

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 SANTA FE SNYDER)	CASE NO. 12,393
CORPORATION FOR COMPULSORY POOLING,)	
LEA COUNTY, NEW MEXICO)	
)	
APPLICATION OF SOUTHWESTERN ENERGY)	CASE NO. 422
COMPANY FOR COMPULSORY POOLING,)	
LEA COUNTY, NEW MEXICO)	
)	(Consolidated)

OIL CONSERVATION DIVISION
RECORDS - 1
MAY 5: 26

REPORTER'S TRANSCRIPT OF PROCEEDINGS

EXAMINER HEARING

ORIGINAL

BEFORE: MICHAEL E. STOGNER, Hearing Examiner

May 18th, 2000

Santa Fe, New Mexico

This matter came on for hearing before the New Mexico Oil Conservation Division, MICHAEL E. STOGNER, Hearing Examiner, on Thursday, May 18th, 2000, at the New Mexico Energy, Minerals and Natural Resources Department, Porter Hall, 2040 South Pacheco, Santa Fe, New Mexico, Steven T. Brenner, Certified Court Reporter No. 7 for the State of New Mexico.

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* * *

1 WHEREUPON, the following proceedings were had at
2 10:31 a.m.:

3 EXAMINER STOGNER: At this time I will call Case
4 Number 12,393, which is the Application of Santa Fe Snyder
5 Corporation for compulsory pooling, Lea County, New Mexico.

6 I'll call for appearances.

7 MR. KELLAHIN: Mr. Examiner, I'm Tom Kellahin of
8 the Santa Fe law firm of Kellahin and Kellahin, appearing
9 on behalf Santa Fe Snyder Corporation. I have two
10 witnesses to be sworn.

11 EXAMINER STOGNER: Any other appearances?

12 MR. BRUCE: Mr. Examiner, Jim Bruce of Santa Fe,
13 representing Southwestern Energy Production Company. I
14 also have two witnesses to be sworn.

15 At this time I'm not sure of the case, but I
16 would also ask that this matter be consolidated with
17 Case -- I think it's 12,423, which is Application of
18 Southwestern Energy Production Company for compulsory
19 pooling, involving the west half of the section at issue in
20 the Santa Fe Application.

21 EXAMINER STOGNER: Any other appearances?

22 Okay, the case that you are referring to is
23 12,423. That case is indeed scheduled, docketed for June
24 the 1st; is that correct?

25 MR. BRUCE: That's correct.

1 EXAMINER STOGNER: Okay, Mr. Kellahin, is this
2 your understanding also?

3 MR. KELLAHIN: Mr. Examiner, we had a motion
4 hearing before Examiner Catanach several weeks ago. The
5 end result of that motion hearing was Mr. Catanach's
6 decision to continue the Santa Fe Snyder case from the
7 earlier docket to today's docket and to advance the
8 Southwestern case from the June 1st docket to today's
9 docket.

10 So Mr. Bruce and I are of the same understanding
11 that both these cases are to be heard by you today.

12 EXAMINER STOGNER: Since this is somewhat
13 unorthodox, I guess at this time I'll call Case Number --
14 in advance, which will not be on the docket until June 1st,
15 which is Case Number 12,423.

16 MS. HEBERT: Application of Southwestern Energy
17 Company for compulsory pooling, Lea County, New Mexico.

18 EXAMINER STOGNER: Are there any other
19 appearances, other than Santa Fe Snyder and Mr. Bruce in
20 this matter?

21 Okay, since we're prepared at this time to
22 consolidate these two cases, is there any need for opening
23 remarks at this time?

24 MR. KELLAHIN: Yes, Mr. Examiner, we believe so.

25 EXAMINER STOGNER: Do you want to begin?

1 MR. KELLAHIN: Yes, sir. Thank you.

2 Mr. Examiner, we're dealing with Section 17 of 23
3 South, 34 East. Section 17 is divided north half, south
4 half. The south half consists of a single federal lease.
5 The north half consists of another single federal lease.

6 In December of last year, Santa Fe Energy, now
7 Santa Fe Snyder Corporation, proposed the drilling of their
8 well at a standard location in the northwest quarter of the
9 section, to be dedicated to the north half.

10 Some three months later, Southwestern proposed a
11 location in the same general vicinity as the Santa Fe well,
12 but Southwestern proposed a west-half orientation.

13 At the motion hearing, the issue being debated by
14 the parties is the issue of the Bureau of Land Management's
15 primary jurisdiction over the orientation of spacing units
16 in a section entirely controlled by federal leases. And as
17 you know, the Bureau of Land Management rules and
18 regulations provide that in conformance with Oil
19 Conservation Division spacing rules, that the orientation
20 of a 320-acre spacing unit shall be done in a fashion to
21 include a single federal lease, subject to certain limited
22 exceptions.

23 And that limited exception is, when there is
24 significant geologic and engineering data to demonstrate
25 the justification on behalf of the Bureau of Land

1 Management to dictate a different orientation, which would
2 then require communitization of those leases.

3 At the time of the motion hearing, that topic was
4 before the Bureau of Land Management in Roswell and had not
5 been decided.

