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 PURPOSES OF CONSIDERING:

CASE NOS. 14480 & 14418

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

CLOSING STATEMENT OF LYNX PETROLEUM CONSULTANTS, INC.

Lynx Petroleum Consultants, Inc. ("Lynx") submits its written closing statement in Case Nos. 14480 and 14418, and states as follows:

Compulsory pooling is limited by statute only to single spacing units. Section 70-2-17 of the Oil and Gas Act provides:

> When two or more separately owned tracts of land are embraced **within a spacing or proration unit**, ... the owner or owners thereof may validly pool their interests and develop their lands as a unit. Where, however, such owner or owners have not agreed to pool their interests, and where one such separate owner, or owners, who has the right to drill has drilled or proposes to drill a well on said unit to a common source of supply, the division, to avoid the drilling of unnecessary wells or to protect correlative rights, or to prevent waste, shall pool all or any part of such lands or interests or both in the spacing or proration unit as a unit."

However, Cimarex is seeking to pool for a project area which by its definition is not a single spacing unit. A "project area" is defined as "an area the operator designates on form C-102 that a spacing unit's outer boundaries enclose, a combination of complete, contiguous spacing units or an approved secondary, tertiary or pressure maintenance project. NMAC

19.15.16.17(I). A "spacing unit" is defined as "the acreage assigned to a well under a well spacing order or rule." NMAC 19.15.2.7(S)(9).

The Division has required an operator who seeks to pool for a project area to also apply for and obtain a non-standard spacing unit, as Cimarex did in this case. See e.g. Case 14057, Order No. 12868-C (Finding 13). A project area, as in this case, is defined as "a combination of complete, contiguous spacing units" and therefore is not a non-standard spacing unit.[1] Rather, since it is combining complete spacing units, the application is more in the nature of unitization.

In fact, when compulsory pooling is combined with the creation of a non-standard spacing unit in one application, the result is statutory unitization. See N.M.S.A .1978, § 70-7-1 et seq. Pursuant to the Statutory Unitization Act, an applicant may unitize lands in order to increase the ultimate recovery from those lands. An applicant must show that the plan of unitization is "fair, reasonable and equitable." *Id.* at § 70-7-5(D). The Division must then find that the participation formula is fair and reasonable. *Id.* at § 70-7-6(A)(6). If the Division determines that the formula "does not allocate unitized hydrocarbons in a fair, reasonable and equitable basis" the Division may make its own determination about the relative value of each tract and how production should be allocated. *Id.* at § 70-7-6(B). Thus, the parties have the opportunity to negotiate on how production from the unit is allocated and the Division has the opportunity to review the participation formula.

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[1] The case of *Rutter & Wilbanks Corp. v. OCC*, 87 N.M. 286, 532 P. 2d 582 (1975) is distinguishable from this case. In that case, R&W argued that the Commission did not properly create a "non-standard spacing and proration unit" and that it had no authority to create a non-standard spacing unit larger than 320-acre unit. In this case, Cimarex seeks to create a non-standard spacing unit by combining complete, contiguous spacing units for a horizontal well's project area. This was undoubtedly not a problem the Court or the Commission considered in 1975 when the horizontal drilling technology had not advanced to where it is today. Even if the Commission relies on this case as supportive, the R&W court recognized that the Commission's powers and duties must first rest on the prevention of waste and the protection of correlative rights.

However, statutory unitization is not authorized for primary production. See e.g. N.M.S.A. 1978, § 70-7-6. Accordingly, there is no requirement that the applicant negotiate how production should be allocated or that the Division review the allocation formula and determine whether it is reasonable.

In Oil Conservation Division Case No. 14057, Black Hills Gas Resources, Inc. applied for a non-standard proration unit for its project area where there were existing vertical wells. The Division recognized in Order No. R-12868-C that "[t]here is no statute or case law in New Mexico that prescribes the allocation of ownership of production from a horizontal well that penetrates multiple spacing units..." Finding 12. Thus, the Division required operators to file with form C-102 a statement certifying that all owners of all interests in the constituent spacing units "have agreed upon a formula for allocating production from the horizontal well." *Id.* Moreover, the Division also found that when an operator applies to compulsory pool a project area, the operator must "demonstrate, by appropriate technical evidence, that the formation of such a unit will prevent waste and will not impair correlative rights." Order No. R-12868-C, Finding 13. In these cases, Cimarex has failed to demonstrate that it will not impair correlative rights.

The Commission is required to determine whether the pooling application will prevent waste and protect correlative rights. N.M.S.A. 1978, § 70-2-17. Similarly, the Commission is also required to find in its orders that each owner of property in a pool has "the opportunity to produce his just and equitable share of the oil or gas, or both, in the pool, being an amount, so far as can be practically determined, and so far as such can be practically obtained without waste, substantially in the proportion that the quantity of the recoverable oil or gas, or both, under such property bears to the total recoverable oil or gas, or both, in the pool..." *Id.* at 70-2-17(A).

Furthermore, all pooling orders "shall be upon such terms and conditions as are just and reasonable and will afford to the owner or owners of each tract or interest in the unit the opportunity to recover or receive without unnecessary expense[2] his just and fair share of the oil or gas, or both." *Id.* at § 70-2-17(C).

Lynx provided testimony and exhibits that show there are significant differences in the reservoir quality between the N/2 and S/2 of Section 21. See e.g. Lynx Exhibit No. 1, 2, 9 & 10. The neutron/density log from the drilling of the pilot hole for the Penny Pincher Well No. 1 shows that there is, at most, only 8 feet of productive sand present. Lynx Exhibit No. 2. In Case No. 14418, Cimarex testified and provided maps that showed they expected to encounter 75 feet of pay from each quarter-quarter section in the project area. Even Cimarex's geologist and engineer now find that there is approximately 30 feet of pay for a change of approximately 45 feet of pay. Neither technical witness could demonstrate that each quarter-quarter section would equally contribute to the project area. Cimarex's engineer admitted that there would be approximately twice as much net pay coming from the S/2 than from the N/2 of Section 21. The evidence now indicates that there are disparate interests in the proposed project area such that allocating on a straight acreage basis would be a violation of correlative rights by not allowing Lynx to receive its just and fair share of production.

In sum, when a project area is comprised of "a combination of complete contiguous spacing units," compulsory pooling is not authorized because the combination of these spacing units is not the creation of a non-standard unit – it is unitization. If this application is granted, Lynx's correlative rights will be violated because it will be deprived of its right to its just and fair

[2] Lynx proposed at the hearing that Cimarex could log one of its proposed wells and interpolate the net pay. This would not add any cost and would more fairly reflect pay thickness and quality. Cimarex then should be required to negotiate with Lynx for a more equitable allocation method. Lynx proposes that Cimarex's application be denied so that they will be required to negotiate a fair and reasonable agreement with Lynx and the other interest owners Cimarex seeks to pool.

share of production underneath those tracts in which it has an interest. If Cimarex wishes to continue with its plans in Section 21 it can negotiate terms with the parties that are fair and reasonable. Therefore, these applications must be denied.

If the Commission determines that it will grant these applications, Lynx respectfully requests that Cimarex be required to furnish the pooled parties with an updated itemized schedule of well costs and that those parties then have 30 days to pay their share of costs.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I certify that on November 19, 2010 I served a copy of the foregoing document to the following by

- ☒ U.S. Mail, postage prepaid
- ☐ Hand Delivery
- ☐ Fax
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