

**STATE OF NEW MEXICO
ENERGY, MINERALS AND NATURAL RESOURCES DEPARTMENT
OIL CONSERVATION DIVISION**

**IN THE MATTER OF THE HEARING
CALLED BY THE OIL CONSERVATION
DIVISION FOR THE PURPOSE OF
CONSIDERING:**

**APPLICATION OF CIMAREX ENERGY CO. FOR A NON-STANDARD OIL
SPACING AND PRORATION UNIT AND COMPULSORY POOLING, LEA
COUNTY, NEW MEXICO**

**CASE NO. 14390
ORDER NO. R-13217**

ORDER OF THE DIVISION

BY THE DIVISION:

This matter came on for hearing at 8:15 a.m. on October 29, 2009, at Santa Fe, New Mexico, before Examiner William V. Jones.

NOW, on this 1st day of February, 2010, the Division Director, having considered the testimony, the record and the recommendations of the Examiner,

FINDS THAT:

(1) Due public notice has been given, and the Division has jurisdiction of this case and of the subject matter.

(2) Cimarex Energy Co. ("Cimarex" or "Applicant"), seeks an order:

(a) Creating a non-standard 160-acre oil spacing and proration unit (the "Unit") for oil production from the Bone Spring formation, including, but not necessarily limited to the South Quail Ridge-Bone Spring Pool (50461), within the N/2 S/2 of Section 34, Township 19 South, Range 34 East, NMPM, Lea County, New Mexico; and

(b) Pooling all uncommitted interests within this unit.

(3) In addition, Cimarex seeks an order pooling all uncommitted interests from surface to the base of the Bone Spring formation as follows:

The NW/4 SW/4 of Section 34 to form a standard 40-acre oil spacing and proration unit for all formations or pools spaced on 40 acres within this vertical extent, which presently include, but are not necessarily limited to the South Quail Ridge-Bone Spring Pool (50461), the Northeast Lea-Delaware Pool (37584), the Undesignated Northeast Lea- Grayburg Pool (96325), the Undesignated Pearl-Grayburg Pool (96725), the Undesignated Pearl-Queen Pool (49780), and the Undesignated Pearl-Seven Rivers Pool (49840).

(4) The proposed Unit is to be dedicated to Applicant's Mallon 34 Fed Well No. 16 (API No. 30-025-32818 "the proposed well"), to be entered at its existing surface location 1980 feet from the South line and 660 feet from the West line (Unit L) of Section 34 and drilled horizontally within the Bone Spring formation to a bottomhole location 1980 feet from the South Line and 330 feet from the East line (Unit I) of Section 34, Township 19 South, Range 34 East, NMPM, Lea County, New Mexico.

(5) The Mallon 34 Fed Well No. 16 is an existing vertical oil well that was completed and produced since 1997 at approximately 10,140 feet in the Bone Spring formation, South Quail Ridge-Bone Spring Pool. Cimarex sees potential to increase production and recover additional hydrocarbons by drilling horizontally from this surface location in an easterly direction at depths of 10,840 feet, still within the Bone Spring formation.

(6) The horizontal well is expected to produce from all four of the penetrated 40-acre oil spacing and proration units within this proposed nonstandard 160-acre unit.

(7) Entering this existing well and drilling horizontally in the Bone Spring is expected to cost approximately 2.6 million dollars which was reported by Cimarex to be less than the cost of drilling a new well beginning from the surface.

(8) The N/2 S/2 of Section 34 is comprised of a single Federal lease. Within the proposed Unit or Units, all parties owning interests were located and at least three parties have chosen not to participate in the drilling of this horizontal well.

(9) Notice of the proposed 160-acre non-standard oil spacing and proration unit was provided to all surrounding affected parties within the Bone Spring formation.

(10) Notice of the proposed compulsory pooling application was provided to those parties not already committed to the drilling of this proposed horizontal well.

(11) Hyde Oil and Gas Corporation, an owner within the proposed 160-acre unit, entered an appearance in this case, but did not appear at the hearing. Cimarex reported at the hearing that it had reached an agreement with Hyde.

(12) Pear Resources and Fuel Products, Inc., as surrounding affected parties, entered appearances in this case but did not appear at the hearing.

(13) No other party appeared at the hearing, or otherwise opposed the granting of these applications.

