for company
9 labor. In August of 1997, his share of that was \$33. So
10 page 1 represents all charges from the period running
11 from August of '97 through -- well, it runs through page
12 3 -- through April of '09. Those would be the monthly
13 charges for that particular breakout for company labor,
14 lease operating expenses. On page 3 you would see the
15 same accounting for Sommer's share of company supervision
16 charges running through that same period of time.

17 CHAIRMAN FESMIRE: Are these actual
18 charged amounts or are they COPAS?

19 THE WITNESS: No, these are charged
20 amounts. . These are not COPAS. If you turn to page --
21 COPAS will be a separate line item, and you find COPAS
22 on --

23 CHAIRMAN FESMIRE: So these are direct
24 costs and the COPAS are overhead costs; right?

25 THE WITNESS: That's correct. Yes, sir.

1 Q. (By Mr. Hall) Are these costs broken out by
2 category for the period that Energen operated the well?

3 A. Yes.

4 Q. This shows costs on 100 percent basis?

5 A. I'm not sure. Yes, it's 100 percent basis.

6 Q. Mr. Rote, are the historic and current monthly
7 lease operating expenses and the overhead rates being
8 charged by Energen reasonable?

9 A. We believe so.

10 Q. In fact, Energen is now bearing 100 percent of
11 operating expenses and overhead; is that right?

12 A. Yes, we are.

13 Q. There's no reason for Energen to charge itself
14 unreasonable expenses?

15 A. No, there is not.

16 Q. It doesn't make sense. Mr. Rote, let me
17 finish up with you. Were Exhibits 1 and 3 through 24 and
18 26 compiled by you from materials maintained in the files
19 of Energen in the ordinary course of business or were
20 they otherwise compiled by you at your direction and
21 control?

22 A. Yes, they were.

23 CHAIRMAN FESMIRE: Mr. Hall, would you
24 give us that list again?

25 MR. HALL: Exhibits 1, 3 through 24 and

1 26. I would ask the Commission to take administrative
2 notice of Exhibit 2, which is a copy of Order Number
3 R-1960-A, and Exhibit Number 25, which is Rule 414 and
4 Order Number R-8361, which led to the adoption of Rule
5 414 by the Commission in 1996. Exhibits 27 and 28 are
6 our notice affidavits and Affidavit of Publication. We
7 move the admission of all of those exhibits and that
8 concludes our direct of this witness.

9 CHAIRMAN FESMIRE: What did you say
10 Exhibit 22 was? You asked us to take administrative
11 notice.

12 MR. HALL: No. Two and 25.

13 CHAIRMAN FESMIRE: Two and 25. Is there
14 any objection to the admission of 1, 3 through 24, 26, 27
15 and 28, or for the Commission to take administrative
16 notice of 2 and 25?

17 MR. BRUCE: No objection.

18 CHAIRMAN FESMIRE: Those exhibits --
19 Exhibits 1 and 3 through 24 and 26, 27 and 28 will be
20 admitted, and the Commission will take administrative
21 notice of Exhibits 2 and 25. Is that the conclusion of
22 your direct of Mr. Rote?
23 (Exhibits 1, 3 through 24, 26, 27 and 28 were admitted.)

24 MR. HALL: Yes, sir.

25 CHAIRMAN FESMIRE: Why don't we take a

1 15-minute break and reconvene at 10:40 back here.

2 (A recess was taken.)

3 CHAIRMAN FESMIRE: We're back on the
4 record in Case Number 13957, a continuation. The record
5 should reflect that all three Commissioners are present.
6 There is, therefore, a quorum present, that we were about
7 to begin Mr. Bruce's cross-examination of Mr. Rote.

8 Before you begin that, I want the record to
9 reflect that I was wearing a tie when we started. It's
10 gotten warm. And anybody that feels like taking a tie or
11 jacket off, feel free. Mr. Bruce?

12 MR. BRUCE: Can I go out and put my shorts
13 on?

14 CHAIRMAN FESMIRE: Let's not go that far.

15 CROSS-EXAMINATION

16 BY MR. BRUCE:

17 Q. Mr. Rote, you testified at the original
18 hearing in this matter, did you not?

19 A. Yes, I did.

20 Q. And I'm going to try to minimize the
21 questions, kind of group them into two categories, the
22 over-production from -- the under- and over-production
23 from the well and the overhead rates. First off, with
24 respect to the overhead rates, did you check to see what
25 the Ernst and Young overhead rates are for wells of this

1 depth in Rio Arriba County?

2 A. Yes, we did.

3 Q. What were they?

4 A. This is their annual publication put out by
5 Ernst and Young. It covers a fixed rate overhead survey
6 for the years 2008 and 9. For those that may not be
7 familiar with it, it's broken out by state and by well
8 depth in New Mexico. Depending upon the well depth, you
9 would have a minimum, an average, a median and a maximum
10 COPAS overhead rate per the Ernst and Young survey.

11 For this particular type of well, I'll give
12 you the median rate or whichever one you prefer to hear.
13 For a well depth of 5,000 to 10,000 feet -- for the
14 record, I'm not sure of the well depth for this well, but
15 I believe it would fall within 5 to 10,000 feet. The
16 median COPAS overhead rate would be \$550.

17 Q. Thank you. And I asked you this the last
18 time. This is a gas well; correct?

19 A. Yes, sir.

20 Q. Is it producing any water?

21 A. I don't believe so.

22 Q. And I think you indicated this well has never
23 been shut in. It's continuously produced?

24 A. According to the State production records, it
25 appears to have not been shut in. It appears to have

1 been continuously produced.

2 Q. When you testified, oh, about a year and a
3 half ago -- and I believe the Examiner's order, the
4 Division order, incorporated what you requested as to
5 overhead rates, and it was \$350 a month or something like
6 that -- I won't hold you to that number -- from 1983 or
7 '84. It escalated under the documents that you presented
8 at hearing today. And you testified that at that point,
9 the overhead rates should be \$748 per month; is that
10 correct?

11 A. I believe that's correct.

12 Q. Why now a year and a half later would it be
13 \$866? That's a 16 percent increase in little over a
14 year.

15 A. Without having a calculator, what we, as a
16 company, did, was to apply the rates as per that COPAS
17 Exhibit Number 21. I think if we were to do math, Mr.
18 Bruce, you'd find that \$746 rate a year and a half or so
19 ago, applying this matrix to it, would raise it up to the
20 current 866.

21 Q. If you turn to your Exhibit 20, Mr. Rote, Mr.
22 Hall had you go through this, and if my language is
23 objectionable to Mr. Hall, he can object, because I'm
24 going to do the same thing he did. You used -- on page
25 19 of this list, you chose the very bottom well on that

1 list, a Pictured Cliffs well operated by ConocoPhillips
2 to show an overhead rate of some \$1,800 per month;
3 correct?

4 A. Yes.

5 Q. And if I can use the phrase, that's cherry
6 picking. And let me do the same. What is the rate for
7 the well immediately above that?

8 A. \$382.

9 Q. If you go back to page 12, which Mr. Hall also
10 had you look at, you used the well operated by Dugan at
11 the bottom for \$852 a month. What are the rates for the
12 Pictured Cliffs well immediately above that?

13 A. \$514.

14 Q. If you turn back to page 1 of this list and go
15 through the first few pages, aren't the operating costs
16 for PC wells consistently in the -- except in one or two
17 instances. I picked out about a dozen of them here where
18 the operating rates are generally 4 to 500 bucks a month.

19 A. Yes. That's what you see. If I may add,
20 there's a multitude of reasons as to why those rates may
21 diverge to the extent that that report shows. As a for
22 instance, you may have had a recent JOA signed, say, last
23 year, and the parties negotiated a monthly COPAS overhead
24 rate at that point in time of \$350. Using the matrix, on
25 the COPAS matrix, that would have raised that to 400 and

1 some-odd dollars, perhaps. So a lot of these rates are a
2 function of the vintage and the age of the Joint
3 Operating Agreements.

4 Q. And with respect to the monthly charges
5 assessed against Sommer or any other person in his place
6 or situation, there are a couple of elements. One is
7 this monthly overhead rate, and you're asking, whatever
8 it is, 800 and some dollars a month; correct?

9 A. Yes.

10 Q. And the other charges are the monthly lease
11 operating expenses?

12 A. That's correct.

13 Q. Now, in the last hearing there was also
14 testimony that you were charging -- Energen was charging
15 a \$73 a month management fee. Is Energen still charging
16 that?

17 MR. HALL: I'll object to that. It's
18 beyond the scope of his testimony in this case. Unless
19 you want to show him transcript testimony that shows
20 that, I think that's improper.

21 CHAIRMAN FESMIRE: Mr. Bruce was alleging
22 it was prior testimony. Isn't he able to go into this
23 witness's prior testimony on this subject?

24 MR. HALL: In the Division hearing. But
25 we'd like to see the transcript to see if that's what was

1 said. We don't know that that's what was said.

2 CHAIRMAN FESMIRE: Maybe Mr. Bruce should
3 rephrase his question. I'll overrule the objection, but
4 you can change the form of the question.

5 Q. Was there testimony at the prior hearing that
6 a -- and if I'm wrong on the amount -- but I believe it
7 was --

8 CHAIRMAN FESMIRE: Mr. Bruce, are you
9 talking about this witness's prior testimony?

10 MR. BRUCE: Yes, sir.

11 CHAIRMAN FESMIRE: Phrase the question
12 that way.

13 Q. (By Mr. Bruce) Mr. Rote, did you testify or
14 agree that there was a \$73 per month management fee being
15 assessed against the Sommer interest?

16 A. Mr. Bruce, I have absolutely no recollection
17 of having testified to that. I have no knowledge of
18 management fees being assessed to Mr. Sommer.

19 Q. Thank you, Mr. Rote. Let's first go to your
20 Exhibit 3, Mr. Rote. Looking at this division of
21 interest, before I ask a few more questions on some other
22 exhibits, in the first table, the top part of the page,
23 which interest owners are not being paid on production?

24 A. Currently, Amadito Valdez is not being paid
25 because he is not marketing his share of gas. Josie

1 Gallegos, she is being credited into a suspense account.
2 She is deceased. So the only people, person, party, that
3 is not being paid would be JAS and Amadito Valdez.

4 Q. Now, Mr. Valdez -- now when I look at this,
5 your testimony was that the sixth person up from the
6 bottom, JAS Oil and Gas Company, its royalty interest
7 that is being paid?

8 A. Yes, it is.

9 Q. Has it always been paid?

10 A. No, it was not always paid. When we acquired
11 the well from Burlington, it was not being paid. We made
12 amends to that and paid back amounts that were due along
13 with statutory interest, which Mr. Sommer had received,
14 and has been in pay status subsequently to that.

15 Q. Looking at the Amadito Valdez interest, what
16 does the "RI" stand for?

17 A. "RI" stands for a revenue interest.

18 Q. Okay. And I'm kind of unclear, because the
19 final column, the unleased mineral interests, you have
20 the unleased mineral interest at eight and a third
21 percent for JAS?

22 A. Correct.

23 Q. But out of that comes the royalty interest, so
24 its working interest is not eight and a third percent?

25 A. Its working interest is eight and a third

1 percent. Its net revenue interest is that amount minus
2 its royalty.

3 Q. If you could turn to page 24, I want to
4 understand, you have four parties with under-production;
5 correct?

6 A. Yes, sir.

7 Q. And is under-production being made up for any
8 of those parties?

9 A. Yes, I believe that's correct. Let me just
10 check this again. Yes. Amadito Valdez is -- his amount
11 is being -- I'm sorry. I retract what I just said. It's
12 Luis Martinez, Estate of Luis Martinez, who is entitled
13 to, in this case, 9 MCF for that production month. His
14 gas was being sold. The sales column there shows 9 MCF
15 and, therefore, there is no build up to that imbalance.
16 The estate of Luis Martinez had signed a marketing
17 agreement with us and we are marketing his gas on his
18 behalf.

19 Q. Is there a signed JOA by Luis Martinez or his
20 estate for this well?

21 A. Luis Martinez signed the JOA.

22 Q. Is there a Division order signed by Joseph
23 Sommer or any of his successors, an Energen Division
24 order?

25 A. No, sir.

1 Q. But you're still paying the royalty interest
2 regardless?

3 A. Yes, we are, in accordance with the Compulsory
4 Pooling Order.

5 Q. The other operators got a signed Division
6 order. Why didn't you?

7 A. Would you repeat that, please?

8 Q. I said Southern Union and Meridian obtained
9 Division orders. Why didn't Energen?

10 A. It's my understanding Mr. Sommer did not want
11 us to sell his gas. The purpose of a Division order is
12 to lay out what the agreed interests, sales interests,
13 will be. We offered Mr. Sommer to sell his gas or
14 offered to have him sell it on his own. There's no need
15 to sign a Division order.

16 Q. He's entitled to a one-eighth royalty interest
17 and the other party -- the other operators had him sign
18 as to his one-eighth royalty interest, didn't they?

19 A. I'm sorry. There was a question there?

20 Q. Didn't the other operators have him sign as to
21 his one-eighth royalty interest?

22 A. If the exhibits show that they signed as to
23 the entirety of his interest, which included his working
24 and his royalty interest.

