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February 27, 1997

Hand Delivered

Michael E. Stogner
New Mexico Oil Conservation Division
2040 South Pacheco Street
Santa Fe, New Mexico 87505

Dear Mr. Stogner:

Enclosed are a copy of a proposed order in Case No. 11,697 (Application of Mallon Oil Company for a downhole commingling reference case), together with a disk (Wordperfect 5.1) with the order on it.

Very truly yours,



James Bruce

| Attorney for Mallon
| Oil Company

cc: Ray Jones w/encl.

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

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

CASE NO. 11697
ORDER NO. R-_____

APPLICATION OF MALLON OIL
COMPANY FOR THE ESTABLISHMENT
OF A DOWNHOLE COMMINGLING
REFERENCE CASE PURSUANT TO
DIVISION RULE 303.E AND THE
ADOPTION OF SPECIAL ADMINISTRATIVE
RULES THEREFOR, SAN JUAN COUNTY,
NEW MEXICO.

ORDER OF THE DIVISION

BY THE DIVISION:

This cause came on for hearing at 8:15 a.m. on January 9, 1997, at Santa Fe, New Mexico, before Examiner Michael E. Stogner.

NOW, on this _____ day of March, 1997, the Division Director, having considered the testimony, the record, and the recommendations of the Examiner, and being fully advised in the premises,

FINDS THAT:

(1) Due public notice having been given as required by law, the Division has jurisdiction of this cause and the subject matter thereof.

(2) The applicant, Mallon Oil Company, pursuant to the provisions of Division Rule 303.E., seeks to establish a downhole commingling "reference case" to provide exceptions for (a) marginal economic criteria, (b) pressure criteria, (c) allocation formulas, and (d) modification of notification rules on a lease-wide basis

for downhole commingling of Fruitland Coal, Pictured Cliffs, Mesaverde, Gallup, and Dakota production in existing or future wells drilled within Jicarilla Apache Tribal Lease Contract Nos. 434 and 435.

(3) Division Rule 303.E., amended by Order No. R-10470-A, currently states:

"If sufficient data exists on a lease, pool, formation, geographic area, etc., so as to render it unnecessary to repeatedly provide such data on Form C-107-A, an operator may except any of the various criteria required under Paragraph 303.D. of this rule by establishing a "reference case." The Division, upon its own motion, or by application from an operator, may establish "reference cases" either administratively or by hearing. Upon Division approval of such "reference cases" for specific criteria, subsequent applications to downhole commingle (Form C-107-A) will be required only to cite the Division order number which established such exceptions and shall not be required to submit data for those criteria."

(4) The applicant is the current operator of Jicarilla Apache Tribal Contract No. 434, which covers all of Sections 4, 5, and 6, and Jicarilla Apache Tribal Contract No. 435, which covers all of Sections 7, 8, 9, and 10, all within Township 22 North, Range 4 West, N.M.P.M., Sandoval County, New Mexico (collectively, the "Leases").

(5) According to its evidence and testimony, applicant seeks to:

- (a) Establish a "reference case" for marginal economic criteria in the Fruitland Coal through the Dakota formations whereby these formations and/or pools may be identified as "marginal" on Form C-107-A's subsequently filed for wells within the described Leases. The applicant further proposes that the data provided in the immediate case serve as supplemental data or confirmation that these

formations and/or pools should be classified as "marginal;"

- (b) Establish a "reference case" for pressure criteria in the Fruitland Coal through the Dakota formations whereby the Division may utilize data provided in the immediate case to verify the pressure data provided on Form C-107-A's subsequently filed for wells within the Leases;
- (c) Establish a "reference case" whereby the Division utilizes the data presented in the immediate case to endorse or approve certain methods of allocating production whereby the applicant need not submit additional data or justification when proposing a certain method of allocating production on Form C-107-A's subsequently filed for wells within the Leases; and
- (d) Establish a "reference case" or an administrative procedure for authorizing the downhole commingling of existing or future drilled wells within the Leases without additional notice to each affected interest owner as required by Division Rule No. 303.D.

(6) In support of its request to except marginal economic criteria, the applicant presented geologic and engineering evidence and testimony which indicates that:

- (a) The Leases are in the southeast San Juan Basin, on the edge of established production;
- (b) Each of the Leases is now held by production from one well upon each Lease, and the Bureau of Indian Affairs has made no demand for further development due to the marginal economics of development on the Leases;
- (c) The Fruitland Coal through the Dakota formations are consistently mappable across the Leases, although not every formation is productive lease-wide;
- (d) Data from wells in Townships 22 and 23 North, Ranges 4 and 5 West, shows that the primary zones of interest are the Pictured Cliffs and Gallup formations. No wells have been drilled in this

area during the 1990s;

- (e) The estimated ultimate recoveries from the better Pictured Cliffs wells in the area range from 170 to 284 MMCF of gas. The estimated ultimate recoveries from the better Gallup/Dakota dual completions in the area range from 51 to 82 MBO and 48 to 151 MMCF of gas;
- (f) The estimated ultimate recoveries from the Pictured Cliffs and Gallup formations are insufficient to justify drilling stand-alone wells and/or dually completed wells to recover such reserves; and
- (g) The applicant will not drill any additional wells within the Leases unless it can downhole commingle production.