6 Since then, both Santa Fe and Southwestern have
7 submitted geologic arguments to the Bureau of Land
8 Management, and yesterday the Bureau of Land Management has
9 exercised its jurisdiction and has approved an application
10 for permit to drill for Santa Fe Snyder Corporation,
11 approving the north-half orientation.

12 So insofar as there was a potential issue for you
13 to decide as to orientation, that issue has been removed by
14 the primary jurisdiction of the Bureau of Land Management
15 where they have decided that they will approve and, in
16 fact, have approved, Santa Fe's application for permit to
17 drill, dictating a north-half orientation.

18 And so the issue before you now is the other
19 components of a compulsory pooling application, which in
20 our opinion are rather ordinary, standard and can be
21 accomplished rather quickly. The position we take is that
22 we have a valid well proposal, it's the first proposal
23 made. It was some three months before Southwestern ever
24 made their proposal.

25 Santa Fe Snyder has done all the necessary work

1 to get this well drilled, permitted, they've invited
2 Southwestern to participate in this well, and up to now
3 Southwestern has chosen not to do so.

4 I believe we're entitled to a compulsory pooling
5 order, and we will present evidence on the sequence and
6 efforts we have exhausted trying to get Southwestern to
7 participate.

8 In addition, we have a short presentation to
9 justify the substantial geologic risk involved, and we'll
10 ask that you award a 200-percent risk factor penalty in the
11 event the parties cannot come to terms, and we will have to
12 rely upon an act pursuant to compulsory pooling order.

13 EXAMINER STOGNER: Mr. Bruce?

14 MR. BRUCE: Mr. Examiner, I think there are --
15 well, two, maybe three issues to address.

16 As Mr. Kellahin said, there are two federal
17 leases involved, and Southwestern has filed data with the
18 BLM asking for a west-half unit. To the best of my
19 knowledge, they haven't heard back from the BLM yet. We'll
20 see what Santa Fe presents today. But we still believe
21 that geology justifies a west-half unit, and at this point
22 we have not heard back from the BLM.

23 There's also another sub-issue, whether to drill
24 to the Morrow or the Atoka. And in connection with that,
25 there are different proposed well locations for the Santa

1 Fe and Southwestern wells. We think the most important
2 consideration in judging upon pooling applications is the
3 geology, and we believe that the geology will support
4 Southwestern's Application.

5 Secondly, it's Southwestern's contention that
6 Santa Fe has never made a valid well proposal. This was
7 argued at the motion hearing which you attended. We will
8 put on evidence about that. But at the time Santa Fe made
9 its well proposal, it owned no interest in the well unit.
10 It never subsequently, after acquiring an interest in the
11 well unit, proposed a well. And we believe that its well
12 proposal is thus invalid, and the only valid proposal on
13 the table is Southwestern's.

14 With that, I would suggest we move on to the
15 evidence.

16 EXAMINER STOGNER: Just for the record here,
17 let's see, Santa Fe, in Case 12,393, is seeking, initially,
18 a laydown north-half dedication for 320.

19 MR. KELLAHIN: Yes, sir.

20 EXAMINER STOGNER: And this is a consolidation of
21 two leases?

22 MR. KELLAHIN: No, sir, it's a single federal
23 lease in the north half. If you stand it up as
24 Southwestern proposes for a west half, that requires
25 consolidation of two federal leases, and that was the issue

1 before the Bureau of Land Management.

2 EXAMINER STOGNER: And what further is Santa Fe
3 seeking?

4 EXAMINER STOGNER: Santa Fe is seeking a
5 compulsory pooling order of the north half, approval of our
6 Application for a compulsory pooling order that includes a
7 200-percent risk factor penalty, and the appropriate
8 overhead rates. We are seeking to drill a well to the base
9 of the Morrow, because we believe it's the primary
10 objective.

11 There should be no discussion or issue about
12 competing pooling cases, because it's really moot before
13 this agency. The BLM has exercised its jurisdiction, and
14 that's no longer a topic for you to worry about. The BLM
15 has already decided that issue.

16 EXAMINER STOGNER: Okay, I guess what I should
17 say, I want to make sure that -- What other force pooling
18 is Santa Fe seeking?

19 MR. KELLAHIN: Well, we'll be seeking to force
20 pool any of the 320 formations, and it will be from the top
21 of the Wolfcamp down to the base of the Morrow.

22 EXAMINER STOGNER: Okay, what else?

23 MR. KELLAHIN: In the event that there is any
24 shallow production, then the Application asks for pooling
25 further shallower zones. All that is pretty speculative,

1 Mr. Stogner. The primary objective is the Morrow. But
2 this is a typical pooling case where we're asking for the
3 various combinations.

4 EXAMINER STOGNER: Okay. And Mr. Bruce,
5 Southwestern Energy is seeking 320 in a standup?

6 MR. BRUCE: In a standup.

7 EXAMINER STOGNER: Is this where the
8 consolidation of the acreage is coming in?

9 MR. BRUCE: Yes, sir. Yes, sir.

10 EXAMINER STOGNER: Okay, and --

11 MR. BRUCE: And then it would also be seeking --
12 and once again, it is speculative -- pooling for the
13 northwest quarter for 160-acre zones, gas well zones, and
14 40 acres comprising the northwest of the northwest for any
15 oil well zones, although again I don't know that there are
16 any in this area.