(14) The evidence presented in this case was focused on the horizontal well costs and procedure as well as the overhead rates to be charged for horizontal wells. However, the case as presented (wholly by affidavit) did not contain evidence of estimated costs or allocation of costs to potential bailout intervals uphole in this wellbore. The likelihood is that costs for vertical well completions and overhead rates would be significantly different from costs to drill and operate a horizontal well. It would not be fair and reasonable to burden non-consenting parties' interests in production from shallower zones that could be recovered from an existing well with recovered costs of the proposed horizontal project.

(15) Applicant's request to pool uncommitted interests within the NW/4 SW/4 of Section 34 for vertical well, 40-acre oil spacing and proration units from surface to the base of the Bone Spring formation, should be denied.

(16) This existing vertical well was drilled in 1997 and has been on production from the Bone Spring for 13 years. Cimarex is proposing to target a deeper horizon in the Bone Spring than is currently producing for purposes of an East-West horizontal oil well.

(17) Approval of the proposed non-standard 160-acre spacing and proration unit will enable Applicant to drill a horizontal well that will efficiently produce the reserves underlying the Unit, thereby preventing waste, and will not impair correlative rights.

(18) Two or more separately owned tracts are embraced within the Unit, and/or there are royalty interests and/or undivided interests in oil and gas minerals in one or more tracts included in the Unit that are separately owned.

(19) Applicant is an owner of an oil and gas working interest within the Unit. Applicant has the right to drill and proposes to drill the proposed well to a common source of supply within the Unit at the proposed location.

(20) There are interest owners in the Unit that have not agreed to pool their interests. There are no un-locatable interest owners or evidence of a title dispute.

(21) To avoid the drilling of unnecessary wells, protect correlative rights, prevent waste and afford to each interest owner the opportunity to recover or receive without unnecessary expense its just and fair share of hydrocarbons, this application should be approved by pooling all uncommitted interests, whatever they may be, in the oil and gas within the proposed horizontally completed 160-acre Bone Spring spacing and proration unit.

(22) Cimarex Energy Co. of Colorado (162683) should be designated the

operator of the proposed well and of the Unit.

(23) Any pooled working interest owner who does not pay its share of estimated well costs should have withheld from production its share of reasonable well costs plus an additional 200% thereof as a reasonable charge for the risk involved in drilling the well.

(24) Reasonable charges for supervision (combined fixed rates) should be fixed at \$7,000 per month while drilling and \$700 per month while producing, provided that these rates should be adjusted annually pursuant to Section III.1.A.3. of the COPAS form titled "*Accounting Procedure-Joint Operations*."

IT IS THEREFORE ORDERED THAT:

(1) A non-standard 160-acre oil spacing and proration unit (the "Unit") is hereby established for production from the Bone Spring formation within the South Quail Ridge-Bone Spring Pool (50461), consisting of the N/2 S/2 of Section 34, Township 19 South, Range 34 East, NMPM, Lea County, New Mexico.

(2) All uncommitted interests, whatever they may be, in the oil and gas within the Bone Spring formation (South Quail Ridge-Bone Spring Pool) underlying the Unit, are hereby pooled.

(3) The portion of this application seeking to pool all uncommitted interests from surface to the base of the Bone Spring formation within the NW/4 SW/4 of Section 34 to form a standard 40-acre oil spacing and proration unit for all formations or pools spaced on 40 acres within this vertical extent is denied.

(4) The Unit shall be dedicated to Applicant's Mallon 34 Fed Well No. 16 (API No. 30-025-32818 "the proposed well"), an existing vertical well to be drilled horizontally within the Bone Spring formation from a location 1980 feet from the South line and 660 feet from the West line (Unit L) of Section 34 and terminating within the Bone Spring formation at a bottomhole location 1980 feet from the South Line and 330 feet from the East line (Unit I) of Section 34, Township 19 South, Range 34 East, NMPM, Lea County, New Mexico.

(5) The operator of the Unit shall commence drilling the proposed horizontal well on or before January 31, 2011, and shall thereafter continue drilling the well with due diligence in a horizontal direction to test the Bone Spring formation.

(6) In the event the operator does not commence drilling the proposed well on or before January 31, 2011, Ordering Paragraph (1) shall be of no effect, unless the operator obtains a time extension from the Division Director for good cause demonstrated by satisfactory evidence.

(7) Should the proposed well not be drilled and completed within 180 days after commencement thereof, then Ordering Paragraphs (1), (2), and (4) shall be of no further effect, and the unit and project area created by this order shall terminate, unless operator appears before the Division Director and obtains an extension of the time for completion of the proposed well for good cause shown by satisfactory evidence.