25 Q. Isn't it also Energen's company policy to have

1 royalty owners sign Division orders?

2 A. Yes, it is.

3 Q. Now, you testified that when Energen or
4 Taurus -- it's basically the same entity; correct?

5 A. Yes.

6 Q. -- took over, there was Sommer -- the Sommer
7 account was assessed in over-production?

8 A. That's what the gas balance statement that we
9 acquired from Burlington showed, yes.

10 Q. And you have used Sommer's working interest to
11 make up that over-production, have you not?

12 A. Yes. We used his working interest, yes.

13 Q. What did you say the over-production was,
14 approximately?

15 A. Back then I believe it was on the order of
16 1,031. I have that figure if you'd like me to find it
17 for you.

18 Q. I'm just asking general numbers.

19 A. Okay.

20 Q. When you bought the well from Meridian --

21 A. Burlington.

22 Q. Burlington, that's right. Excuse me. I
23 should know the chain of title there -- from Burlington,
24 if and when Energen would sell this well, who would be
25 liable for the Sommer under-production?

1 MR. HALL: I'm going to object. I think
2 that calls for speculation. We didn't ask that on
3 direct. I think it's beyond the scope.

4 CHAIRMAN FESMIRE: It calls for a legal
5 conclusion. I think I'll sustain the objection.

6 Q. But Energen certainly used the Burlington
7 Meridian over-production --

8 A. Yes.

9 Q. -- to minimize its liability towards Sommer?

10 MR. HALL: I'm going to object. I think
11 it calls for a legal conclusion at this point.

12 CHAIRMAN FESMIRE: Why don't you rephrase
13 that question, Mr. Bruce?

14 Q. (By Mr. Bruce) Put it this way, Mr. Rote.
15 When you acquired -- and I should say when Taurus/Energen
16 acquired the well from Burlington -- there was, like you
17 say, something of -- over 1,000 MCF of over-production
18 which Sommer owed to the other working interest owners?

19 A. Yes.

20 Q. And you did not -- they owed you money;
21 correct?

22 A. Burlington owed me money.

23 Q. Not Burlington. Sommer.

24 MR. HALL: I'm going to object. I think
25 the question is confusing. Are we talking about the

1 joint interest billings, outstanding expenses?

2 MR. HALL: I'm talking about the
3 over-production.

4 CHAIRMAN FESMIRE: I'll overrule the
5 objection.

6 A. Would you like to rephrase, and I'll --

7 Q. Sure. I'm trying to think of how to say this
8 more concisely. Sommer was over-produced and Sommer
9 actually owed you money?

10 A. From an accounting standpoint, that would be
11 the result, yes.

12 Q. And so you took their gas so that they didn't
13 owe you any money anymore --

14 MR. HALL: I'm going to object.

15 Q. -- and sold gas?

16 MR. HALL: I'm sorry. Why don't you
17 rephrase that? I'll withdraw the objection.

18 Q. Energen sold 100 percent of the gas and used
19 the revenues attributable to the Sommer interest to make
20 up that over-production?

21 MR. HALL: I'll object. I think that is
22 beyond the scope of direct. He didn't testify and there
23 was no testimony or evidence offered that Energen
24 utilized proceeds attributable to an interest owner who
25 did not market his gas.

1 CHAIRMAN FESMIRE: Mr. Hall, I think it's
2 a valid question here. I'm going to overrule the
3 objection. Do you want to try again?

4 Q. (By Mr. Bruce) Well, then, Mr. Rote, how did
5 Energen account for the imbalance? What did they do with
6 the over-production?

7 A. Mr. Bruce, I am not here to testify as a
8 revenue accountant. I'm not an expert in that field.

9 Q. I understand.

10 A. I will make an attempt to answer your
11 question. This occurred back in the 1998 time frame. It
12 seems to me if you had a positive number versus a
13 negative number, positive meaning an over-produced
14 position versus an under-produced position, Mr. Sommer,
15 according to Burlington's records, was over-produced by
16 approximately 1,000 MCF.

17 We took over the operations of the well, sold
18 the gas. And what would happen is because he was not
19 selling his gas, we would build -- that thousand MCF
20 would reduce each month until it hit zero. He continues
21 to not sell his gas, that account now becomes a minus
22 figure, which continues to build up to the current
23 under-produced amount of 8,000 MCFs.

24 CHAIRMAN FESMIRE: Did the JAS interest
25 actually make up that over-production after you all

1 acquired the well?

2 A. It would have balanced out. It would have
3 worked off from that positive thousand down to zero and
4 continued down --

5 CHAIRMAN FESMIRE: So they went from an
6 over-produced to the current 8,000 some-odd MCF
7 under-production?

8 THE WITNESS: Yes, sir.

9 Q. (By Mr. Bruce) And so, in essence, Energen
10 was selling Sommer's gas to make up the over-production?

11 A. Yes, sir.

12 Q. And I guess my question is, why can't Energen
13 sell the gas to make up the under-production?

14 A. We can sell the gas to make up the
15 under-production. If -- but not in a lump sum. It needs
16 to be worked off in accordance with industry standard
17 mechanisms which would be found under normalized gas
18 balancing type agreements, whereby the party would work
19 that off through selling their gas, either through the
20 operator or on their own, plus an additional, as we
21 testified previously, 25 to 40 percent additional
22 interest over their actual working interest.

23 Q. And during the period of time it would have
24 taken to sell that gas to make up Sommer's
25 over-production, they were being charged monthly

1 overhead, monthly lease operating expenses?

2 A. Yes.

3 Q. And I think -- let me be clear here today --
4 you testified that Energen -- you indicated you're
5 willing to increase the Sommer entitlement by
6 approximately how many percent?

7 A. Forty percent.

8 Q. To make up the under-production, at that rate
9 have you calculated how long it would take to make up the
10 Sommer under-production?

11 A. Yes, we have.

12 Q. What is that time period?

13 A. It's in excess of 49 years.

14 Q. Does that well have 49 years of life left in
15 it?

16 A. Yes, it does. According to our engineering
17 evaluation, it has a remaining life of 49.5 years.

18 Q. And gas is a fungible commodity, is it not,
19 natural gas, Mr. Rote?

20 A. Yes.

21 Q. I mean, you could sell the gas now and make it
22 up at any time, could you not?

23 A. I'm not clear on what you're asking.

24 Q. Well, you could -- there's nothing preventing
25 you from making up the over-production at a greater

1 rate -- the under-production at a greater rate?

2 A. The well produces what it produces. I'm not
3 sure if you're asking if I can increase the flow of the
4 well --

5 MR. BRUCE: I'm not asking that, no. Mr.
6 Chairman, I think that's all I have at this point.

7 CHAIRMAN FESMIRE: Commissioner Bailey?

8 EXAMINATION

9 BY COMMISSIONER BAILEY:

10 Q. Through all the paperwork I hear no requests
11 and no offer for an independent oil and gas auditor to
12 review the Sommer's JAS account. Has that not come up?

13 A. Not to my knowledge, ma'am.

14 Q. Okay. Under gas balancing, you say that
15 historical prices are paid at the time of production --

16 A. No, ma'am.

17 Q. -- or balancing out the gas volumes. So the
18 figures we see are volumes and not dollars; right?

19 A. I'm sorry?

20 Q. And you use historical dollar values for
21 settling out the account. Is there any way for one of
22 the working interests to understand on what basis that
23 historical value is based so that they can see what kind
24 of deductions the operator is making for payout?

25 A. In trying to answer your question, ma'am, at

1 the point in time that the gas imbalance would be
2 settled, typically at depletion of the well -- it can be
3 done before, it could be done today -- what we would do
4 is go back in our accounting records to show month by
5 month by month how much we received, what price we
6 received for the volumes that were sold. That would be
7 the same amount that will be paid to the under-produced
8 party.

9 Q. Without deductions?

10 A. No. And you would also have to deduct from
11 that their share of the unpaid JIB bills, lease operating
12 expenses. So what you get is a net number which is based
13 on historical prices we received less that party's share
14 of the expenses that would have been paid had they not
15 marketed their gas.

16 Q. Then let's look at Exhibit 19, the very last
17 page, you're charging interest owners for groceries and
18 food? Is that a legitimate --

19 A. Well, ma'am, I can't particularly answer that.
20 I would point out that that shows in February of 2000, 91
21 cents gross was charged somehow to a food account. I
22 don't believe it to be common, certainly. Though -- and
23 I'm speculating here -- but if we have people out on the
24 well, living there for a workover, food expenses would
25 certainly be appropriate for people that are working on a

1 24-hour basis. I can't be specific about that particular
2 91-cent charge.

3 Q. I just question how a working interest can
4 actually understand all of the charges against their
5 account and which charges are allowed under the gas
6 balancing agreements.

7 A. This Exhibit 19 shows what is a typical -- any
8 operator will have a breakdown of the lease operating
9 expenses on a monthly basis. That's what these are.
10 They include electrical, chemicals, vehicles,
11 supervision, et cetera --

12 Q. And Twinkies?

13 A. -- 91 cents. The nonoperator, the working
14 interest parties, will get a JIB statement each month
15 which we showed on another exhibit here which broke out
16 those particular charges what they are being billed for,
17 for that particular month.

18 THE WITNESS: What was that exhibit,
19 Scott?

20 Q. Let me ask about the allocations that are
21 shown under Exhibit 3. Do you use the top chart of the
22 100 percent well gross net interests or do you show the
23 bottom, or allocate according to the bottom part of that
24 page, revenue DOI interest inflated?

25 A. The answer to that would be -- and, again,

1 we're talking about co-owners, working interest
2 co-owners, not the royalty owners. They're not charged
3 any of these expenses. So the working interest owners
4 would be charged in accordance with that top chart, which
5 is the hundred percent division of interest. That is the
6 true gross working interest that the nonoperated working
7 interest owner would have. That is the basis upon which
8 they would be billed.

9 For clarification, that bottom half of the
10 page was what we called an inflated debt. That was to
11 allow for proper payments to be made in those cases where
12 the operator is not selling 100 percent of the gas flow
13 from the well. To summarize the answer to your question,
14 the working interest owners would be charged their gross
15 working interest percentage in accordance with that top
16 chart.

17 Q. So the well which could have, according to
18 Ernst and Young, costs, overhead costs, of \$550?

19 A. Yes.

20 Q. JAS would be responsible for 8.33 percent --

21 A. Of that amount.

22 Q. -- of that 550?

23 A. That's correct, yes.

24 Q. Could you look on your brochure and give me
25 the Ernst and Young overhead rate for wells that are not

1 as deep as you gave us the rating for?

2 A. That are not what?

3 Q. That are not as deep as the rating you gave
4 us.

5 A. From 0 to 5,000 feet, the median is \$436 and
6 maximum is \$912. For wells 5,000 to 10,000 feet, the
7 median is 550, the maximum is 750. For wells between
8 10,000 and 15,000 feet, the median \$796, the maximum is
9 \$1,102.

10 Q. Are there many wells that produce from the
11 Pictured Cliffs that are 5,000 feet, Pictured Cliffs
12 production?

13 A. Ma'am, I'm not a geologist. I would be
14 guessing to answer that. I'm not sure of the answer. I
15 don't know.

16 Q. So the basis for much of this case has to do
17 with charges for overhead and supervision?

18 A. I would agree that that is a large part to
19 this. Also, if I may, it also has to do with marketing a
20 co-owner's gas. Throughout these years we have not been
21 able to get permission to market this gas on their
22 behalf, nor have we -- nor have they taken on the ability
23 to market on their own account. That's the problem.

24 The problem is we can't market their gas.
25 They will not allow us to market the gas, and that's what

1 creates this imbalance situation. In my mind there's two
2 main issues. One is the ability to sell this gas. We
3 will do it. We're willing to do it. They have the
4 ability to sell their own share of that gas if they found
5 their own market. The second issue is whether or not the
6 costs were to be deemed reasonable, and we believe that
7 they are.

8 Q. What recourse would a small working interest
9 owner have if they don't agree with being charged 91
10 cents for Twinkies?

11 A. I guess they could call me and we can do what
12 we need to do to make everyone happy, I suppose. We can
13 accommodate requests, and if that was a reasonable
14 charge, we would certainly look into it and determine the
15 facts of the situation and adjust if we needed to. If it
16 wasn't a legitimate charge, certainly we would knock it
17 off of the bill. We respond to many questions about
18 charges, about issues like that, and I believe our
19 company does a fine job of accommodating those questions
20 and resolving those issues to the satisfaction of both
21 our working interest parties and our royalty owners.

22 COMMISSIONER BAILEY: That's all.

23 CHAIRMAN FESMIRE: Commissioner Olson, do
24 you have any questions?

25 COMMISSIONER OLSON: No questions.

EXAMINATION

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BY CHAIRMAN FESMIRE:

Q. Mr. Rote, can we look at Exhibit 15 real quick on page 4?

MR. HALL: I'm sorry?

CHAIRMAN FESMIRE: Fifteen on page 4.