17 EXAMINER STOGNER: Okay. Now, how about the
18 location of these wells? What's the difference there?

19 MR. BRUCE: Mr. Examiner, Southwestern's is 1310
20 feet from the north line and from the west line of the
21 section.

22 EXAMINER STOGNER: Okay, and Santa Fe?

23 MR. KELLAHIN: Santa Fe's location is 1980 from
24 the north, 660 from the west. It's our position you can't
25 decide this based upon a difference of well locations.

1 EXAMINER STOGNER: Mr. Bruce, is your Application
2 missing something?

3 MR. BRUCE: Mr. Examiner, you may be right. It
4 would be missing unorthodox location in the oil well zone.
5 And if that's the case, we would dismiss any portion of the
6 Application asking for a pooling of the 40-acre zones.

7 EXAMINER STOGNER: I'm not going to act on that
8 motion just yet, but a motion has been made and we'll hear
9 the testimony as it affects the upper zones.

10 Okay, we've had opening remarks at this time.
11 Unless otherwise an agreement between Mr. Bruce and Mr.
12 Kellahin, I am assuming that Santa Fe is going to start
13 today?

14 MR. KELLAHIN: Yes, sir, that's our preference.

15 Mr. Examiner, our first witness is Mr. Steve
16 Smith. Mr. Smith is a petroleum landman. He works for
17 Santa Fe Snyder Corporation, and he resides in Midland,
18 Texas.

19 (Thereupon, the witnesses were sworn.)

20 STEVEN J. SMITH,
21 the witness herein, after having been first duly sworn upon
22 his oath, was examined and testified as follows:

23 DIRECT EXAMINATION

24 BY MR. KELLAHIN:

25 Q. For the record, sir, would you please state your

1 name and occupation?

2 A. My name is Steven James Smith. I'm a senior
3 staff landman for Santa Fe Snyder Corporation.

4 Q. Mr. Smith, on prior occasions have you testified
5 before the Division in compulsory pooling applications?

6 A. Many times, yes.

7 Q. In fact, one of the times you testified was in
8 the Mitchell Energy Case that involved the compulsory
9 pooling of Strata Production and Mark Murphy and others?

10 A. That's correct.

11 Q. At that time you were working for Mitchell
12 Energy, were you not?

13 A. That's correct.

14 Q. Subsequently, you were employed by Santa Fe
15 Snyder Corporation, and you have testified on occasions for
16 that company in compulsory pooling matters, have you not?

17 A. Yes, I have.

18 Q. So you understand the process and the basic
19 components involved in this type of case?

20 A. Yes, I do.

21 Q. Have you made yourself knowledgeable about the
22 ownership in Section 17?

23 A. Yes, I have.

24 Q. And were you the responsible employee for your
25 company to engage in negotiations with various companies

1 and entities over participation in the Santa Fe Snyder
2 Corporation proposal?

3 A. Yes, I was.

4 Q. In addition, would you be the responsible party
5 that would receive any communications from Southwestern
6 concerning responses to Santa Fe's proposal or proposals on
7 behalf of that company?

8 A. My boss, Curtis Smith, might respond on my
9 behalf, but I would be the primary contact for responses.

10 MR. KELLAHIN: All right, sir. We tender Mr.
11 Smith as an expert petroleum landman.

12 EXAMINER STOGNER: Any objection?

13 MR. BRUCE: No.

14 EXAMINER STOGNER: I assume you're speaking of
15 this Mr. Smith today.

16 MR. KELLAHIN: Yes, sir.

17 EXAMINER STOGNER: Okay, Mr. Steven Smith, who is
18 here today in the witness stand --

19 MR. KELLAHIN: Yes, sir.

20 EXAMINER STOGNER: -- is accepted as an expert
21 witness.

22 THE WITNESS: Thank you.

23 Q. (By Mr. Kellahin) All right, sir, would you turn
24 to what is marked as Exhibit Number 1? Let's take a moment
25 and identify for the Examiner what we're seeing in this

1 plat.

2 A. What we have here is, again, a photocopy of a
3 Midland map that has been used to create a plat for Santa
4 Fe Snyder purposes. It is acreage in and around Township
5 23 South, 34 East. Santa Fe's acreage in the area is
6 highlighted in yellow.

7 The proposed location for our well in Section 17
8 is shown with a red square around it, and the anticipated
9 320-acre proration unit is shown with a green line around
10 it.

11 Q. All right. The yellow acreage indicates acreage
12 where Santa Fe Snyder has an interest; it doesn't all
13 interests within that acreage?

14 A. That's correct, it just is a gross
15 representation.

16 Q. Let's look at 17. How is Section 17 subdivided?

17 A. It is divided into two separate federal leases,
18 the north half being Federal Lease 97157, and in the south
19 half Federal Lease 065194.

20 Q. Who is the current lessee or working interest
21 owners for the south half?

22 A. Conoco is the record title owner, and Santa Fe
23 currently has a term assignment from Conoco covering 100
24 percent of that tract.

25 Q. What is the current status of the working

1 interest ownership in the north-half lease?

2 A. Attached to the plat is a summary of that
3 ownership. Again, Concho Resources, Inc., has 100 percent
4 of the record title. Santa Fe Snyder Corporation has half
5 of the operating rights, subject to its term assignment,
6 and Southwestern Energy Production Company has the other
7 half, again subject to the term assignment it has with
8 Concho.

