



NEW MEXICO ENERGY, MINERALS
& NATURAL RESOURCES DEPARTMENT

OIL CONSERVATION DIVISION
2040 South Pacheco Street
Santa Fe, New Mexico 87505
(505) 827-7131

May 2, 1997

Thomas J. Hynes, Esq.
Hynes, Hale & Gurley
1000 West Apache
Farmington, NM 87401

RE: OCD Case No. 11768---Sirgo Brothers Energy Corporation application for compulsory pooling for re-entering the Moore Well No. 1 (Unit E, S/2 NW/4, Sec. 12, T29N, R15W, San Juan County, New Mexico)

Dear Mr. Hynes:

Due to the objection to the above-referenced application raised in your April 23, 1997 letter, we have continued this case until May 29, 1997, at which time the case will again be called unless Mr. Kennedy and Sirgo Brothers come to an agreement by then.

Please be advised of the following. The Oil Conservation Division (OCD) cannot (and as a matter of policy, would not) require Sirgo to reimburse Mr. Kennedy for the \$15,000 invested with a prior operator, S&I, for the drilling of this well. This was an investment made by Mr. Kennedy with S&I (whether voluntarily outside of a compulsory pooling order or under the "consent" provision of a pooling order) which proved to be unprofitable.

The well is worth nothing without a new operator coming in and bringing the well back onto production. In fact, the well is a liability since the well is required to be plugged if not brought back onto production. Normally, the Division would look only to the current operator (which has posted a plugging bond for the plugging the well) for the responsibility for plugging but Mr. Kennedy brings up an interesting question: If a party who paid for the drilling of a well can claim continuing ownership in that hole (even if the underlying leases have expired) so as to require that party's consent for any further use of that hole, is not that party also responsible for its share of the costs of plugging that well?

Mr. Kennedy is apparently concerned about being responsible for his share of well costs and is obviously desirous of recouping the \$15,000 he invested with S&I. Mr. Kennedy can avoid being responsible for any costs since he has been presented with the option of signing a lease whereunder he would be receive a royalty and not be responsible for any costs. Apparently, Mr. Kennedy also had that option with S&I too but unfortunately (in retrospect) chose to forego that option in favor of participating as a working interest owner (whether under the "consent" provisions of a pooling order or not).

The leases have apparently expired underlying the spacing unit for this well and Sirgo has

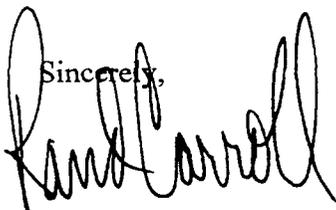
obtained new leases or obtained agreements to participate from all the mineral interests in this 80 acres from every owner except Mr. Kennedy. Therefore under Sec. 70-2-17.C. NMSA 1978, Sirgo as an owner with the right to drill has the right to force pool the uncommitted interests in this 80 acre spacing unit. The Division will force pool Mr. Kennedy's interest pursuant to Sirgo's application absent an objection more valid than not having recouped a \$15,000 investment in the original drilling of this well from the original operator of that well. The Division notes that the hole is not located on Mr. Kennedy's acreage.

We do take notice of the fact that Sirgo has not requested a risk penalty (up to 200% is allowed by statute) for the reimbursement of the costs of reworking this well. This means that Mr. Kennedy will not have to pay his share of the costs (estimated to be \$1,236.94) up front but could have his share of the costs deducted from his share of revenues, if any, without penalty. If the well never produces, Mr. Kennedy would still not be liable for the rework costs. Thus under a pooling order, Mr. Kennedy can only receive revenue and not be required to pay anything out-of-pocket.

The Division is charged with the duties of prevention of waste and protection of correlative rights. Obtaining production or additional production from non-producing wells is an important aspect of those duties. Forced pooling of mineral interests to facilitate the drilling or reworking of wells is one of the primary tools the Division utilizes to accomplish these goals. The reason forced pooling is often necessary is to prevent a mineral owner from preventing the drilling (or reworking) of a well by demanding an unreasonable amount of consideration for his consent.

The Division has continued this case to May 29, 1997 to allow the parties additional time to come to an agreement. We will at that time (unless the case is dismissed) call the case and, if no one appears and presents evidence or argument, take the case under advisement for the issuance of an order based upon the documentation already submitted, i.e., the application of Sirgo and the objection filed by Kennedy.

If you have any questions, please feel free to call me at 505/827-8156.

Sincerely,


Rand Carroll
Legal Counsel

cc: Michael E. Stogner, OCD Hearing Examiner
David R. Catanach, OCD Hearing Examiner
Frank Chavez, OCD Aztec District Supervisor
Ernie Busch, OCD Aztec
Brian M. Sirgo, Sirgo Brothers Energy Corp.