Q. You made a statement during your testimony that I didn't quite follow. You said something about you couldn't estimate the operating expenses and sell only that amount. Could you clarify what you meant by that?

A. I'll try. I get mindlock on this whole concept because I don't believe it's even possible to do. As I understand what this concept is, is that out of the flow of gas, I can segregate out, in this case 8.33 percent of those molecules, minus the share -- that share of the JIB costs, two molecules of gas. So I have to account for two molecules of gas in the next upcoming billing cycle, and I'm guessing what -- whether it's two molecules or is it four molecules or is it three and a half molecules.

And the accounting for that is just -- as I said, I cannot testify as an oil and gas revenue accountant. Maybe somebody more well versed in those can grasp this concept. I personally am having a hard time understanding how that could be implemented using our

1 current systems and -- not only for our company, but for
2 others. Now, I admit it's not a very good answer. I'm
3 sorry. That's the best I can do.

4 Q. By the time you're required to make payments,
5 you know what the actual operating expenses are, don't
6 you? Why would you have to estimate them?

7 A. Perhaps you're correct. Perhaps it could be
8 done. I don't know how to do it. I would need some
9 guidance and some expertise and discussions with people
10 that know how to set up the accounting systems to know
11 whether or not its even possible.

12 Q. Okay. Exhibit 18, now, that wasn't executed
13 on -- what is the relationship of this McCroden C #1 to
14 this Martinez #1? Are they different horizons on the
15 same lease?

16 A. Yes, that's exactly right. McCroden is a
17 different formation than the Martinez, and that the --
18 Mr. Sommer owned an interest in the section that both of
19 these wells are situated in.

20 Q. If I understand correctly, the Sommer interest
21 executed this Model Form Operating Agreement on McCroden?

22 A. That's correct. Yes, sir.

23 Q. Why would they have executed that and not a
24 similar agreement on the Martinez well?

25 A. This was executed in 2006. I cannot answer

1 your question. I think you need to ask that of Mr.
2 Sommer, himself.

3 Q. Okay. The conditions in this Model Form
4 Operating Agreement are essentially what you requested on
5 the Martinez well?

6 A. Yes.

7 Q. Let's talk about that 40 percent, the makeup
8 factor. What is this well producing now?

9 A. It currently produces approximately 24 M's a
10 day.

11 Q. Twenty-four MCF a day? And that's got a
12 49-year life?

13 A. Last week I had our engineering manager look
14 at the well and determine that the EUR, estimated
15 ultimate recovery, was 166,000 MCF, estimated that at a
16 three and a half percent decline rate, that the remaining
17 life of the well is 49 and a half years. I will also
18 add, perhaps, to my detriment, that when we had offered
19 the 40 percent gas increase over his current interest,
20 what would happen is it would -- the well may likely
21 deplete before that gas balance got back down to zero.
22 So I asked the question, what percent would it take to
23 have that not happen. The answer to that is 60 percent.

24 So in order for that gas and balance to be
25 built off, we would have to give Mr. Sommer his current

1 8.33 percent plus the additional 60 percent for --

2 Q. Sixty percent of the 8.33 percent less the
3 revenue share?

4 A. That's exactly right.

5 Q. And you'd have to give it to them at that 60
6 percent -- I guess I'm not understanding. Forty percent
7 just exactly equals the life of the well?

8 A. Actually, the 40 percent probably extended
9 past the 49 and a half years, okay? And, really, it
10 depends on what decline curve you use. If you use a
11 three and a half percent rate of decline or a 4 percent
12 rate of decline and two and a half percent of that, that
13 all got very variable out toward the end of this curve.

14 Q. If we would grant this, and assuming your
15 assumptions are correct, we would essentially be taking
16 the JAS interest out of the well; is that correct?

17 A. Taking the interest out of the well?

18 Q. They would get -- all they would do is make up
19 the -- out of the over-production now?

20 A. No. They would continue to get their 8
21 percent. That 40 percent would be -- the imbalance would
22 be built off, but they would continue to get their 8
23 percent. And that 40 percent additional or 60 percent
24 additional would build off that imbalance.

25 Q. I think I slipped a cog here. Can you explain

1 that to me again?

2 A. I'll try. Let's use the 40 percent. That
3 additional 40 percent volume would -- that 40 percent
4 volume works off that gas imbalance, okay? The 8 percent
5 they would continue to receive through the life of the
6 well.

7 Q. And they're 8,200 MCF under-produced; is that
8 correct?

9 A. Yes. We have a gas imbalance that's gotten
10 quite large for the volume and the life of this well.
11 That's a fact. We don't debate that. In my mind, the
12 best solution at this point in time is to settle out that
13 gas imbalance today, historical prices, move forward and
14 market -- have them market their gas, or we will market
15 for them, their 8 percent share, for the remaining life
16 of the well less JIBs, expenses, which include lease
17 operating costs, which is inclusive of COPAS overhead
18 rates. That's the solution to this whole problem.

19 Q. At 24 MCF a day, up there they're making about
20 \$2.50 to \$3 an MCF. So we're looking at 60-plus dollars
21 a day from that well. You take the royalty out of that,
22 you're looking at, oh -- I'm assuming the royalties are
23 all near the same at the eight?

24 A. Yes.

25 Q. So you're looking somewhere around \$52 per day

1 and the costs at 550 per day are just under \$20, so
2 you're looking at \$40 a day, which is about \$1,200 a
3 month. But it concerns me that you're calculating a
4 49-year life at -- what was the decline rate?

5 A. Three and a half percent.

6 Q. That seems awfully optimistic for the life.

7 A. Perhaps it is. Obviously, this is a marginal
8 well. It may not last that long, particularly if it
9 becomes uneconomic as the prices decline. At that point
10 you reach what we call the depletion point. Again, I go
11 back to the normalized industry standard. At that
12 depletion point, you settle out this cash imbalance at
13 historical pricing, less that co-owner's share of the
14 lease operating expenses that were necessary to produce
15 the well. It's a marginal well. You're exactly correct.

16 Q. And you talked a little bit about the Ernst
17 and Young overhead rates. How are they related to the
18 COPAS rates? I guess I didn't follow what was going on
19 there.

20 A. I can speculate. I don't know the correct
21 answer for sure. I think what they do is just an
22 industry survey. They survey operators to come up with
23 those numbers, as opposed to COPAS, which uses some
24 factoring for an inflation rate. They look at the actual
25 well costs, they accelerate it over the past year, the

1 wage price index type data to come up with their detail.
2 This is just a survey of operators, saying, "What are you
3 charging?" I think that would be the distinction between
4 the two.

5 Q. In an ideal world, the COPAS rate would be the
6 rate that Ernst and Young comes up in their survey. But
7 in reality, there are differences; right?

8 A. There would appear to be, yes

9 Q. So the COPAS amount is the actual amount
10 negotiated in that year, escalated -- I'm assuming it's
11 always escalated -- by some percentage that is calculated
12 by COPAS?

13 A. Yes, but it has not always been escalated.
14 There have been years where it declined

15 Q. Yeah, there have been. I apologize for that.
16 So when you testified to the Ernst and Young overhead
17 rates, we sort of switched horses. We've gone from
18 talking about the COPAS rate which is calculated -- which
19 was the 1984 negotiated rate times the 240 some-odd
20 percent?

21 A. Yes, sir.

22 Q. But that wasn't the negotiated rate that the
23 JAS interests negotiated, because they weren't party to
24 that agreement that you were talking about; right?

25 A. That's correct.

1 Q. Do you happen to know -- on the other well,
2 the model operating agreement that was signed in 2006, do
3 you happen to know what the operating overhead allowable
4 in that agreement was? We didn't get all of the
5 agreement.

6 MR. HALL: Mr. Chairman, we ask that we be
7 allowed to supplement the record with the entirety of
8 that Joint Operating Agreement so the record is complete.
9 We'll get that to you.

10 CHAIRMAN FESMIRE: Do the Commissioners
11 have any objection? Mr. Hall, I'm not sure if we can get
12 the information that we're talking about. I'm not sure
13 that's proper.

14 THE WITNESS: Without having it in front
15 of me, I will say that it likely was somewhere between
16 350 to \$500.

17 Q. (By Chairman Fesmire) What was that -- that
18 was in 2006?

19 A. Yes, sir.

20 Q. Do you know the depth of that McCroden well?

21 A. This was a Mesaverde well, and that's deeper
22 than the Pictured Cliff.

23 Q. And the overhead there was between 350 and
24 \$550?

25 A. Yes, to start, under that Joint Operating

1 Agreement. That's typically a negotiated number entered
2 into at the time that these agreements are contemplated
3 between working interest parties.

4 CHAIRMAN FESMIRE: And what was the COPAS
5 exhibit, Mr. Hall?

6 MR. HALL: The inflation index was 21.

7 Q. (By Chairman Fesmire) If we take 350 to 550
8 starting in 2006 --

9 A. Yes. You would go to the second page of that
10 exhibit and the top line, go all the way over to 2006,
11 and you would drop down to 2009, and so that rate --

12 Q. What would that factor be?

13 A. Basically, 123.19 percent.

14 Q. If we apply 123 percent to the 350 to -- what
15 was the maximum, 550?

16 A. Yes, I would guess so. I don't have that with
17 me.

18 Q. So we're talking about, at a maximum, \$650 for
19 a deeper well?

20 A. Yes. That's right.

21 Q. Why would the Martinez Well require -- what
22 was it you're asking -- 800?

23 A. 860 some-odd -- yes. It was because the
24 application of the COPAS inflation factors caused that to
25 occur. It doesn't become a judgment call at some point

1 down the road. It's just a very automatically imposed
2 inflation factor using industry-accepted procedures and
3 standards devised by COPAS.

4 Q. You see the point I'm trying to make? You've
5 got a deeper well, and if you take an agreement that the
6 JAS interests were a party to and inflate the maximum to
7 that, you're still, you know, by a factor of 25, 30
8 percent, under what you all are asking for the Martinez
9 Well.

10 A. Yes, that's correct.

11 Q. Turning to Exhibit 3, I've got a whole slew of
12 questions there. You indicated that Amadito Valdez is
13 not participating, either, that his and the JAS interests
14 were the only ones?

15 A. Yes. Mr. Valdez had signed the Joint
16 Operating Agreement and is not marketing his share, so --

17 Q. Why aren't you seeking to, in essence, make
18 him a part of the pooling agreement, also?

19 A. I don't know how to answer that. We have
20 attempted to contact Mr. Amadito. We've sent him letters
21 to ask him to accommodate his situation, and he's never
22 responded. We just can't seem to work with the man.

23 Q. But I guess the point I'm trying to make, if
24 you're going to this expense and this effort to modify
25 the pooling agreement for the JAS interest, why aren't we

1 talking about Valdez interest, too?

2 A. I would assume that the modification to the
3 pooling order would accommodate his interest, as well,
4 perhaps.

5 Q. Okay. Talking about, again, on Exhibit 3, the
6 type of interest, "OR," I'm assuming is override?

7 A. Yes.

8 Q. "RY" is royalty interest?

9 A. "RY" is royalty.

10 Q. And "URI" is unsigned revenue interest?

11 A. Unleased royalty interest.

12 Q. Royalty or revenue?

13 A. Royalty.

14 Q. Unleased royalty interest. And "UMI" is
15 unleased mineral interest?

16 A. Yes, sier.

17 Q. How does an unleased mineral interest differ
18 from an unleased royalty interest?

19 A. I think what we attempted to do there was
20 differentiate -- break out the JAS working interest from
21 their one-eighth royalty interest. It was an
22 accommodation to be able to account for that one-eighth
23 interest.

24 Q. Now, to make sure I understand what's going on
25 in the next deck, the revenue DOI deck, what you've done

1 is you've taken their revenue or royalty interest -- and
2 I have a tendency to group them together, and I know
3 they're not, so if I misstate that, I apologize -- but
4 you've taken that and divided it by the 9.027, which is
5 the JAS interest and the -- how do you get from 8.33
6 percent times their seven-eighths to the 10 percent or
7 near the 10 percent that's the reduction here?

8 A. Well, again, I don't have those calculations
9 in front of me, but I believe it was done by taking the
10 8.33 plus a couple of those other numbers to get --

11 Q. The Martinez and the --

12 A. Whatever would add up to 90 percent.

13 Q. To get this number, you divide their revenue
14 interest by this percentage, and that's to distribute the
15 revenue stream from current production to those owners
16 who have --

17 A. -- who share in that stream. Again, I do not
18 testify to be an expert here at all, but I will try --
19 and you've already determined how bad my math can be. As
20 I understand how the inflation factors work, and, again,
21 this is common to the industry, let's assume that we
22 have -- Energen has a 50 percent working interest in a
23 well, Exxon has a 50 percent working interest, same well.
24 We both have a royalty owner for one-eighth royalty. But
25 for me and for Exxon I would now have 50 percent gross

1 working interest and a 37 and a half percent net revenue
2 interest. Now, 37 and a half plus the 12 and a half
3 percent, so -- okay. So we both have those decks.