9 EXAMINER STOGNER: And this represents an
10 undivided 50-50?

11 THE WITNESS: That's correct.

12 Q. (By Mr. Kellahin) Can you approximate for us,
13 Mr. Smith, when you first commenced trying to acquire
14 acreage and lease positions in this area for a potential
15 well to be drilled by your company?

16 A. Late 1998, December of 1998, is when I really
17 first in earnest began trying to assemble this prospect.

18 Q. How did Santa Fe come to acquire an interest in
19 the north half of Section 17?

20 A. Well, we do what we normally do when we identify
21 a piece of property, we have a broker run title to it for
22 us so we know who the owners are.

23 Based upon that ownership, we found of record
24 that Southwestern had a half interest in this via term
25 assignment and a half interest undivided in the operating

1 rights, and Concho had the other 50 percent of the
2 operating rights. And so we decided to attempt to acquire
3 the other half from Concho?

4 Q. And were you successful in acquiring the other 50
5 percent from Concho?

6 A. Yes, I was.

7 Q. And how did you accomplish that? What type of
8 form did that document take?

9 A. It is a term assignment, it is Exhibit 2 here.

10 Q. Well, let's take a moment and look at Exhibit 2.
11 Is Exhibit 2 an accurate copy of the term assignment that
12 Concho executed and conveyed to Santa Fe Snyder Corporation
13 for a 50-percent interest in the north half of Section 17?

14 A. Yes, it is.

15 Q. Was this document recorded?

16 A. Yes, it was.

17 Q. When you turn to the execution page, describe for
18 me what is supposed to be the effective date of this
19 agreement. When you turn to page 4, just above the
20 assignor's signature, it says "In witness whereof..."

21 A. The date first set above.

22 Q. So when we turn back to the date first set above,
23 what is that date?

24 A. December 1, 1999.

25 Q. All right. Mr. Bruce in his opening statement

1 made reference to the fact that he contends Santa Fe's well
2 proposal is invalid because at the time you made it, Mr.
3 Smith, Santa Fe Snyder had no interest?

4 A. That is his statement.

5 Q. Is that true?

6 A. No, it is not.

7 Q. When did you make your well proposal to
8 Southwestern?

9 A. It was made by letter December 9 of 1999, and
10 that proposal is Exhibit 3.

11 Q. All right. Let's stick with the term assignment.
12 The term assignment provides you the opportunity on behalf
13 of your company to do what?

14 A. Explore for, produce and sell oil and gas and any
15 other minerals covered by the term assignment.

16 Q. And that term assignment is into Santa Fe Snyder
17 Corporation?

18 A. That's correct.

19 Q. Under this document, then, you would have a
20 working interest ownership in this federal lease, would you
21 not?

22 A. We would have operating rights which would
23 entitle us to a working interest, yes.

24 Q. And pursuant to those operating rights, you have
25 made a well proposal of December 9th to Southwestern Energy

1 Production Company?

2 A. That's correct.

3 Q. When we look at the term assignment, is there
4 anything in this term assignment that discloses to you that
5 Concho had any kind of commitment or burden on your 50
6 percent that involves Southwestern?

7 A. In fact, no. In fact, the entireties clause of
8 the assignment clearly states that this constitutes the
9 entire agreement, and there are no other between the
10 parties.

11 Q. Did you make yourself aware that Concho had, by a
12 term assignment, assigned the first 50 percent to
13 Southwestern?

14 A. Yes, when we ran title, we became aware of that
15 term assignment.

16 Q. Is there anything in the term assignment between
17 Concho and Southwestern that limits, controls or otherwise
18 modifies the term assignment that you received?

19 A. None whatsoever. And in fact, it has the same
20 entirety clause that ours does, which clearly states that
21 there are no other agreements between Concho and
22 Southwestern.

23 Q. December 1st, Santa Fe Energy or Santa Fe Snyder
24 has got 50 percent interest, and then you propose a well to
25 Southwestern, correct?

1 A. That's correct.

2 Q. Let's turn to the proposal, Exhibit Number 3. Is
3 this your proposal?

4 A. It is.

5 Q. And do you have authority on behalf of your
6 company to make these proposals?

7 A. Yes, I do.

8 Q. Does this proposal include a recommendation as to
9 what the spacing unit is to be?

10 A. It does.

11 Q. Does it specify where the well is to be located?

12 A. It does.

13 Q. Did you provide a complete and accurate of well
14 costs for your well?

15 A. Yes, I did.

16 Q. The total well depth on the AFE was 13,700 feet;
17 is that not true?

18 A. That is correct.

19 Q. And it was intended to be a Morrow gas test?

20 A. That's correct.

21 Q. You sent this to Southwestern?

22 A. Yes, I did.

23 Q. What, if any, response did you receive from
24 Southwestern?

25 A. Well, by cc, by carbon copy, I got a letter that

1 Sam Thompson with Southwestern sent to Concho that
2 basically refuted our having an interest and basically told
3 us that our proposal was invalid.

4 Q. All right, let's look at that. It's Exhibit 4,
5 it's Mr. Thompson's December 14th letter, and you received
6 this letter by copy?

