

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. 11722

**APPLICATION OF NEARBURG EXPLORATION
COMPANY, L.L.C. FOR COMPULSORY POOLING,
LEA COUNTY, NEW MEXICO**

ORDER NO. R-_____

**NEARBURG EXPLORATION COMPANY'S
PROPOSED
ORDER OF THE DIVISION**

BY THE DIVISION:

This cause came on for hearing at 8:15 a.m. on March 20, 1997 at Santa Fe, New Mexico, before Examiner David R. Catanach.

NOW, on this _____ day of March, 1997, the Division Director, having considered the testimony, the recorded 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, Nearburg Exploration Company, L.L.C. ("Nearburg"), filed its application seeking an order pooling all mineral interests from the surface to the base of the Morrow formation underlying the E/2 of Section 28, Township 20 South, Range 33 East, NMPM, Lea County, New Mexico, forming a standard 320-acre gas spacing and proration unit for any and all formations and/or pools developed on 320 acre spacing within said vertical extent, which presently includes but is not

necessarily limited to the South Salt Lake-Morrow Gas Pool and the Halfway-Atoka Gas Pool. Said unit is to be dedicated to its proposed Opal "28" Federal Com Well No. 1 (previously identified incorrectly as the Tomahawk "28" Federal Com, Well No. 1) to be drilled at a standard gas well location within Unit G of said spacing unit.

(3) As of January 8, 1997, the gross working interest ownership in the E/2 of said Section 28 was as follows:

Nearburg	12.50 %
Penwell Energy/ CoEnergy Central Exploration	65.625 %
Murphy Petroleum Corporation	11.5234375 %
Mitchell Energy Corporation	6.25 %
Santa Fe Energy Resources	3.125 %
Arrowhead Oil Corporation	0.78125 %
Branko, Inc.	0.1953125 %

(4) The Murphy Petroleum Corporation interest is derived from its operating rights ownership of Federal Oil & Gas Lease NM-82927 covering the SW/4SE/4 (40-acres) which is burdened by sixteen overriding royalties totalling 34.6875 % as follows:

Steve Mitchell	0.50 % ORR
George L. Scott, III	0.50 % ORR
Scott Exploration, Inc.	3.74 % ORR
Duane Brown	1.80 % ORR
S. H. Cavin	0.72 % ORR
Terry & Barb Kramer	10.80 % ORR
Landwest, a Utah General Partnership	0.36 % ORR
Candace McClelland	0.765 % ORR
Permian Hunter Corp.	1.44 % ORR
Robert Eaton	5.625 % ORR
Charles I. Wellborn	0.72 % ORR
Warren, Inc.	1.8 % ORR
Winn Investments, Inc.	0.36 % ORR
Lori Scott Worrall	0.36 % ORR

Xion Investments	3.6%	ORR
Strata Production Company	6.6%	ORR

(5) The applicant has the right to drill and proposed this well to all interest owners in this spacing unit.

(6) At the time of the hearing, Nearburg had obtained the voluntary agreement of Penwell Energy, Inc./CoEnergy Central Exploration Inc. and Arrowhead Oil Corporation with the balance of the interest owners in the proposed spacing unit having not executed written agreements to pool their interest.

(7) At the time of the hearing, Penwell Energy was the only working interest owner to enter its appearance in this case and none of the overriding royalty interest owners had filed an appearance.

(8) Nearburg provided evidence at hearing which demonstrated that:

(a) the costs of the well will be paid based upon the net working interest percentage ("net revenue interest") of the working interest owners in this spacing unit;

(b) Nearburg's policy and the general industry practice is to avoid drilling wells in which any net revenue interest is less than 75% because it adversely affects the economics of drilling a well;

(c) Murphy Petroleum Corporation's net revenue interest in the SW/4SE/4 is 52.8125% because it is burdened with a 12.5% federal royalty and 34.6875% overriding royalty burdens.

(d) Except for the SW/4SE/4 of Section 28, all other net revenue interests in this spacing unit are equal to or greater than 75%.

(e) if the total overriding royalty burden in the SW/4SE/4 of Section 28 are not reduced, Nearburg estimates that this will result in a 1.89 % return on investment and a 20.02 % rate of return.