4 I'm selling my gas, Exxon is selling their
5 gas, split stream. I get a check for my gas for \$100.
6 When that check comes in the door, if I apply that to 100
7 percent deck, \$50 is going over to Exxon and it shouldn't
8 because that's my money, so I've inflated my deck. In
9 this case I've taken my net divided by my gross, my 37.5
10 divided by 45, which gives me .75. So that check comes
11 in. It hits. \$75 is mine and \$25 goes to my royalty
12 owners and zero goes to the Exxon deck.

13 That's about the best I can do to try to
14 explain how that works. The theory is so that when I'm
15 selling my gas, I have -- another party is selling their
16 gas. When my check comes in, it doesn't get booked to
17 the 100 percent deck, which would cause a portion of my
18 money to go to Exxon.

19 Q. And you're selling -- I think you're selling
20 100 percent of the gas from this well; correct?

21 A. Yes.

22 Q. But a portion, about 10 percent of that
23 production is -- and I don't mean this accusatorily --
24 but almost 10 percent of that gas isn't yours to sell.

25 A. Right.

1 Q. So what this does is adjust those royalty
2 interests for that gas that every one of these people is,
3 in essence, building up a debt, a gas debt, let's call
4 it, to the JAS interest and the other unsigned interests?
5 Is that --

6 A. I would say that that's pretty accurate.

7 CHAIRMAN FESMIRE: I think that's all the
8 questions I have. Mr. Hall, do you have any redirect?

9 MR. HALL: Briefly, Mr. Chairman.

10 REDIRECT EXAMINATION

11 BY MR. HALL:

12 Q. Let's make sure the record is clear and our
13 understanding is clear on the various interests here. If
14 we refer back to Exhibit 3, the revenue decks, is it
15 correct that the interest of Josie Gallegos, Amadito
16 Valdez and the Estate of Luis Martinez are all
17 participating in the well pursuant to a Joint Operating
18 Agreement?

19 A. Yes, that's correct. They all signed a Joint
20 Operating Agreement.

21 Q. And in the case of Luis Martinez, when he
22 participates as a mineral interest owner, did he
23 participate with 100 percent of his interest?

24 A. I think -- yes, he did.

25 Q. That's why there's no separate royalty column

1 reflected for Luis Martinez's interest; is that right?

2 A. Right.

3 CHAIRMAN FESMIRE: Can I ask a question
4 here? Yet he's carried on the records as an unleased
5 mineral interest?

6 MR. HALL: Not royalty.

7 CHAIRMAN FESMIRE: Not royalty interest.
8 Okay. I'm sorry.

9 MR. HALL: Clear on the concept?

10 CHAIRMAN FESMIRE: I'll figure it out
11 eventually.

12 Q. (By Mr. Hall) Isn't it correct to say that
13 the relationship between the Luis Martinez estate
14 interest and Energen is pursuant to that contract, that
15 Joint Operating Agreement, and not under the Compulsory
16 Pooling Order?

17 A. Yes. And they also signed a marketing
18 agreement with us to allow us to market their gas.

19 Q. Okay. Refer briefly to our Exhibit 24. Let's
20 make sure the record is correct on this. We show on
21 there an under-produced position for JAS of 8,378 MCF;
22 correct?

23 A. Yes.

24 Q. But that is not net of the royalty interest --
25 royalty revenues that have been paid to JAS; correct?

1 A. That is their gross number.

2 Q. So to derive the current under-produced
3 position attributable to the pooled seven-eighths working
4 interest owner, it's factored by 12 and a half percent,
5 one-eighth; correct?

6 A. Right.

7 CHAIRMAN FESMIRE: Mr. Hall, can I ask a
8 couple of questions? I'm really not following that, as
9 you can tell by my questions. The under-produced
10 figures -- I'm going to call it the 8,400 MCF -- the
11 under-produced -- does JAS hold two interests, a mineral
12 interest and a royalty interest?

13 MR. HALL: No, sir.

14 CHAIRMAN FESMIRE: So the division is to,
15 basically, satisfy the way that the OCD orders are
16 written. They have to pay the royalty independent of
17 the -- on the unleased interest independent of the
18 working interest?

19 MR. HALL: Exactly.

20 CHAIRMAN FESMIRE: So this 8,400 MCF, is
21 that seven-eighths?

22 MR. HALL: That's the under-produced
23 position attributable to the eight-eighths mineral
24 interests.

25 CHAIRMAN FESMIRE: Okay. So what's

1 actually owed to them is seven-eighths of this?

2 MR. HALL: Correct. Since you're allowing
3 me to testify, Mr. Chairman, factor that by 12 and a half
4 percent, that reduces that by 1,047 MCF. The actual
5 under-produced position is 7,331.

6 CHAIRMAN FESMIRE: Okay.

7 Q. (By Mr. Hall) Energen has operated the
8 Martinez #1 Well since 1997?

9 A. That's correct.

10 Q. It's taken us 12 years to get to the position
11 we are now with respect to the production imbalances; is
12 that right?

13 A. Yes. That's right.

14 Q. Even though Energen acquired the well with JAS
15 interest in over-produced status, that position was
16 worked down over the years by virtue of the refusal and
17 failure of Sommer JAS to allow for the marketing of their
18 interest; is that right?

19 A. That's correct.

20 Q. There were a couple of questions from Mr.
21 Bruce with respect to why there's no current Division
22 order, Energen Division order, covering the Sommer JAS
23 interest. Let's establish the ownership of JAS is not in
24 dispute at all; is that right?

25 A. No, not at all.

1 MR. HALL: That's all I have, Mr.
2 Chairman.

3 CHAIRMAN FESMIRE: Mr. Bruce, anything on
4 that?

5 MR. BRUCE: Just a couple.

6 RECROSS-EXAMINATION

7 BY MR. BRUCE:

8 Q. And you might not know answer to this one, Mr.
9 Rote, but it goes back to a question or questions that
10 the Commissioners asked you. Your engineer's prediction
11 of a 49-and-a-half-year life, what gas price do they use
12 in making that prediction, that calculation?

13 A. I don't believe price was a function of that
14 equation. I think it was strictly a volume versus time
15 versus decline rate equation that they used.

16 Q. So, in addition, that 49.5 years would not
17 take into account any requested COPAS adjustment of the
18 operating costs, either?

19 A. As I said, I believe all they did was a simple
20 equation of time and decline rate without economics built
21 into it.

22 MR. BRUCE: That's all I have, Mr.
23 Chairman.

24 CHAIRMAN FESMIRE: Anything further from
25 the Commissioners?

1 COMMISSIONER BAILEY: No.

2 COMMISSIONER OLSON: No.

3 MR. SMITH: Do you mind if I ask a
4 question?

5 CHAIRMAN FESMIRE: Sure.

6 MR. SMITH: Mr. Rote, you recall when you
7 were answering questions of Chairman Fesmire, you were
8 talking about the McCroden well, and I think you
9 estimated that the starting point there was 350 to 500?

10 THE WITNESS: Yes, sir.

11 MR. SMITH: Okay. That was beginning in,
12 I think, 2006; right?

13 THE WITNESS: Yes.

14 MR. SMITH: Is the difference between the
15 figure that you have, whatever it is, 900 or something,
16 and the 1.23 times the 500 for the McCroden well, is that
17 largely a function of the date and time that you start?

18 THE WITNESS: Yes, sir, I believe that to
19 be the case. If I have an operating agreement that was
20 signed in 1960, that's 50 years ago and they had a \$200
21 rate in 1950, escalated over time, as inflation will have
22 it, is a very, very large number today. The new JOA that
23 was signed last year, add \$1,000, you know, agreed to
24 overhead rate is probably going to be \$1,100 today, but
25 the 1960 agreement may be 1,500.

1 MR. SMITH: Why did you pick 1984? I
2 think that's what you testified --

3 THE WITNESS: That was the Joint Operating
4 Agreement that was signed for the Martinez Well by the
5 operator and the co-owners at that point in time, and as
6 the Commissioner pointed out, with the exception of Mr.
7 Sommer.

8 MR. SMITH: Okay. Thank you.

9 CHAIRMAN FESMIRE: You're welcome. Mr.
10 Hall, anything further?

11 MR. HALL: That concludes our case on
12 direct.

13 CHAIRMAN FESMIRE: Mr. Bruce, we've got 10
14 minutes to lunch. Do you want to call your first witness
15 or would you like to break for lunch and come back?

16 MR. BRUCE: Why don't we just break for
17 lunch and come back?

18 CHAIRMAN FESMIRE: Okay. With that we'll
19 adjourn for lunch and reconvene at 1:00.

20 (A lunch recess was taken.)

21 CHAIRMAN FESMIRE: We're back on the
22 record in the continuation of Cause Number 13957. The
23 record should reflect it's 1:00 on Wednesday, May 27th.
24 All three Commissioners are present. We, therefore, have
25 a quorum. Mr. Bruce, I believe you were getting ready to

1 call your first witness.

2 KURT A. SOMMER

3 Having been first duly sworn, testified as follows:

4 DIRECT EXAMINATION

5 BY MR. BRUCE:

6 Q. Would you please state your name for the
7 record?

8 A. Kurt A. Sommer.

9 Q. And where do you reside?

10 A. 756 Calle Altamira, Santa Fe, New Mexico.

11 Q. What is your relationship to JAS Oil and Gas
12 Company?

13 A. I'm the trustee of the Joseph A. Sommer
14 Revocable Trust, which is 100 percent owner of JAS Oil
15 and Gas, LLC.

16 Q. And JAS Oil and Gas does own the 8.33 percent
17 mineral interest in this particular well unit?

18 A. Yes, it does.

19 Q. Are you familiar with the matters involved
20 with the trust, with JAS and its mineral interest
21 involved in this application?

22 A. I am.

23 MR. BRUCE: Mr. Chairman I'm not
24 qualifying Mr. Sommer as an expert witness.

25 CHAIRMAN FESMIRE: Not yet.

1 MR. BRUCE: Not yet. I could as an
2 attorney, but --

3 Q. (By Mr. Bruce) Just to start off with, Mr.
4 Sommer, if you could be brief, what is JAS's position in
5 this case?

6 A. Its position is pretty simple. It objects to
7 some of the overhead charges that we're being charged and
8 have been charged by Energen on the Martinez Well, and it
9 objects to the fact that 100 percent of the minerals are
10 being sold and it is not being credited back its
11 proportionate share of the sales. In fact, it is being
12 shown as a gas imbalance or due-to type of credit. It
13 objects because Energen is using the money from the well
14 and not even paying interest on its -- on the money being
15 received from the sales, and it simultaneously is
16 charging back costs of operating the well.

17 Q. So it's JAS's position that the gas balance
18 and credits should not be -- are not proper?

19 A. That's correct.

20 CHAIRMAN FESMIRE: Mr. Bruce, we have to
21 take a short side trip here. The attorney for the
22 Commission has a disclosure that he feels that he
23 ethically has to make before we continue.

24 MR. SMITH: I don't believe that is in the
25 nature of a conflict, but Mr. Sommer does work for Mining

1 and Minerals Division, and Mining and Minerals Division
2 is one of the divisions for whom I work as assistant
3 general counsel. They're one of my primary charges. I
4 believe you've done some real estate work for MMD; is
5 that right?

6 THE WITNESS: If I could explain the
7 nature of the representation, I think you'll --

8 CHAIRMAN FESMIRE: Why don't we let him
9 finish?

10 THE WITNESS: Okay.

11 MR. SMITH: No. I just wanted to bring
12 that up. If you'd like to explain the nature of the
13 representation. I don't think I'm disqualified from
14 representing the Commission in this matter, but I don't
15 want any kind of trouble to come up later on, so I
16 thought I'd bring it up. And if you all don't mind,
17 maybe Mr. Sommer could discuss his representation of MMD.

18 CHAIRMAN FESMIRE: Mr. Sommer?

19 THE WITNESS: Our firm was retained to
20 review title reports and title issues and appraisals for
21 MMD on property that was being put up for security by, at
22 the time, Phelps Dodge and now its successor. We
23 performed that work some time ago, and Phelps Dodge put
24 up its collateral and we reviewed the mortgages for the
25 State of New Mexico or NMMMD. We've had a continuing

1 role in the sense that every five years there's new
2 material to be produced and we review the material for
3 them. It has nothing to do with any of the properties
4 in question with this.

5 CHAIRMAN FESMIRE: Mr. Smith, you don't
6 see any problem with your continuing in this case?

7 MR. SMITH: No, I don't. I just wanted to
8 make sure that everyone else knew about this so if they
9 thought there was a problem, they could raise it now.

10 CHAIRMAN FESMIRE: Mr. Hall, do you have
11 any concerns?

12 MR. HALL: I don't believe so. There's no
13 indication that Mr. Smith has represented the agency on
14 any matter relating to this application at all, as I
15 understand what you're saying, so I don't think the rules
16 would prohibit him.

17 MR. SMITH: MMD is a completely different
18 division. It's a mining division, and the -- I mean, the
19 properties that are involved in Mr. Sommer's work are
20 properties owned by other companies elsewhere and they're
21 used as collateral for financial assurance. They don't
22 have anything to do with this property.

23 CHAIRMAN FESMIRE: Mr. Hall, if at any
24 point it gets to where you do have concerns, would you
25 please raise those concerns at that time?