7 A. In fact, Southwestern faxed it to me, yes.

8 Q. All right. Mr. Thompson is contending that Santa
9 Fe has no interest in the north half, right?

10 A. Correct.

11 Q. Did you provide Mr. Thompson with information to
12 demonstrate to him that you, in fact, had a 50-percent
13 interest in the lease?

14 A. We advised him of our term assignment, and he
15 again at that point told us that our term assignment was
16 invalid because he believed there was a JOA in place that
17 we were subject to.

18 Q. All right, let's talk about the joint operating
19 agreement.

20 A. All right.

21 Q. He's referring to a joint operating agreement
22 between Concho and Southwestern?

23 A. That's correct.

24 Q. At the time you acquired your interest from
25 Concho, was that operating agreement of record?

1 A. No, it was not.

2 Q. Did you have any knowledge, or your company have
3 any knowledge about this operating agreement?

4 A. No, we did not. And in fact, I point-blank
5 inquired of Concho, when we attempted to acquire this from
6 them, whether or not there was a JOA in place, and I was
7 told by Mike Gray at Concho that there was no JOA in place.
8 And we moved forward to acquire that term assignment based
9 upon the representation by Concho that there was, in fact,
10 no JOA in place.

11 Q. As a landman, are you of the opinion that you are
12 not subject, or your company is not subject, to this
13 operating agreement?

14 A. It is my opinion that we are a bona fide
15 purchaser for value. We did everything that would be
16 reasonably and prudently expected of anyone to do, to
17 determine whether or not there was a JOA in place. We ran
18 title, there was no evidence of title. We inquired of the
19 selling party as to the existence and were told there was
20 none.

21 Q. When we look at the joint operating agreement,
22 Mr. Thompson is referencing his position that your proposal
23 is invalid because Southwestern didn't waive the
24 maintenance of uniform interest provision; do you see that?

25 A. Yes.

1 Q. Describe for us your understanding of what that
2 provision means.

3 A. Well, that's a preprinted portion of a standard
4 model form operating agreement that is intended to keep the
5 ownership within a contract area whole so that the operator
6 is not obligated to keep up with increasingly diverse and
7 complicated ownership. That's basically the intent of that
8 clause.

9 Q. If the parties involved in that agreement, who
10 have signed that agreement -- if one of them violates that
11 agreement, does that have anything to do with you if you
12 didn't sign the agreement?

13 A. No, it does not.

14 Q. So if Southwestern has recourse, it's against
15 Concho?

16 A. That would be correct.

17 Q. All right. What then happens, Mr. Smith?

18 A. There were some phone conversations between
19 Southwestern and myself, and it was made clear to us that
20 they did not desire or were not going to participate in our
21 well, and discussions were really broken off at that point.
22 Sometime later we got a proposal from Sam, proposing their
23 well.

24 Q. When you turn to Exhibit 5, what is that?

25 A. That is Southwestern's proposal to drill their

1 Baywatch "17" Fed Com Number 1 well by letter of March 9th.
2 It's proposed as an Atoka test, 12,600, and it was an
3 anticipated proration unit of the west half.

4 Q. He says if you're interested in participating in
5 their well proposal, he will forward to you a standard
6 operating agreement, naming Southwestern as operator.

7 A. That's correct.

8 Q. Does he make any reference to the Concho-
9 Southwestern operating agreement?

10 A. No, he does not.

11 Q. Does he tell you that the Concho-Southwestern
12 operating agreement named Concho as the operator?

13 A. No, he does not.

14 Q. So he's proposing a different operating
15 agreement?

16 A. Yes, he is.

17 Q. It can't be the same one, can it?

18 A. Apparently.

19 Q. His well proposal is for a well to be drilled to
20 12,600 feet as an Atoka well?

21 A. That's correct.

22 Q. And what is his proposed total AFE cost?

23 A. The completed well cost is \$1.5 million and
24 change.

25 Q. So he's \$150,000 higher, and he's 1000 feet

1 shallower for a different zone?

2 A. That's correct.

3 Q. What then happens, Mr. Smith?

4 A. I've got these a little out of order.

5 Q. I have Exhibit Number 6, which is February 8th.

6 A. Right, February 8th I basically made an offer or
7 tried to make it clear to Southwestern if they didn't want
8 to participate in our well, we would entertain a term
9 assignment of their interest so that we could move forward
10 to get the well drilled.

11 We made them an offer, I believe a reasonable
12 offer, for a term assignment of their interest.

13 Q. All right, the sequence is that we have the
14 December 9th Santa Fe Snyder well proposal --

15 A. That's correct.

16 Q. -- and then first proposal you get from
17 Southwestern is March 9th?

18 A. Correct.

19 Q. And then you, Mr. Smith, and Mr. Thompson trade
20 letters back and forth about the proposal?

21 A. That's correct.

22 Q. All right. Were you able to reach any agreement
23 with Southwestern?

24 A. No, we were not.

25 Q. Exhibits 7 and 8, for the record, are what, sir?

1 A. Exhibit 7 is a letter to Sam reiterating
2 Southwestern's desire -- excuse me, Santa Fe's desire to
3 drill its proposed well, and again extending to them our
4 willingness to enter into a term assignment, should they
5 choose not to participate.