(8) Upon final plugging and abandonment of the proposed well and any other well drilled on the Unit pursuant to Division Rule Part 13, Sections 9 through 11, the pooled Unit created by this Order shall terminate, unless this order has been amended to authorize further operations.

(9) Cimarex Energy Co. of Colorado (OGRID 162683) is hereby designated the operator of the well and of the Unit.

(10) After pooling, uncommitted working interest owners are referred to as pooled working interest owners. ("Pooled working interest owners" are owners of working interests in the Unit, including unleased mineral interests, who are not parties to an operating agreement governing the Unit.) After the effective date of this order, the operator shall furnish the Division and each known pooled working interest owner in the Unit an itemized schedule of estimated costs of drilling, completing and equipping the proposed well ("well costs").

(11) Within 30 days from the date the schedule of estimated well costs is furnished, any pooled working interest owner shall have the right to pay its share of estimated well costs to the operator in lieu of paying its share of reasonable well costs out of production as hereinafter provided, and any such owner who pays its share of estimated well costs as provided above shall remain liable for operating costs but shall not be liable for risk charges. Pooled working interest owners who elect not to pay their share of estimated well costs as provided in this paragraph shall thereafter be referred to as "non-consenting working interest owners."

(12) The operator shall furnish the Division and each known pooled working interest owner (including non-consenting working interest owners) an itemized schedule of actual well costs within 90 days following completion of the proposed well. If no objection to the actual well costs is received by the Division, and the Division has not objected, within 45 days following receipt of the schedule, the actual well costs shall be deemed to be the reasonable well costs. If there is an objection to actual well costs within the 45-day period, the Division will determine reasonable well costs after public notice and hearing.

(13) Within 60 days following determination of reasonable well costs, any pooled working interest owner who has paid its share of estimated costs in advance as provided above shall pay to the operator its share of the amount that reasonable well costs exceed estimated well costs and shall receive from the operator the amount, if any, that the estimated well costs it has paid exceed its share of reasonable well costs.

(14) The operator is hereby authorized to withhold the following costs and charges from production:

- (a) the proportionate share of reasonable well costs attributable to each non-consenting working interest owner; and
- (b) as a charge for the risk involved in drilling the well, 200% of the above costs.

(15) The operator shall distribute the costs and charges withheld from production, proportionately, to the parties who advanced the well costs.

(16) Reasonable charges for supervision (combined fixed rates) are hereby fixed at \$7,000 per month while drilling and \$700 per month while producing, provided that these rates shall be adjusted annually pursuant to Section III.1.A.3. of the COPAS form titled "*Accounting Procedure-Joint Operations*." The operator is authorized to withhold from production the proportionate share of both the supervision charges and the actual expenditures required for operating the well, not in excess of what are reasonable, attributable to pooled working interest owners.

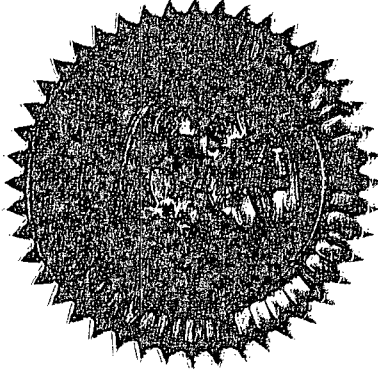
(17) Any unleased mineral interest shall be considered a seven-eighths (7/8) working interest and a one-eighth (1/8) royalty interest for the purpose of allocating costs and charges under this order. Any well costs or charges that are to be paid out of production shall be withheld only from the working interests' share of production, and no costs or charges shall be withheld from production attributable to royalty interests.

(18) Should all the parties to this compulsory pooling order reach voluntary agreement subsequent to entry of this order, this order shall thereafter be of no further effect.

(19) The operator of the well and Unit shall notify the Division in writing of the subsequent voluntary agreement of all parties subject to the forced pooling provisions of this order.

(20) Jurisdiction of this case is retained for the entry of such further orders as the Division may deem necessary.

DONE at Santa Fe, New Mexico, on the day and year hereinabove designated.



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STATE OF NEW MEXICO
OIL CONSERVATION DIVISION

A handwritten signature in cursive script, appearing to read "Mark E. Fesmire".

MARK E. FESMIRE, P.E.
Director