1 MR. HALL: I will.

2 CHAIRMAN FESMIRE: Mr. Bruce, I don't know
3 that you'd have a standing to object. Is there any
4 problem for you?

5 MR. BRUCE: Nonetheless, I have no
6 objection.

7 CHAIRMAN FESMIRE: Why don't you go ahead
8 and continue and re-ask the last question.

9 Q. (By Mr. Bruce) So as a result, it's JAS's
10 position that gas credits, whether it's over-production
11 or under-production, are inappropriate with respect to a
12 force-pooled well unit?

13 A. That's correct.

14 Q. Let's go to your exhibits and let's start with
15 Exhibit 4. Explain what this is.

16 A. This is a letter to Scott Hall in September of
17 2005, and the request was -- to deal with the imbalance
18 was either to deliver the actual gas that was due as a
19 credit or shown as a credit at the time or to pay for the
20 gas as a way of dealing with the imbalance. So it was a
21 demand upon Energen through Mr. Hall, who was
22 representing them at the time, to deal with this
23 imbalance.

24 Q. What was their response?

25 A. We had no response. They wouldn't deliver the

1 gas and they wouldn't pay for what they were showing as a
2 credit.

3 Q. So you were here listening to Mr. Rote today,
4 were you not?

5 A. Yes.

6 Q. And Energen stated that Sommer has made no
7 attempt to take its gas. Does this letter refute that?

8 A. This letter refutes it. In conversations with
9 Energen subsequent to this letter over the last several
10 years, their idea of giving us credit for the gas was to
11 take it out of the well only, even though they've sold
12 all the gas.

13 Q. Let's skip over again just to keep on the same
14 theme, the over/under-production. What is Exhibit 5?

15 A. Exhibit 5 is a statement of gas imbalance as
16 of February 2007, which showed what the gas imbalance
17 that Energen believed was due to JAS, Josie Gallegos, the
18 Luis Martinez Estate, Amadito Valdez and the
19 over-production that was taken out of the well by
20 Energen.

21 Q. Now, I've handed you also what was marked as I
22 think Energen Exhibit 24?

23 A. Yes.

24 Q. And that's a more up-to-date -- I believe
25 that's a more up-to-date gas balancing statement?

1 A. Yes. I actually received a statement I
2 believe through April, which shows a little over 8,500 in
3 terms of gas imbalance.

4 Q. If you take Energen's -- I think Mr. Rote also
5 testified that, other than JAS, all of these other people
6 were under a JOA or some type of written agreement with
7 Energen?

8 A. That's my understanding, yes.

9 Q. If you compare Exhibit 5, which is from
10 February '07 to the more recent statement over two years
11 later, the under-production keeps increasing for all
12 these people, does it not?

13 A. It has increased -- it appears it has only
14 increased as to the Estate of Luis Martinez slightly, and
15 it appears it's increased, as well, to -- actually, it
16 appears that it's increased as to all of them.

17 Q. If that's the case, what does signing a JOA
18 get you?

19 A. It won't get me anything because it won't deal
20 with this imbalance and the money that's been used and
21 taken for the sales.

22 Q. Let's move on to your Exhibit 8 at this point.
23 I think this might have been in Energen's exhibit
24 booklet, also. But could you identify that and state to
25 the Commission what your position is with respect to this

1 letter?

2 A. This is a letter that was written by Joseph
3 Sommer, my father, on October 15, 2002, to Mr. Rote
4 trying to explain to Mr. Rote that the JOA was never
5 signed by him and to assume that he should be operating
6 under the terms and conditions of that JOA as the basis
7 on which the costs and operation and supervision under
8 the pooling agreement was inappropriate, because there
9 was never a signed JOA. He was also trying to explain
10 that the imbalances at the rate of 40 percent, which was
11 offered, would never pay out. And a consequence of that,
12 he was trying to explain to Mr. Rote that it was
13 inappropriate to settle on the basis that was being
14 proposed.

15 Q. Let's move back to your Exhibit 7. What is
16 that letter?

17 A. It's a letter from me dated December 21st,
18 2006, to Energen dealing with a payment of money due for
19 pro rata share of a work-over on the McCroden Well which
20 I agreed to participate in for that work-over of that
21 well. And so what I was doing is transmitting the
22 \$12,949.56 to Energen to make sure that we were credited
23 with our cost of the work-over.

24 Q. And this is the deeper Mesaverde test that is
25 in the west half of Section 2?

1 A. I believe so, yes.

2 Q. And I notice in the second paragraph you say,
3 "I expect that we will be paid our pro rata share of all
4 gas sales on a monthly basis." Have you been?

5 A. No, I have not. In fact, this month I wrote a
6 letter and explained that they had no basis on which to
7 do a gas imbalance on the McCroden well particularly
8 because we had signed an agreement with them. It wasn't
9 significant at this point, but it was about 200 MCF.

10 Q. Would you agree that the best way to resolve
11 this issue is for a lump sum to be paid to JAS and then
12 move forward on an ongoing basis with respect to gas
13 sales?

14 A. I believe the best way to resolve this is for
15 JAS to be paid its pro rata shares of historical sales of
16 this well that has been collected by Energen, including
17 the imbalance that it claims as a credit which I think
18 they got as an offset for the cost of the well that they
19 took credit for in this imbalance that they're showing,
20 together with interest at the statutory rate from the 30
21 days from the date of payment, together with the attorney
22 fees and costs that we've incurred in having to enforce
23 this particular matter.

24 Q. Let's discuss the overhead rates a little bit.
25 And, first of all, I think this goes back to a question

1 that was asked of Mr. Rote. What is Exhibit 12, Sommer
2 Exhibit 12?

3 A. Exhibit 12 is a Model Form Operating Agreement
4 that appears to have been tendered vis-a-vis or with
5 respect to the Martinez Well #1.

6 Q. And down at the bottom it shows that this was
7 Energen Exhibit 20 in the Oil Conservation Division case?

8 A. That's correct.

9 Q. And did Joseph A. Sommer, your predecessor
10 interest, sign this agreement?

11 A. No. He refused to because they wouldn't make
12 any changes in it to reflect what he thought was fair and
13 proper, and it also did not deal with the imbalance, so
14 he refused to sign an operating agreement.

15 Q. And this portion of the operating agreement
16 two or three pages back also includes the overhead rates?

17 A. It does. I believe it does. If you look on
18 page 3 of this Exhibit C, there's an overhead rate of
19 \$350 a well. I don't find that amount objectionable. It
20 was that it didn't deal with the fact that the prior
21 charges were based on higher amounts.

22 Q. And with respect to overhead rates, let's move
23 on to your Exhibit 6. What is that?

24 A. This appears to be a statement from Energen to
25 JAS Oil and Gas for 9/30/07 showing what they believe to

1 be the charges that were due at that particular time for
2 this well.

3 Q. And if you'll turn to page 2. Look at its
4 fixed producing overhead. What is that amount?

5 A. Fixed producing overhead was \$748.12.

6 Q. That's the amount they requested at the
7 hearing when we went to hearing in November of 2007?

8 A. That's correct.

9 Q. They were already charging you that amount?

10 A. That's what they were charging. That's what
11 the charges have been based upon. That's correct.

12 Q. So even though there was no agreement as to
13 the overhead rates, they were already charging you that
14 amount?

15 A. That's correct.

16 Q. Move on to Exhibit 9. Briefly, what is that,
17 Mr. Sommer?

18 A. This is a letter that was written by Thomas F.
19 McKenna, who was law partner of my father at the time, in
20 April 1961, dealing with the pooling arrangement that was
21 entered by the Commission at that particular time. So
22 it's -- this letter deals with the pooling order that was
23 entered that is the subject of this hearing.

24 Q. And what does the third paragraph state?

25 A. "Our position is that the applicant should be

1 limited to the lowest actual expenditures plus a
2 reasonable charge for supervision after the well is
3 completed and put on production if such is the case."

4 Q. Is that still JAS's position?

5 A. It continues to be JAS's and its predecessor's
6 position.

7 Q. I asked Mr. Rote a question and he didn't know
8 about it, but I referenced a management fee that had been
9 charged by Energen against the Sommer interest. Do you
10 know about that?

11 A. There was a management fee imposed at one
12 point as part of their billings. I don't see a copy of
13 it in the exhibits we have here. I think that's what
14 you're probably referring to.

15 Q. Was that a fixed fee that was charged on a
16 monthly basis?

17 A. It was at the time. I don't believe that it's
18 imposed now. I think if you look at the exhibit we were
19 just looking at, that it's shown as overhead now.

20 Q. Were there ever discussions with them
21 regarding the reason for charging this management fee?

22 A. There's numerous letters. If you look at the
23 petition, there's an exhibit book back and forth about
24 the reasonableness of the overhead charges that Mr.
25 Sommer was contesting.

1 Q. Finally, with respect to the exhibits, I'll
2 ask you about Exhibit 14, Sommer Exhibit 14. Mr. Sommer,
3 I believe that that's already been submitted as Energen
4 Exhibit 20 today. Have you reviewed this exhibit which
5 was prepared by Energen with respect to the Pictured
6 Cliffs overhead rates?

7 A. I did review it, and what it told me is that
8 there were lower charges going on for similarly-situated
9 wells than what was being charged by Energen as the basis
10 of its JIB costs being billed to JAS Oil and Gas.

11 Q. And JAS does not object to reasonable charges,
12 does it?

13 A. No. JAS's position is that we were willing to
14 pay a reasonable charge and Mr. Sommer's objection was
15 that the charges were not reasonable and, therefore, he
16 wasn't going to pay them, particularly in light of the
17 fact that they were collecting the revenue on the sales
18 and not paying it.

19 Q. You agree that JAS did sign a JOA for the
20 McCroden Well?

21 A. Yes, we signed the -- I signed the JIB and the
22 model operating agreement after having marked it up and
23 being told that they would not accept any changes to the
24 operating agreement. Take it or leave it was, basically,
25 the bottom line. And if we were going to invest in the

1 well, I felt that the only prospect of getting our
2 payment was to sign the operating agreement as presented.

3 Q. And the operating agreements for the deeper
4 well are substantially less than the \$806 that they're
5 asking today?

6 A. I'm not sure what their current charges are
7 but they began at \$350 per month.

8 Q. Mr. Sommer, do you have anything else that
9 you'd like to state with respect to this matter?

10 MR. HALL: I'm going to object. That's a
11 big question.

12 Q. Do you have any further comments with respect
13 to the over-production/under-production and making that
14 up and selling Sommer's share of gas?

15 A. The only comment I have to make is that the
16 statements have been shown for Exhibit 24, which was in
17 Energen's packet. I think it would be unfair to use that
18 as the basis of determining whether or not that is, in
19 fact, the amount owed. Because if an offset was shown in
20 the purchase of this well for that overpayment,
21 essentially what is credited, and then they collected it
22 again from Joseph Sommer, as the owner at the time, I
23 think they're getting paid twice. So I think that there
24 ought to be a substantiation as to the amount of the
25 imbalance.

1 Q. Mr. Sommer, were Exhibits 4, 5, 6, 7, 8 and 9
2 prepared by you or taken from JAS's business record?

3 A. They were taken from our business records.

4 MR. BRUCE: And, Mr. Examiner, obviously
5 there's some duplication -- Mr. Chairman, there's
6 obviously some duplication of exhibits. Sommer Exhibit 1
7 is the original pooling order. Sommer Exhibit 2 is the
8 amended order R-19-16-A.

9 CHAIRMAN FESMIRE: Rather than try to sort
10 them out here, why don't we just, as long as there's no
11 objection, go ahead --

12 MR. BRUCE: They're either duplicates of
13 exhibits or some Division orders, and I would ask that
14 Exhibits 1 through 14 be admitted into the record.

15 CHAIRMAN FESMIRE: Admitting that there's
16 some duplicates, Mr. Hall, do you have any objection?

17 MR. HALL: Only with respect to one
18 exhibit, 14, it's indicated that that's a copy of our
19 Exhibit 20, which shows applicable overhead charges as of
20 2009. The JAS exhibit is from 2007. Those --

21 MR. BRUCE: I would withdraw that one, Mr.
22 Chairman, and just go with Energen's Exhibit 20.

23 CHAIRMAN FESMIRE: One through 13?

24 MR. BRUCE: Yes, sir.

25 CHAIRMAN FESMIRE: Noting no objection to

1 Exhibits 1 through 13, they will be admitted to the
2 record. Exhibit 14 will be stricken and not admitted to
3 the record.

4 (Exhibits 1 through 13 were admitted.)

5 (Exhibit 14 was stricken.)

6 CHAIRMAN FESMIRE: Anything further, Mr.
7 Bruce?

8 MR. BRUCE: No, sir. I pass the witness.

9 CHAIRMAN FESMIRE: Mr. Hall?

10 CROSS-EXAMINATION

11 BY MR. HALL:

12 Q. First, Mr. Sommer, can we stipulate before the
13 Commissioners, we're friends? We've known each other --

14 A. -- for a long time.

15 CHAIRMAN FESMIRE: Everything is coming
16 out today.

17 Q. Let me ask you a couple of things about your
18 testimony. You referred to your Exhibit Number 4. Let's
19 look at that. It's the September 27, 2005 letter from
20 your father. Is it accurate to say he was demanding
21 \$15.50 MCF for gas?