6 Exhibit 8 is Sam Thompson's response to my
7 letter, again taking the position that our well proposal is
8 invalid and that they would move forward with their plans.

9 Q. Mr. Smith, on behalf of your company, have you
10 taken all the necessary prerequisites to having this well
11 drilled?

12 A. Yes, we have.

13 Q. What have you done?

14 A. We have had title examined to the north half; I
15 have a drilling title opinion in hand. We've also made
16 application, an APD, to drill, with the BLM for both Atoka
17 and the Morrow. And based upon a north-half orientation,
18 and --

19 Q. Let's look at that. If you'll turn to Exhibit 9,
20 what are we seeing in Exhibit 9?

21 A. This is the APD that was submitted for our well,
22 to the BLM, and it is for both the Atoka and the Morrow
23 formations, and it's based upon a north-half orientation.

24 Q. When you turn to page 2 of the APD, there is a
25 copy of Division Form C-102?

1 A. That's correct.

2 Q. And what does this show you?

3 A. It shows our staked and proposed location to be
4 at 1980 from the north, 660 from the west of Section 17,
5 and that the anticipated proration unit would consist of
6 the north half of the section.

7 Q. In addition, the caption indicates the two pool
8 names, to the best of your knowledge, you're looking for
9 the Atoka-Morrow --

10 A. That's correct.

11 Q. -- and you've identified it? All right.

12 Subsequent to filing the Application for permit
13 to drill, Mr. Smith, are you aware that the Bureau of Land
14 management issued a letter to the Division in which they
15 discuss about the Bureau of Land Management's rules and
16 regulations concerning communitization of leases?

17 A. Yes, I am, I'm familiar with this letter.

18 Q. This letter was transmitted by facsimile on May
19 1st from the Bureau of Land Management. In response to
20 this issue, did Santa Fe Snyder Corporation submit to the
21 Bureau of Land Management geologic support for its
22 contention that the Bureau of Land Management ought to
23 approve a north-half orientation of the spacing unit and
24 correspondingly, then, by that action, deny Southwestern's
25 request for a west-half orientation?

1 A. Yes, we did.

2 Q. To your knowledge, you are aware that
3 Southwestern submitted their geologic presentation to the
4 Bureau of Land Management, are you not?

5 A. I've been led to believe that they did. I have
6 not seen that material.

7 Q. In response to addressing that issue, has the
8 Bureau of Land Management acted? And if so, how have they
9 acted?

10 A. They acted by approving our APD, after having
11 reviewed both Santa Fe's and Southwestern's geological
12 evidence.

13 Q. Mr. Smith, I show you what's marked as Santa Fe
14 Snyder Exhibit Number 11. Would you identify that for me?

15 A. This is a faxed copy of the BLM approval of --
16 the first page of our APD that shows that the BLM has, in
17 fact, approved our APD, effective May 17th.

18 MR. KELLAHIN: Mr. Stogner, that concludes my
19 examination of Mr. Smith. We move the introduction of
20 Santa Fe Snyder Corporation's Exhibits 1 through 11.

21 EXAMINER STOGNER: Any objection?

22 MR. BRUCE: No, sir.

23 EXAMINER STOGNER: Exhibits 1 through 11 will be
24 admitted into evidence at this time.

25 Thank you, Mr. Kellahin.

1 Mr. Bruce, your witness.

2 MR. BRUCE: Just a few questions.

3 CROSS-EXAMINATION

4 BY MR. BRUCE:

5 Q. In the south half of Section 17, what operating
6 rights does Santa Fe Snyder own?

7 A. 100 percent.

8 Q. Looking at your -- regarding the term assignment
9 from Concho, did anyone from Santa Fe ever go look at
10 Concho's files?

11 A. No, we simply inquired of them as to -- assuming
12 that they would be aware of what they were subject to.

13 Q. Your term assignment from Concho was signed on
14 what date? What, December, 1999?

15 A. It was signed on December 8th by the grantor,
16 that's correct, of 1999.

17 Q. Why wasn't it recorded until April 14th, 2000?

18 A. There was some discussion we had to -- When
19 Southwestern made their assertions as to the validity of
20 our term assignment, we chose to not record it until we had
21 satisfied ourselves that there was nothing that would
22 prevent us from having a valid claim.

23 So it was not immediately recorded. It was in
24 order to investigate Southwestern's claim.

25 Q. One final question, Mr. Smith. You said Santa Fe

1 submitted a letter to the BLM regarding a north-half unit.
2 I believe you testified that Santa Fe submitted a letter
3 after the motion hearing requesting approval?

4 A. We provided geological materials at their
5 request, hand-delivered them to Armando Lopez in Roswell.

6 Q. And you don't have a letter; what you do have is
7 the APD?

8 A. Approved APD, correct.

9 MR. BRUCE: That's all I have, Mr. Examiner.

10 EXAMINER STOGNER: Thank you, Mr. Bruce.

11 Any redirect?

12 MR. KELLAHIN: Yes, Mr. Examiner, if I may. I
13 neglected to ask Mr. Smith his recommendation for overhead
14 rates.

15 REDIRECT EXAMINATION

16 BY MR. KELLAHIN:

17 Q. Mr. Smith, would you advise the Division Examiner
18 what your recommendation is concerning overhead rates on a
19 monthly basis for drilling and producing?