(7) The evidence and testimony presented by the applicant indicates that the Fruitland Coal through the Dakota formations within the Leases should properly be classified as "marginal."

(8) In support of its request to except pressure criteria within the Fruitland Coal through the Dakota formations within the Leases, the applicant presented engineering evidence and testimony which indicates that:

- (a) The pressure gradient in the Fruitland through the Dakota formations is normal; and
- (b) Crossflow is not anticipated.

(9) There is sufficient pressure data available within the area so as to except pressure criteria as proposed by the applicant.

(10) The applicant proposed that the following allocation methods be utilized for downhole commingled wells within the Leases, depending on the circumstances, as follows:

- (a) Gas production will be allocated to each formation

based on the amount of the perforated interval in each formation; and

- (b) Oil production will be allocated only to the Gallup and Dakota formations, and the allocation will be based on the amount of the perforated interval in each formation.

(11) The allocation methods proposed by the applicant are reasonable based on the small amount of production in the area of the Leases, and therefore the proposal to except allocation formulas should be approved.

(12) In support of its request to establish a "reference case" or administrative procedure for eliminating notice requirements within the Leases, the applicant presented evidence and testimony which indicates that:

- (a) Interest ownership in Jicarilla Apache Tribal Contract No. 434 is common as to all zones, and interest ownership in Jicarilla Apache Tribal Contract No. 435 is common as to all zones;
- (b) Pursuant to Division Rule 303.D., applicant is currently required to notify all interest owners within the Leases every time a Form C-107-A is submitted to the Division;
- (c) Providing notice to each interest owner within the Leases of subsequent downhole commingling is unnecessary and is a burden on the applicant;
- (d) The downhole commingling of wells within the Leases will benefit working, royalty, and overriding royalty interest owners. In addition, the downhole commingling of wells within the Leases should not violate the correlative rights of any interest owner; and
- (e) Notice was given of the application herein to all interest owners in the Leases, and no interest owner appeared at the hearing in opposition to the establishment of a "reference case" or eliminating the notice requirement.

(13) An administrative procedure should be established for obtaining approval for downhole commingled wells on the Leases without notice to interest owners in the Leases; provided, however, that all other provisions contained within the Division Rule 303.C. are complied with.

(14) Approval of the proposed "reference case" for marginal economic criteria, pressure criteria, allocation formulas, and notice will lessen the burden on the applicant insofar as providing the data required pursuant to Division Rule 303.D. and Form C-107-A, will provide the applicant a streamlined method for obtaining downhole commingling approvals within the Leases, and will not violate correlative rights.

IT IS THEREFORE ORDERED THAT:

(1) The application of Mallon Oil Company to establish a "reference case" for (a) marginal economic criteria, (b) pressure criteria, (c) allocation formulas, and (d) modification of notification rules on a lease-wide basis for downhole commingling of Fruitland Coal, Pictured Cliffs, Mesaverde, Gallup, and Dakota production within existing or future drilled wells within Jicarilla Apache Tribal Contract Nos. 434 and 435, Sandoval County, New Mexico, is hereby approved.

(2) Upon filing of Division Form C-107-A's for wells subsequently downhole commingled within the Leases, the applicant shall not be required to submit supporting data to justify the classification of the Fruitland Coal through the Dakota formations

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as "marginal," supporting data to verify the pressure information provided on Fruitland Coal through the Dakota formations, and support or justification for utilizing a given method or formula for allocation of production; provided, however, that in the event any of the data described above appearing on Form C-107-A appears to be beyond the data range provided in this case, the Division may require the submittal of additional supporting data.

(3) In order to obtain Division authorization to downhole commingle wells within the Leases, the applicant shall file a Form C-107-A with the Santa Fe and Aztec Offices of the Division. Such application shall contain all the information required under Rule 303.C. of the Division Rules and Regulations; provided, however, that the applicant shall not be required to provide notice to all interest owners within the Leases of such proposed commingling.

(4) Jurisdiction of this cause 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.

STATE OF NEW MEXICO
OIL CONSERVATION DIVISION

WILLIAM J. LEMAY
Director