22 A. If he was going to be paid directly by
23 Energen, he was demanding that that was the MCF charge
24 that was on the New York Stock Exchange that particular
25 day, or if they didn't want to pay that, he was asking

1 that they deliver the gas itself to a place where he
2 could sell it.

3 Q. By delivering the gas, what do you mean?

4 A. Tell us where you will deliver whatever the
5 imbalance is and we will find a buyer for it. Gas being
6 the fungible commodity, Energen being in the business of
7 production of gas, it has that commodity. Anywhere it
8 could do an exchange agreement, we would do the exchange
9 agreement if they would tell him where they'd deliver it.
10 That's what he was asking.

11 Q. You were asking for approximately 7,000 MCF to
12 be delivered to you FOB some warehouse?

13 A. Some transport place.

14 CHAIRMAN FESMIRE: It's in the back of the
15 truck.

16 MR. HALL: It's in the back of the truck,
17 Mr. Chairman.

18 Q. Do you have any evidence to present to the
19 Commission that anyone in the San Juan Basin ever
20 received \$15.50 for gas?

21 A. I have no evidence that anyone in the San Juan
22 Basin received that amount.

23 Q. I thought I understood you to say that there
24 was no response received from either myself or Energen?

25 A. I received no written response to this letter.

1 Q. You're not representing to the Commission that
2 no response was made at any time?

3 A. No. I just recall not receiving a written
4 response within the times required by this letter.

5 Q. You'll acknowledge the receipt of subsequent
6 letters from --

7 A. There were subsequent letters from you and
8 there were discussions with various people within Energen
9 regarding the delivery of the gas.

10 Q. So you'll have to agree that Energen was
11 responsive, not to your satisfaction, but they were
12 responsive?

13 A. Energen responded by not delivering the gas
14 and by not tendering any money. That's correct.

15 Q. But they responded in writing and in
16 conversation? Is that accurate?

17 A. They did.

18 Q. Show us this management fee you're objecting
19 to.

20 A. I don't have a copy of it in front of me.
21 What Joe was objecting to primarily was the overhead
22 charges that were being imposed upon him through the JIB
23 billing that he received. I don't have a particular -- I
24 get one every month. I did not bring one.

25 Q. So when we say, "management fees," are we also

1 speaking of the overhead and supervision fees as the same
2 thing?

3 A. I believe that it's probably one in the same
4 when you break it out.

5 Q. Let's stipulate that the JAS interest did
6 participate in the drilling of the McCroden C 1 Well.

7 A. It absolutely did participate.

8 Q. JAS signed the operating agreement along with
9 all of its exhibits; correct?

10 A. After I was told my objections to the
11 operating agreement would not be accepted, I signed the
12 operating agreement. That's correct.

13 Q. When you signed the operating agreement for
14 the McCroden Well, did you take the opportunity to review
15 the gas balancing agreement?

16 A. I did.

17 Q. And did you find it to be objectionable?

18 A. There were parts of it I found to be
19 objectionable. I marked it up. I sent it back to
20 Energen. Energen said that if I didn't like it, don't do
21 it.

22 Q. So you have agreed to the terms; is that
23 correct?

24 A. I have now agreed to the terms.

25 Q. Do you have any evidence to present to the

1 Commissioners which would establish that the lease
2 operating expenses that have been charged are
3 unreasonable?

4 A. The evidence that we have -- best evidence
5 that I could find are two things. One, the model
6 operating agreement that was presented to me on the
7 McCroden Well for 2006, was \$350. The Exhibit 20 that
8 you presented shows that there's a wide range of prices
9 being charged out there for wells of this type,
10 significantly less than the 800 and some dollars that
11 Energen is now wanting to impose upon JAS.

12 Q. I've confused you with my question. Let's
13 leave aside overhead and supervision charges and talk
14 only about lease operating expenses.

15 A. Straight lease operating expenses, JAS and its
16 predecessors do not object to.

17 Q. You're offering no evidence to the Commission
18 to establish that the charges to JAS have otherwise been
19 unreasonable; is that right?

20 A. I'm not making an objection to those
21 particular charges.

22 Q. Can you offer the Commission any evidence at
23 all that would tend to establish that the current
24 balancing statement is in any way incorrect?

25 A. Short of actually going to the well logs and

1 looking also at the purchase agreement for this well that
2 Energen did with Meridian over Energen's successor, and
3 how they treated the liability, whether they got a credit
4 for it, I can't tell you that it's correct or incorrect.
5 That purchase agreement has not been produced to me. I
6 have to take it on good faith that the number less that
7 offset that they took for 1,030 MCF would be then
8 correct.

9 Q. And we're not in disagreement, JAS is
10 receiving royalty proceeds today; correct?

11 A. It is today after an objection and a letter
12 and a demand for payment with interest.

13 Q. JAS never went to the OCD and asked the
14 Division to address well costs or overhead charges for
15 the Martinez #1 Well, did they?

16 A. Neither JAS nor Energen did until I brought a
17 lawsuit in Rio Arriba County.

18 Q. In fact, the application Energen brought
19 preceded your lawsuit; isn't that accurate?

20 A. I don't believe that is accurate. I believe
21 that I sent you a copy of the lawsuit and it was filed
22 and your subsequent submission to this Division came. If
23 you'll look at the date --

24 Q. The record will speak for itself. But the
25 fact remains, you have never asked -- JAS has never asked

1 the Division to review well costs?

2 A. No. We asked Energen to review the well costs
3 and were told that was the charge. It's very expensive
4 to bring a process --

5 MR. HALL: No more questions, Mr.
6 Chairman.

7 CHAIRMAN FESMIRE: Commissioner Bailey?

8 EXAMINATION

9 BY COMMISSIONER BAILEY:

10 Q. The point was made that Energen has not
11 produced an order for the Martinez Well. Is that a
12 requirement?

13 A. It would be a requirement in order to put it
14 in pay status, I believe, Commissioner.

15 Q. Can you explain what you're saying?

16 A. To put the pro rata share of payment to JAS's
17 pay status, i.e., that Energen would pay, they would ask
18 for a Division order to be executed. No Division order
19 has been presented to me to put it into pay status.

20 Q. Is there no recourse for working interest
21 owners when a company presents an operating agreement?

22 A. I know of no recourse other than to say,
23 "Don't sell my gas."

24 Q. Then we have a situation we have today?

25 A. That's correct. It's a take it or leave it

1 circumstance with respect to their contract.

2 Q. Do you have a copy of the Energen exhibits? I
3 have a question on one of their exhibits to see why you
4 have no objection to a charge there.

5 MR. BRUCE: Mr. Chairman, can I approach
6 the witness?

7 CHAIRMAN FESMIRE: You may.

8 Q. (By Commissioner Bailey) Exhibit 19, page 12.
9 Do you see where it says, "632 GL Account \$800.09 LOE
10 plug & abandonment"?

11 A. I do see that.

12 Q. The amount charged to JAS is \$142.40 --

13 A. I see that.

14 Q. -- for plugging and abandonment?

15 A. I do see that.

16 Q. This well is not PA?

17 A. It's not plugged or abandoned. We have just
18 been ignoring these charges all along. We're not paying
19 them until we get some sort of resolution. And because
20 there's a pending lawsuit, I haven't spent any time
21 reviewing each of these accounts. This presentation
22 would have been done in 1988 to Joe Sommer, and I don't
23 know -- he objected. If you look at some of his letters
24 back in '98, that they said this thing was plugged,
25 there's a whole lot of correspondence between Mr. Sommer

1 and Energen about the plugging and continued charges, so
2 he did object.

3 Q. But you just testified that you're not
4 objecting to any of this type of charge, only to the
5 overhead charges.

6 A. I said -- I believe my testimony was that I
7 was not objecting to the operating costs of the well, and
8 I don't object to paying a pro rata share of the actual
9 operating costs of the well. I think that's fair in the
10 production of the well. What was being objected to were
11 unfair charges that were being appended to the operating
12 JIB costs that were being submitted without any
13 discussion.

14 Q. Is it normal for an operator to send copies of
15 invoices for work-over?

16 A. It's normal if they're requested. They have
17 an obligation to submit those costs, Commissioner.

18 Q. Do they do that for you on a regular basis?

19 A. No. All we get is a line item statement such
20 as what was presented in -- this would be Exhibit 5 --
21 I'm sorry. It would have been Exhibit 9, is all I get on
22 a monthly basis.

23 COMMISSIONER BAILEY: That's all I have.

24 CHAIRMAN FESMIRE: Commissioner Olson?

25 COMMISSIONER OLSON: I have no questions.

EXAMINATION

1

2 BY CHAIRMAN FESMIRE:

3 Q. Mr. Sommer, how deep is the Martinez Well? Do
4 you know?

5 A. I am not certain of its depth, but I
6 understand that it's in the range of 5,000 feet.

7 Q. Now, at one point you were talking about the
8 1984 Joint Operating Agreement that wasn't signed?

9 A. That's correct.

10 Q. And you indicated that the \$350 per well was
11 not objectionable; is that correct?

12 A. I believe that the 350 charge, from what I
13 understand of wells of this nature and my own experience,
14 is a reasonable charge from a monthly basis.

15 Q. In 1984?

16 A. Not in 1984, in 2006, when I signed for the
17 McCroden Well.

18 Q. That may be the problem. What is that cost in
19 the 1984 agreement?

20 A. I'm not sure what it was in the 1984
21 agreement. I don't believe I've ever seen the 1984
22 agreement.

23 Q. So when you said that \$350 per well was not
24 objectionable, you were talking about a current time?

25 A. That's correct.

1 Q. Have you made arrangements to sell the gas?

2 A. If I would have been delivered the gas in
3 October, within that time period, or told where I could
4 have had it picked up, I would have made arrangements to
5 sell it and I did have a buyer.

6 Q. You did have a buyer?

7 A. I had a buyer in San Juan who was willing to
8 do the deal with us. Because this was in the San Juan
9 Basin, I was assuming it could be delivered physical
10 quantities someplace within that basin.

11 Q. So you said the \$350 per well would be a
12 reasonable cost. Is that a 1. -- or is that part of a
13 range or -- what do you think would be a reasonable cost
14 to operate this 5,000-foot well?

15 A. Today?

16 Q. Yes.

17 A. Probably in the neighborhood of \$400 is what I
18 believe that they would be trading at today per well, an
19 operating agreement.

20 Q. You made an interesting statement that I
21 didn't follow. You were comparing the cost and you said
22 that means that they're getting paid twice for this. Do
23 you remember which exhibit that was?

24 A. It wasn't an exhibit. I was referring to the
25 fact that at the time that Energen purchased this well

1 from Meridian, there was an overpayment due both to
2 Meridian's -- or Energen's status as they acquired it and
3 to Sommer, is what they were saying, that we'd been over
4 paid. In any normal transaction those would have been
5 offset from the price of the well. So if they took it as
6 an offset for money that would have to be paid, I believe
7 that collecting it again from us would be collecting it
8 twice.

9 Q. So they took it as an offset in the sale. Did
10 they take your portion as an offset in the sale?

11 A. I'm not sure how they dealt with our portion
12 in that purchase agreement.

13 Q. That would make a big difference in your
14 statement.

15 A. It would. And I said subject to reviewing and
16 auditing that statement would be the appropriate way to
17 deal with that imbalance, whether it was accurate. That
18 was what I said.

19 Q. Now, turning to your Exhibit 4, now, you
20 indicated that you had a buyer. Were you talking about
21 that you had a buyer in September of 2005?

22 A. Yes, that's correct

23 Q. Without getting into the specifics of who it
24 was, can you tell me how that would have worked?

25 A. Because gas fungible, if Energen had at the

1 time is 6 or 7,000 MCF in the San Juan Basin, all I had
2 to do was find a buyer and say, "Take that from them and
3 pay us." They'd take an offset of their credit or from
4 their reserves or their storage.

5 Q. And you indicated that you were presented with
6 a copy of the Model Form Operating Agreement for the
7 McCroden Well?

8 A. That's correct

9 Q. And that you made some changes and that they
10 weren't acceptable to Energen. What changes -- what were
11 the major changes you wanted to make in the operating
12 agreement?

13 A. Some of the major changes were to strike or
14 add words such as "reasonableness," strike
15 indemnification language or, if there is indemnification
16 language, to make it mutual. And there was
17 indemnification language in there. Changes of that
18 nature. I wasn't changing the financial terms that were
19 being presented. I was changing terms and conditions
20 that were set forth in that document. I marked it up,
21 sent it off to them. I was told that not a single change
22 was acceptable.

23 Q. And you realize that these AAPL forms have
24 been tried and tested for a long time and they've been
25 modified occasionally. And I'm not saying this to be

1 snotty, but it's going to come across that way. What
2 made you think that you had a better idea than all these
3 other people that have been doing this for a long time?