20 A. We would recommend the monthly drilling rate to
21 be \$6000 and producing rate to be \$600. This is based upon
22 the JOA that Southwestern and Santa Fe are currently
23 subject to the north and that that is the overhead rate
24 provided for in that.

25 The rate we're asking for is unescalated. It is

1 the same overhead rate that we started at when the JOA was
2 signed.

3 EXAMINATION

4 BY EXAMINER STOGNER:

5 Q. \$6000 while drilling, \$600 while producing,
6 unescalated.

7 A. We would also -- that's what I'm saying -- Well
8 let me make sure I'm not misunderstood.

9 We considered asking for an overhead rate based
10 upon the current rates to the north, but decided that that
11 would be inequitable, and we are going to ask that we start
12 at the same rates we started at to the north.

13 But I would also ask that we be given the right
14 to escalate these per COPAS rules, should we receive an
15 order.

16 Q. Okay, first you said you wanted unescalated, then
17 you wanted escalated --

18 A. Well, that's why I --

19 Q. -- I guess I'm a little confused.

20 A. Well, yes, when I said unescalated what I'm
21 trying to say is that the rates we're asking to start at
22 are at the same rates that the JOA that Southwestern and
23 Santa Fe started at and the JOA that is subject to -- or to
24 acreage to the north, which we could or thought about
25 considering asking for the current rates for that JOA,

1 which have been escalated. We are not doing that.

2 Q. Okay, so you're basing that \$6000/\$600
3 unescalated on what was given on an order, I'm assuming, up
4 to the north or an agreement?

5 A. No, no, it's a voluntary agreement that both
6 Southwestern and Santa Fe are subject to.

7 Q. And when you say "up north", I'm --

8 A. The Gaucho Unit, approximately four miles north,
9 covering several thousand acres.

10 EXAMINER STOGNER: Thank you. No questions at
11 this time.

12 Mr. Kellahin?

13 MR. KELLAHIN: Thank you.

14 STEVEN D. HULKE,

15 the witness herein, after having been first duly sworn upon
16 his oath, was examined and testified as follows:

17 DIRECT EXAMINATION

18 BY MR. KELLAHIN:

19 Q. Mr. Hulke, would you please state your name and
20 occupation?

21 A. My name is Steven Delbert Hulke. I'm a senior
22 staff geologist for Santa Fe Snyder Corporation in Midland,
23 Texas.

24 Q. Do you spell your last name H-u-l-k-e?

25 A. That's correct.

1 Q. On prior occasions, have you testified as a
2 petroleum geologist before the Division?

3 A. Yes, I have.

4 Q. Are we about to look at your geologic work
5 product?

6 A. That's correct.

7 Q. Are you the geologist for Santa Fe Snyder
8 Corporation that is principally responsible for picking
9 this well location?

10 A. That's correct.

11 Q. In addition, in response to my request, have you
12 analyzed the issues concerning orientation of spacing units
13 and opportunities for a well in Section 17 to test either
14 the Morrow, Atoka or both?

15 A. That's correct.

16 MR. KELLAHIN: We tender Mr. Hulke as an expert
17 petroleum geologist.

18 EXAMINER STOGNER: Any objections?

19 MR. BRUCE: No, sir.

20 EXAMINER STOGNER: Mr. Hulke is so qualified.

21 Q. (By Mr. Kellahin) Mr. Hulke, when we begin to
22 look at your exhibits and see your analysis, were you able
23 to form an opinion as to a recommendation concerning the
24 appropriate risk factor penalty to recommend to Examiner
25 Stogner in this case?

1 A. Yes, I have.

2 Q. Based upon that analysis, are you of the opinion
3 that the risks involved in this well are such that the
4 maximum 200 percent is justified?

5 A. Yes, I am, I believe this is a high-risk Morrow
6 wildcat.

7 Q. When we look at your information, were you able
8 to reach any reliable analysis or preparation of isopachs
9 based upon the available data?

10 A. No, I have not. The well control is sparse, and
11 there are no nearby wells which -- Let me back up. The
12 nearby wells allow me to do anything with the contours I
13 want in this area. Hence, I would say that a net sand map
14 is unreliable.

15 Q. When you're looking at the primary objective for
16 this well, what in your opinion should that objective be?

17 A. The primary objective here is the middle Morrow
18 Grama Ridge sand.

19 Q. And why will that be the primary objective?

20 A. That's the primary objective because the closest
21 large accumulation of gas is in the Gaucho Unit to the
22 north, and we need a large reserve potential to justify the
23 high risk of this well.

24 Q. Southwestern has proposed an Atoka well, have
25 they not?

1 A. Yes, that's correct.

2 Q. Would you rank for us the relationship between
3 the Atoka and the Morrow in terms of priority of
4 opportunity in this section?

5 A. Well, the Atoka is definitely below the Morrow,
6 and I would rank the Atoka below the Grama Ridge sand and
7 below what I call the middle Morrow "A" sand and the Middle
8 Morrow "C" sand. It would be about number four.