(f) if these total overriding royalty burdens are reduced to 12.5 % it will increase Murphy Petroleum Corporation net revenue interest to 75 % which will result in a 2.11 % return on investment and a 24.97 % rate of return.

(g) in this case the 34.6875 % ORR is excessive and should be reduced.

(h) the total 34.6875 % overriding royalty burden on the SW/4SE/4 should be reduced to a total of 12.5 % in order provide the necessary economics to support drilling this well.

(9) Nearburg testified that Mark Murphy of Murphy Petroleum Corporation had concurred that the ORR burdens on its lease were excessive and had entered into an agreement to reduce those interest.

(10) Said overriding royalty burdens placed on the Murphy Petroleum Corporation's acreage is in excess of reasonable overriding royalties based on current economic and marketing conditions as detailed in Nearburg Exhibit 16.

(11) Without reducing those ORR burdens then the other working interest owners bear an unreasonable and therefore unnecessary cost burden as to that portion of the spacing unit bearing said overriding royalty.

(12) In order to protect correlative rights, prevent waste and to avoid compulsory pooling under terms that are not just or reasonable, any compulsory pooling order issuing in this case should provide for proportionate reduction of each of the sixteen overriding royalty burdens set forth in Finding (4) above for the SW/4SE/4 of said Section 28 to not more than 12.5 %.

(13) The Division finds that Nearburg's proposal is fair and reasonable and should be adopted by the Division in order to provide an equitable solution for the exploration of this spacing unit.

(14) To avoid the drilling of unnecessary wells, to protect correlative rights, to avoid waste, and to afford to the owner of each interest in said unit the opportunity to recover or receive with out unnecessary expense his just and fair share of the production in any pool completion resulting from this order, the application of Nearburg should be approved by pooling all mineral interests, whatever they may be, within said unit.

(15) At the request of the applicant, Nearburg Producing Company, or an agreed upon successor operator, should be designated the operator of the subject well and unit.

(16) Any non-consenting working interest owner should be afforded the opportunity to pay his share of estimated well costs to Nearburg Producing Company, as the operator, in lieu of paying his share of reasonable well costs out of production.

(17) Any non-consenting working interest owner who does not pay his share of estimated well costs should have withheld from production his share of the reasonable well costs plus an additional 200 percent thereof as a reasonable charge for the risk involved in the drilling of the well.

(18) Any non-consenting working interest owner should be afforded the opportunity to object to the actual well costs but actual well costs should be adopted as the reasonable well costs in the absence of such objection.

(19) Following determination of reasonable well costs, any consenting working interest owner who has paid his share of estimated costs should pay to the operator any amount that reasonable well costs exceed estimated well costs and should receive from the operator any amount that paid estimated well costs exceed reasonable well costs.

(20) \$6000.00 per monthly while drilling and \$600.00 per month while producing should be fixed as reasonable charges for supervision (combined fixed rates); the operator should be authorized to withhold from production the proportionate share of such supervision charges attributable to each non-consenting working interest, and in addition thereto, the operator should be authorized to withhold from production the proportionate share of actual expenditures required for operation the subject well, not in excess of what are reasonable, attributable to each non-consenting working interest.

(21) All proceeds from production from the subject well which are not disbursed for any reason should be placed in escrow to be paid to the true owner thereof upon demand and proof of ownership.

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

(23) The operator(s) of the well and unit shall notify the Director of the Division in writing of the subsequent voluntary agreement of all parties subject to the forced pooling provisions of the order.

IT IS THEREFORE ORDERED THAT:

(1) The application of Nearburg Exploration Company, L.L.C. ("Nearburg") for an order pooling all mineral interests from the surface to the base of the Morrow formation underlying the E/2 of Section 28, Township 20 South, Range 33 East, NMPM, Lea County, New Mexico, forming a standard 320-acre gas spacing and proration unit for any and all formations and/or pools developed on 320 acre spacing within said vertical extent, which presently includes but is not necessarily limited to the South Salt Lake-Morrow Gas Pool and the Halfway-Atoka Gas Pool is **hereby approved.**

(2) Said unit is to be dedicated to its proposed Opal "28" Federal Com Well No. 1 (previously identified incorrectly as the Tomahawk "28" Federal Com, Well No. 1) to be drilled at a standard gas well location within Unit G of said spacing unit.