4 A. It's not that I had a better idea. Being a
5 lawyer and looking at documents that require that I
6 indemnify somebody for something makes me cringe. There
7 are provisions in that document that I didn't find
8 reasonable. It was up to me to ask. The worst they're
9 going to tell me is, "No, we can't do it," or, "No, we
10 won't do it."

11 Q. So it didn't bother you to be making changes
12 to what had been a pretty tested form?

13 A. Well, Mr. Chairman, with all due respect, it's
14 a tested form that's been presented -- prepared by the
15 majors to impose upon the little people. It didn't
16 bother me to ask for the changes because I'm used to
17 doing it every single day in my line of work.

18 Q. Okay. I'm not going to argue with you on that
19 one. Why was JAS not being paid on the McCroden Well?
20 You know, you indicated that you had to discuss a
21 lawsuit. And why were you not being paid on another
22 well? Was it the same lease, same deal?

23 A. The recent payment discrepancy or imbalance
24 that is shown on the McCroden Well, I wrote a letter and
25 asked that I get paid.

1 Q. So you were being partially paid?

2 A. I was being paid until about three months ago,
3 and I don't know what happened. They started accruing an
4 imbalance and I didn't understand it. So I was getting
5 the bills, obviously, for the operation, so I wrote and
6 said, "I'm willing to pay this, but I also want to get
7 paid for what you sold. You don't have a right to do an
8 imbalance on me," is what I was telling them.

9 Q. You did have a gas balancing agreement with
10 them on that?

11 A. Yes, I did.

12 Q. Surely they gave you some reason for
13 implementing the gas balancing agreement, didn't they?

14 A. No. I had no reason for the gas balance. We
15 had an agreement they'd sell it and I'd get paid. The
16 gas imbalance, I don't know why it started all of a
17 sudden.

18 Q. Do you have a larger interest in the McCroden
19 Well than -- how do you say that?

20 A. McCroden.

21 Q. Do you have a larger interest than the
22 Martinez Well?

23 A. No. It's the same interest.

24 Q. Is it the same lease?

25 A. It's a different lease, as I recall.

1 Q. So you don't know why they ceased paying you
2 on that?

3 A. No. I've written a letter fairly recently. I
4 don't anticipate a response until a week or two.

5 Q. Do you have any reason to believe it was part
6 of this dispute or part of the lawsuit?

7 A. No. I think there's some glitch some place.
8 I just -- I'm not sure. I've been paid fairly regularly
9 since we signed the model operating agreement, and we've
10 been paid our pro rata share of the cost of the well.

11 Q. All of the problems then relate to the
12 Martinez Well?

13 A. That's correct.

14 Q. Now, the Division order -- I believe
15 Commissioner Bailey asked you about the Division order --
16 it's not a legal requirement, is it?

17 A. It is not a legal requirement. Payors like to
18 get them so that they're assured if somebody gets paid
19 erroneously, they're going to get their money back.
20 That's why people ask for it.

21 Q. But here are transactions that occur without a
22 Division order?

23 A. Absolutely, as is the case here. We're paid
24 on our royalty interest without a Division order.

25 Q. You heard this morning that the Martinez Well

1 is making about 24 MCF per day?

2 A. I did hear that.

3 Q. Is that similar -- have you ever looked at the
4 engineering or the reserves on this month?

5 A. I have not. I've been told what the engineers
6 were when I was discussing a settlement at one point with
7 Energen, but I did not actually see the engineering
8 reports. It wouldn't surprise me that the 24 is an
9 accurate number.

10 Q. And do you have any idea what the reserves or
11 the life of this well would be?

12 A. I have no idea what the reserves of the life
13 of the well are, but I have concerns that it won't out
14 live the imbalance that's there.

15 Q. I need to ask you, you realize that gas
16 balancing takes place in the oil field real regularly,
17 real often?

18 A. I understand.

19 Q. Is it your position that it shouldn't be
20 occurring here because there is no gas balancing
21 agreement?

22 A. It's my position that it ought not to be
23 occurring here because the pooling order in 1961 did not
24 provide for it. The terms of which they want to impose
25 on the gas balancing are terms in a contract that have

1 not been agreed to by JAS. So I don't believe that a gas
2 balancing in this particular circumstance is appropriate
3 where the seller of the gas keeps 100 percent of the
4 proceeds and charges you for your pro rata share of the
5 operation and pays you none of the money received.

6 Q. But that's the way it's done under gas
7 balancing agreements often.

8 A. If there's an agreement, that's correct.

9 Q. And your position is that you've never agreed
10 to that, that the State has never ordered it, you never
11 agreed to it, that, therefore, it shouldn't be --

12 A. It shouldn't be imposed upon us by the
13 operator of the well. That's my position. Because the
14 State hasn't ordered it and there is no agreement to the
15 contrary.

16 CHAIRMAN FESMIRE: I have no further
17 questions. Mr. Bruce, do you have any redirect of this
18 witness?

19 MR. BRUCE: No, I don't.

20 CHAIRMAN FESMIRE: Mr. Hall, I assume
21 since there's no redirect, your recross is going to be
22 extremely short.

23 MR. HALL: No more questions for Mr.
24 Sommer. Can I take a minute -- is there other witnesses
25 to be presented?

1 MR. BRUCE: No, sir.

2 MR. HALL: May I take a moment to confer
3 with my client? We may present some rebuttal evidence.

4 CHAIRMAN FESMIRE: Okay. Why don't we
5 take about a 10-minute break?

6 (A recess was taken.)

7 CHAIRMAN FESMIRE: The record should
8 reflect that this is the continuation of Case Number
9 13957, that Mr. Hall has asked to recall Mr. Rote.

10 Mr. Rote, you understand that you've been
11 previously sworn in this case and that you're still sworn
12 for the entire testimony given in this case?

13 MR. ROTE: Yes, sir.

14 CHAIRMAN FESMIRE: Mr. Hall?

15 MR. HALL: For the record, Mr. Chairman, I
16 apologize for the delay. I appreciate the Commission's
17 indulgence.

18 PAUL ROTE

19 FURTHER REDIRECT EXAMINATION

20 BY MR. HALL:

21 Q. Mr. Rote, you were present for the examination
22 of Sommer just now, were you not?

23 A. Yes, sir.

24 Q. One question came up with respect to operating
25 expenses for the well in our Exhibit 19. Commissioner

1 Bailey pointed out that there was a charge for plugging
2 and abandonment in 1998. Do you recall that?

3 A. Yes, I do.

4 Q. Tell us again when Energen acquired the well.

5 A. Latter part of 1997, early part of 1998.

6 Q. Was the well plugged and abandoned?

7 A. No. It was producing at the time.

8 Q. Why would there have been an \$800 charge shown
9 on Exhibit 19 on page 12?

10 CHAIRMAN FESMIRE: Mr. Hall, I think
11 that's an account number. I think the amount is 142.40.

12 A. Yeah. We believe that that would have been to
13 post a plugging bond with the State as required, and that
14 was a gross charge, not net, to the Sommer interest. All
15 these charges are gross, not net interests. I also point
16 out if you look further down that exhibit page under,
17 "Environmental compliance," you can see that some charge
18 was attempted to be made for that charge under the
19 environmental compliance category it was booked to there.
20 Apparently, it was netted out and moved back up to plug
21 and abandonment category, and I can assume that that
22 would be for a plugging bond.

23 Q. We also heard Mr. Sommer testify with respect
24 to payments for the JAS participation in the McCroden
25 Well. I don't want to get the two wells confused. But

1 did you understand Mr. Sommer to say that he's not
2 receiving payment for production from the McCroden Well?

3 A. That's my understanding. That's what he said,
4 yes.

5 Q. Did your staff in Birmingham receive a letter
6 recently from Mr. Sommer making that assertion?

7 A. We received that letter yesterday, Tuesday,
8 sometime during the day. It was forwarded -- emailed to
9 Mr. Hall and myself yesterday afternoon.

10 Q. Did you have your staff confirm whether or not
11 payment was being made by Energen to the JAS Oil and Gas
12 Company for production from the McCroden Well?

13 A. Yes, we did.

14 Q. Let's look at Exhibit Number 29. Can you
15 identify that for us, please?

16 A. This is a check payable to JAS Oil and Gas
17 dated May 25th of this year, '09, for \$87.26 representing
18 his net proceeds from sale of gas for the months of
19 February and March.

20 Q. Let's clear up one more issue with respect to
21 participation in the Martinez Well and the McCroden Well.
22 In either case the JAS interests are not under lease; is
23 that right?

24 A. That's correct.

25 Q. For participation in the McCroden Well, did

1 JAS participate with 100 percent of its working
2 interests?

3 A. Yes, it did.

4 Q. Its unleased mineral interests?

5 A. Yes.

6 Q. And is the Mesaverde Formation spaced on 320
7 acres? Do you know?

8 A. Yes. I believe it is.

9 Q. Would that result in a smaller participation
10 factor for JAS in the McCroden Well than in the Martinez
11 Well?

12 A. Yes. You'd have a lesser gross interest.

13 Q. Is Exhibit 29 a true and exact copy of the
14 revenue checks issued by Energen to its interest owners
15 in wells, in this case JAS Oil and Gas Company?

16 A. Yes, it is.

17 MR. HALL: That concludes my redirect of
18 this witness. I'll move the admission of Exhibit 29.

19 CHAIRMAN FESMIRE: Any objection?

20 MR. BRUCE: No objection.

21 CHAIRMAN FESMIRE: Exhibit 29 will be
22 admitted.

23 Mr. Bruce, do you have a cross-examination of
24 the witness?

25 (Exhibit 29 was admitted.)

1 MR. BRUCE: I don't think so, Mr.
2 Chairman.

3 CHAIRMAN FESMIRE: Commissioners?

4 COMMISSIONER BAILEY: No.

5 CHAIRMAN FESMIRE: Mr. Rote, thank you
6 very much. Mr. Hall, do you have a close?

7 MR. HALL: Mr. Chairman, Commissioners, I
8 think the presentation of evidence to you today, the
9 whole panoply of correspondence back and forth between
10 well operator and interest owner JAS makes clear to you
11 the situation that the operator has been placed in over
12 the years and the efforts that the operator has made to
13 try to correct that situation.

14 Let's review the history of the Sommer JAS
15 position throughout as evidenced by the exhibits. First
16 of all, there were broad objections to the overhead
17 rates. There were broad, unspecified objections to lease
18 operating expenses, but nowhere today did JAS present to
19 you any evidence to rebut the reasonableness of either
20 the overhead rates or the operating expenses.

21 The evidence presented to you is what it is,
22 and that's what you must base your decision on. That is
23 part of the function of the Division and the Commission.
24 If there is an issue with respect to operating expenses
25 under a Compulsory Pooling Order, then recourse may be

1 had to the agency to address that. Sommer JAS never did
2 that. We did.

3 We're asking that the 1961 vintage pooling
4 order be updated to establish that past operating
5 expenses, current operating expenses, past historic
6 overhead and current overhead are reasonable and
7 appropriate. We ask that those provisions be included in
8 a new order to be issued by the Commission.

9 Let's look at the other issue this application
10 presents you. Over the years there was a market for gas.
11 That market went away in the 1990s. The market changed.
12 The nonoperator was directed to make arrangements for
13 marketing its share of gas and advise the operator of its
14 plans or it would be placed into an under-produced
15 imbalancing situation.

16 JAS Sommer never addressed that. Instead,
17 what JAS did, JAS took the position that the operator
18 cannot market its share for it. And at the same time,
19 you cannot -- the operator could not market its own share
20 of gas unless 100 percent of the interest owners were
21 being marketed, then none of the interest owners could be
22 marketed. The practical effect of that position is to
23 require a shut-in of the well. That's an impractical
24 position to take, because it's within practices of the
25 industry.

1 JAS Sommer took at times different positions.
2 Ultimately they took a position that you can't market my
3 working interest share. You have to pay me for my
4 royalty. You can only market so much of my working
5 interest share, my force-pooled seven-eighths share, as
6 necessary to cover monthly operating expenses. The
7 testimony establishes today that that is simply not
8 possible. That would require an operator to know in
9 advance what its expenses may be and does not account for
10 unanticipated expenditures that might arise.

11 It is not possible for an operator to schedule
12 gas sales in advance to cover future upcoming expenses.
13 It's just not practicable. Sommer offered no testimony
14 or evidence establishing that it would be possible to do
15 that.

16 Finally, after all of this back and forth of
17 correspondence between the parties for years and years,
18 this application, a previous examiner hearing, JAS
19 Sommer presents us with a new position, and I think that
20 new position offers us a way out here. If you look at
21 the Sommer prehearing statement, on page 5, Sommer has
22 taken for the first time this position. JAS Sommer now
23 says Energen must sell Sommer's share of gas, deduct
24 overhead costs, account to Sommer and pay Sommer its
25 share of proceeds. That is exactly what we were asking

1 to do.

2 Now, practicably how does the Commission
3 fashion an order to accomplish that? It seems to me
4 there are two ways to go about it. The order could
5 provide, as Energen has offered, to allow Energen, the
6 operator, to market the JAS share of gas for it at an
7 inflated entitlement of 40 percent to allow it to make up
8 under-production that has accrued for 12 years, make that
9 under-production up sooner than it would be able to
10 otherwise.

11 This under-produced position did not accrue
12 overnight. It took a number of years for it to grow to
13 this situation, but I think the evidence shows you that
14 Sommer simply would not allow the operator to deal with
15 it. There's no way out for the operator. What the
16 operator can do under the Commission's own rule, Rule 14,
17 is ask you to fashion relief to get it out of that
18 situation. It can allow for the inflation of the
19 interest, allow the operator to market the nonmarketing
20 party's share or, alternatively, as the evidence shows
21 you in the correspondence, the order can provide that the
22 operator can buy out the under-produced position of JAS
23 in accordance with the custom and practice of the
24 industry.

25 And that custom and practice was established

1 by our Exhibit 18, the Exhibit A to the Joint Operating
2 Agreement, that is the gas balancing agreement, that is
3 the template, I believe, for the Commission to fashion
4 relief here, and take any one or all of the remedies that
5 are set forth in the gas balancing agreement and apply
6 them to this dispute.

7 The gas balancing agreement allows for
8 inflated entitlement to make up an imbalance of actual
9 production or it authorizes a buy-out.

10 If you'll look at page 3 of the gas balancing
11 agreement, paragraph 7(b), that is the buy-out provision.
12 It says on depletion -- if there is concern about the
13 well being able to make up the past imbalance on
14 depletion, then the operator shall account to and pay the
15 nonmarketing party based on historic prices received for
16 production. That is cash balancing. And you will also
17 see that it's the custom and practice in the industry
18 that those buy-outs not accrue interest.

19 It's just inconceivably incorrect that gas
20 that's left in the ground should accrue interest on it
21 when that nonmarketing party has not made the effort to
22 market its own share. That's what the balancing
23 agreement provides for. I think either of those two
24 remedies offer appropriate relief that the Commission can
25 look to and afford the well operator in this case. Thank

1 you, Mr. Chairman.

2 CHAIRMAN FESMIRE: Mr. Bruce, close?

3 MR. BRUCE: Mr. Chairman, once again
4 there's a couple of issues. The first one is the
5 overhead rates. I think my co-counsel, Ms. Lee, during
6 the break told me what I think is the proper view of
7 this.

8 Energen is punishing Sommer for not signing a
9 JOA. They signed one on the deeper well two, three years
10 ago, and the overhead rates are \$350 a month, and here
11 today they want \$866 for a shallower well where there is
12 no JOA. I just think that's unconscionable.

13 Their Exhibit 20 on the overhead rates shows
14 that most people are charging 4 or 450 bucks a month
15 charge. To charge 866 bucks a month at this time is just
16 improper and, apparently, they have been charging that
17 amount or lesser amounts escalated ever since they've
18 taken over, or I should say at that point, de-escalated
19 ever since they've taken over the well.

20 If you look at one of the Sommer's exhibits,
21 it shows that in October of 2007, before the hearing was
22 held before the Examiner in this matter, they were
23 charging \$748 a month, so they had been taking advantage
24 of this. And, obviously, anything you have to look at, I
25 think you'd have to go back for those seven years -- or

1 excuse me -- 12 years now since Energen took over, and
2 reduce the amounts. If you set whatever the rate is
3 today, I think that rate has to be decreased going back
4 over 12 years to set a fair amount, because Energen has
5 not shown what it has charged every month since it took
6 over.

7 Obviously, I think it has been taking those
8 rates, the \$350 a month, from 1984 and escalated it, and
9 I think those are improper rates. They're too high.
10 When it comes to the over- and under-production, you
11 know, for better or worse, we're not dealing with
12 voluntary agreements here today. We're dealing with a
13 forced pooling order. There is no JOA in place. And
14 what you get to is this: There's a force pooling order
15 in place, but Energen is using its nonpayment of Sommer
16 to force Sommer to sign a JOA and/or a gas balancing
17 agreement and/or a gas marketing agreement.

18 Now, I've always told my clients that force
19 pooling orders, as bare bones as they are, operate as
20 JOAs, for better or for worse. But when an operator
21 seeks and obtains relief under the State's force pooling
22 jurisdiction, then that's what they have to go under. So
23 what you have to look at is the force pooling statutes
24 and the force pooling order.

25 And, of course, the more I do this work, the

1 more that's unclear to me. But I think you take a look
2 at the practicalities of the situation. And I had -- the
3 reason I had enclosed my Exhibit 3 -- and, unfortunately,
4 I don't see the last page in here -- Exhibit 3 of my
5 packet is Order Number R-13000. I chose this one since
6 it was a fairly recent pooling order and since it doesn't
7 involve Energen or my client or any of my clients.

8 But under a modern force pooling order, they
9 all provide that their unlocateable mineral interest
10 owners, the operator, whether or not it's before or after
11 payout or anytime, has to sell that person's share of gas
12 and place it in a bank account in the county in which the
13 well is located. And my clients do that whether or not
14 it's before or after pay-out. My point is why treat an
15 unlocateable interest owner better than a person you can
16 locate? I see no reason.

17 I think that any time there is a force pooled
18 interest owner and whether or not they go nonconsent in
19 the well, the operator ought to be selling that gas and
20 accounting to and paying to that interest owner as a
21 matter of course, because that's the only fair way to do
22 it. And the reason I say it's only fair to do it, is
23 because, more and more these days -- now, Mr. Sommer has
24 at least some experience in the Oil and Gas business.
25 But how many small, nonconsenting mineral interest owners

1 are there out there who I am force pooling on a weekly
2 basis for my clients who know very little about the
3 business?

4 They're expected to keep track of all this
5 stuff and to go out and market gas. It's just not going
6 to happen. So for a practical matter, for them to
7 receive any revenue at all, the operator has to go out
8 and sell the gas.

9 Another factor is operators of a well often
10 change. They might even go out of business. What
11 happens to the over- and under-production at this point?
12 Fortunately, in this case we are dealing with two
13 reputable operators, Energen and Burlington Resources,
14 and they kept balances. That's not always going to
15 happen.

16 Furthermore, if you look at under-production,
17 if it was made up today -- I think Mr. Rote said that,
18 but I always understood under-production should be made
19 up at cash balancing. If it was cash balancing, like Mr.
20 Hall said, it would be at the prices received at the date
21 the gas was sold. Now, who's going to have that data?
22 It's going to be the old operator. If there's a change
23 of operator over the next 49 years, what's going to
24 happen to that information? Another impracticality
25 you're imposing upon small interest owners.

1 Furthermore, if Energen must sell gas to pay
2 Sommer's one-eighth royalty share, and under the revised
3 order, to sell enough gas of Sommer's to cover operating
4 costs, how much more difficult is it to just -- since
5 they have a complete division of interest, just to have
6 the machine issue the check and sent it to Sommer? I
7 just see it as a practical matter. As a practical
8 matter, Energen must sell Sommer's share of gas, as we
9 stated in the prehearing statement, deduct the overhead
10 costs and account and pay.

11 But in this instance, there's also another
12 problem, which is you have to pay the past due amounts.
13 I mean, from what I heard here today, this well isn't
14 going to produce 49 years. If it did, I'd be stunned.
15 But it is -- assuming it does, just to pay out over 49
16 years, as Mr. Sommer said, at no interest, who's getting
17 the benefit of that? It's the operator. I think the
18 operator, if they want to operate, they should sell the
19 gas under a forced pooling order and pay Sommer the
20 amount due.

21 And insofar as anything that I raised in the
22 past as to past due amounts, there's an issue of the
23 Division issuing retroactive relief. We don't think any
24 retroactive relief should be granted in this case so far
25 as operating costs go, so we can leave that to the

1 parties and their pending lawsuit, I think.

2 CHAIRMAN FESMIRE: Mr. Bruce, what exactly
3 does that lawsuit cover?

4 MR. BRUCE: Boy, it's been a while
5 since -- it's been dormant.

6 CHAIRMAN FESMIRE: Mr. Hall?

7 MR. HALL: It purports to be -- I think it
8 purports to establish a class action for other interest
9 owners similarly situated. It purports to state tort
10 claim under a conversion theory. I think it also asks
11 for an accounting in payment.

12 MR. BRUCE: It asks for accounting in
13 payment under the Oil and Gas Proceeds Payment Act.

14 CHAIRMAN FESMIRE: So that sort of renders
15 moot any discussion in this forum of past due amounts or
16 past due expenses, doesn't it?

17 MR. HALL: I would disagree. I think
18 that's a matter of primary jurisdiction for the Division,
19 and we've filed motions to stay the District Court
20 litigation pending this agency action. There's a partial
21 order of stay now. We don't have a judge at the moment.
22 But we have argued and continued to argue that the
23 Division has continuing jurisdiction over its pooling
24 orders, particularly with respect to operating costs,
25 overhead issues, statute mandates, that the Commission

1 assumes jurisdiction over those issues. It's where
2 parties go for redress on these issues.

3 CHAIRMAN FESMIRE: I agree with you on
4 that respect, but if it's a class action suit --

5 MR. HALL: It has not been certified for a
6 class action suit, and I don't believe it can be.

7 MR. BRUCE: As to -- Mr. Chairman,
8 certainly if the Division came out and said let's just
9 take Energen's position, that the overhead rates should
10 be \$866 per month, does that mean they're ratifying all
11 past overhead rates charged by Energen going back to 1997
12 or so? If -- or if you took our position and cut that in
13 half and say, well, what are the rates going to be in
14 '97, '98, '99, et cetera?

15 MR. HALL: I'll address that point that
16 the statute has no limitation on it. It says the
17 Division is to address any dispute over costs. It may do
18 it retroactively, and I think we can provide you with
19 orders where the agency has accorded retroactive relief.
20 Santa Fe Exploration/Stevens operating case that went
21 through the Supreme Court comes to mind where the agency
22 retroactively established an allowable with a pool with
23 three producing oil wells which resulted in some parties
24 being under-produced, others being over-produced and
25 provided a remedy for that going forward. This doesn't

1 seem to be too far a departure from that type of relief.
2 And I think that's also the very reason that this
3 Commission saw fit to adopt Rule 414, is to provide
4 operators and nonoperators with recourse to address this
5 very situation.

6 CHAIRMAN FESMIRE: You don't happen to
7 know the renumbered Rule 414, do you?

8 MR. HALL: I do. It's our Exhibit 25.
9 It's 19.15.24.8, and the order is R-8361. It's in the
10 book, as well.

11 CHAIRMAN FESMIRE: Mr. Bruce, one of the
12 things that your client has asked for is interest and --

13 MR. BRUCE: Yes, correct, Mr. Chairman. I
14 don't think you have the jurisdiction to award that.

15 CHAIRMAN FESMIRE: That was going to be my
16 question, because we had this argument before.

17 MR. BRUCE: Argument? Discussion.

18 CHAIRMAN FESMIRE: Commissioner Bailey,
19 anything else?

20 COMMISSIONER BAILEY: No.

21 CHAIRMAN FESMIRE: No? Mr. Olson?

22 COMMISSIONER OLSON: No.

23 CHAIRMAN FESMIRE: This is an incredibly
24 interesting legal case. Thank you all for bringing it to
25 us, especially on a day when we have a long afternoon. I

1 appreciate the presentations from both attorneys and
2 thank you. If there's nothing else in this case, we will
3 recess and convene in executive session. What we're
4 going to do when we do that, is normally and from this
5 point forward -- Mr. Hall, I didn't get a chance to tell
6 you -- we're going to be asking for recommended
7 conclusions and findings, even in the one-day cases and
8 anything like that.

9 But since I didn't give you all a chance to
10 talk about that today, what we're going to do is go ahead
11 and deliberate and figure out how we want to structure
12 the decision and transmit that to the attorneys and ask
13 them to draft proposed findings and conclusions of the
14 proposed order.

15 MR. HALL: One housekeeping matter. Did
16 we get Exhibit 29 into the record?

17 CHAIRMAN FESMIRE: I thought we did.

18 MR. BRUCE: We did. I did not object to
19 it.

20 CHAIRMAN FESMIRE: Let the record reflect
21 that Energen Exhibit 29 has been admitted into the record
22 and will be made part of the official record. Anything
23 else in Cause Number 13957?

24 MR. HALL: No, sir.

25 MR. BRUCE: No.

1 CHAIRMAN FESMIRE: Thank you very much.

2 At this time we'll take a quick break and go into
3 executive session.

4 (The Commission went into executive session.)

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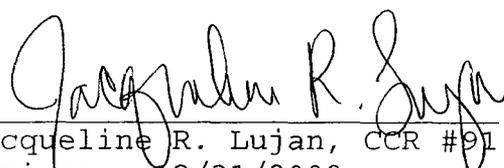
REPORTER'S CERTIFICATE

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I, JACQUELINE R. LUJAN, New Mexico CCR #91, DO
HEREBY CERTIFY that on May 27, 2009, proceedings in the
above captioned case were taken before me and that I did
report in stenographic shorthand the proceedings set
forth herein, and the foregoing pages are a true and
correct transcription to the best of my ability.

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

WITNESS MY HAND this 9th day of June, 2009.


Jacqueline R. Lujan, CCR #91
Expires: 12/31/2009