(3) The sixteen overriding royalty interests totalling 34.6875 % which burden the Murphy Petroleum Corporation's net revenue interest in the SW/4SE/4 as identified in Finding (4) above, are hereby proportionately reduced to 12.5 %.

(4) Nearburg Producing Company, or an agreed upon successor operator, is hereby designated the operator of the subject well and unit.

(5) The operator of said unit shall commence the drilling of said well on or before the 1st day of July, 1997, and shall thereafter continue the drilling of said well with due diligence to a depth sufficient to test the Morrow formation.

PROVIDED FURTHER THAT, in the event the operator as the said operator does not commence the drilling of said well on or before the 1st day of July, 1997, Ordering Paragraph No. (1) of this order shall be null and void and of no effect whatsoever, unless said operator obtains a time extension from the Division Director for good cause shown.

PROVIDED FURTHER THAT, should said well not be drilled to completion, or abandonment, within 120 days after commencement thereof, said operator shall appear before the Division Director and show cause why Ordering Paragraph No (1) of this order should not be rescinded.

(6) After the effective date of this order and within 90 days prior to commencing said well, Nearburg shall furnish the Division and to each of the known working interest owners of record as of **January 27, 1997 which is the date the application was filed**, an itemized schedule of estimated well costs **unless** said working interest has been acquired by the operator or otherwise has been voluntarily committed to participation under terms acceptable to the operator.

(7) Within thirty (30) days from the date the schedule of estimated well costs is furnished to him, any working interest owner shall have the right to pay his share of estimated well costs to Nearburg in lieu of paying his share of reasonable well costs out of production, and any such owner who pays his share of estimated well costs as provided above shall remain liable for operation costs but shall not be liable for risk charges.

(8) The operator shall furnish the Division and each known working interest owner an itemized schedule of actual well costs within 90 days following completion of the 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 said schedule, the actual well costs shall be the reasonable well costs; provided however, if there is objection to actual well costs within said 45-day period the Division will determine reasonable well costs after public notice and hearing.

(9) Within 60 days following determination of reasonable well costs, any non-consenting working interest owner who has paid his share of estimated well costs in advance as provided above shall pay to the operator his pro rata share of the amount that reasonable well costs exceed estimated well costs and shall receive from the operator his pro rata share of the amount that estimated well costs exceed reasonable well costs.

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

(A) The pro rata share of reasonable well costs attributable to each non-consenting working interest owner who has not paid his share of estimated well costs within thirty (30) days from the date the schedule of estimated well costs is furnished.

(B) As a charge for the risk involved in the drilling of the well, 200 percent of the pro rata share of reasonable well costs attributable to each non-consenting working interest owner who has not paid his share of estimated well costs is furnished to him.

(11) The operator shall distribute said costs and charges withheld from production to the parties who advanced the well costs.

(12) \$6000.00 per month while drilling and \$600.00 per month while producing are hereby fixed as reasonable charges for supervision (combined fixed rates); the operator is hereby authorized to withhold from production the proportionate share of such supervision charges attributable to each non-consenting working interest, and in addition thereto, the operator is hereby authorized to withhold from production the proportionate share of actual expenditures required for operation such well, not in excess of what are reasonable, attributable to each non-consenting working interest.

(13) 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 the terms of this order.

(14) Any well costs or charges which are to be paid out of production shall be withheld only from the working interest's share of production, and no costs or charges shall be withheld from production attributable to royalty interests.

(15) All proceeds from production from the subject well which are not disbursed for any reason shall immediately be placed in escrow in Lea County, New Mexico, to be paid to the true owner thereof upon demand and proof of ownership, the operator shall notify the Division of the name and address of said escrow agent within 30 days from the date of first deposit with said escrow agent.

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

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

(18) Jurisdiction is hereby retained for the entry of such further orders as the Division may deem necessary.

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

STATE OF NEW MEXICO
OIL CONSERVATION DIVISION

WILLIAM J. LEMAY, Director