9 But they're all -- The Grama Ridge sand is high
10 risk, the other zones are even higher risk.

11 Q. Would you target a prospect well based upon a
12 preference for the Atoka?

13 A. Not with the data I have in hand.

14 Q. It would be too speculative, in your opinion?

15 A. That's correct.

16 Q. When you look at the difference in locations
17 between Southwestern and Santa Fe, is there sufficient
18 geologic data to derive any comfort that that difference in
19 location means anything?

20 A. I have no data in hand to suggest that one
21 location is better than the other one for the Atoka, or any
22 other zone for that matter.

23 Q. Is there sufficient data that you can reliably
24 map the size, shape and orientation of any of these sand
25 packages?

1 A. No, there is not. And furthermore, the data is
2 insufficient to reliably predict that the sand is even
3 present in this location.

4 Q. All right. I have marked your exhibits and that
5 log, the A-A' cross-section, is Exhibit 12, the
6 stratigraphic cross-section, B-B', is Exhibit 13, and then
7 finally your structural middle Morrow marker map as 14.
8 Let's start with 14 first, all right? If you'll unfold
9 that.

10 If you'll look in the southern portion of your
11 display, let's find Section 17. You've got a red square
12 and a green square. What do those represent?

13 A. This map is at a scale of one inch equals 2000
14 feet. North is at the top. The two red squares in Section
15 17 -- the red one is the Santa Fe Snyder location, proposed
16 location; the green square is the proposed Southwestern
17 location. The distance between the wells is approximately
18 900 feet, between the locations, is approximately 900 feet.

19 Q. Is this one of the geologic displays that you
20 submitted to Armando Lopez at the Bureau of Land
21 Management, which form part of their basis for a decision
22 to approve Santa Fe's north-half orientation?

23 A. Yes, it is.

24 Q. When we look at the structure map, what is it
25 that you see in the structure map that causes you to have a

1 preference for placing this well in the northwest quarter?

2 A. I see that it's the -- one of the highest two
3 quarter sections within our acreage block.

4 Q. Why does that mean anything?

5 A. That's important because to the north in the
6 Gaucho Unit, we have six wells producing from the Grama
7 Ridge sand, which is our primary objective, and the two
8 best wells are the two highest wells.

9 Q. Is there a direct structural relationship in the
10 Gaucho area between the best wells and the highest wells?

11 A. Yes, in the Gaucho area there is. The two
12 best --

13 Q. Show us some examples of that.

14 A. In the Gaucho area, the best cumulative
15 production to date is the 2-Y well, in the southwestern
16 quarter of Section 29.

17 The well in the southwestern quarter of Section
18 20 is the Number 3 Gaucho Unit well. At its current rate
19 of production it will surpass the 2-Y.

20 These are predicted to be the two best wells in
21 the unit by a substantial amount.

22 Q. And what do those two wells enjoy over the other
23 wells in this area that causes them to be more productive?

24 A. They have thick sands, but other wells also have
25 thick sands. The important thing seems to be that they are

1 the highest two wells.

2 Q. When we take that analogy and infer it down to
3 17, what is it that you're trying to achieve in 17, based
4 upon the structure map?

5 A. Well, in Section 17, the best location, then,
6 would be the northwestern quarter of Section 17 where it is
7 the highest. And the lowest would be the southeastern
8 quarter of Section 17.

9 Q. Let's talk about your data points. There is a
10 control well in 18 to the west. There is a control well in
11 Section 19 to the southwest. Let's take a moment and pull
12 out the B-B' cross-section, Exhibit 13, and take a look at
13 the logs of those two wells.

14 When we look at the B-B' cross-section, Exhibit
15 13, there is a structural relationship between the well in
16 18 versus the well in 19?

17 A. Yes, the well in 18 is about -- approximately 200
18 feet high to the well in Section 19.

19 Q. Okay. Did either one or both of those wells show
20 any opportunity for gas production in this middle Morrow
21 sand member?

22 A. Yes, the well in Section 19 -- Well, let me back
23 up.

24 Both of these wells were drilled to the Devonian.
25 After the Devonian depleted, we came uphole and attempted

1 to complete in the Grama Ridge sand and other thin sandy
2 zones in the Morrow. The well in Section 19 actually
3 produced about one-third of a BCF from the Grama Ridge and
4 other sands. The well in Section 18 swabbed a show of gas
5 from those sands.

6 Q. Let's look at the log, and let's go uphole and
7 look at the area shaded in blue that corresponds to the
8 Atoka. Do you find that?

9 A. Yes.

10 Q. What have you shaded in here?

11 A. I've shaded in the Atoka bank, which is the -- In
12 this area when you're looking for Atoka, you're looking for
13 a thick Atoka bank.

14 Q. Did either of the operators of these two wells
15 attempt to complete in the Atoka bank?

16 A. No, they did not.

17 Q. And why not?

18 A. The Atoka bank is thin and tight, very tight.

19 Q. How far away do we have to go from Section 17 to
20 find any Atoka bank production?

21 A. To the east, we can go about three miles to the
22 southeast, about three miles.

23 Q. Okay.

24 A. In those locations, the Atoka bank achieves 200
25 to 250 feet thickness and beautiful porosity.

1 Q. You don't see that opportunity here in 17?

2 A. No, these -- The two wells in 18 and 19 are much
3 thinner, thinner productive wells, and the reservoir is
4 tombstone. This is...

5 Q. Southwestern proposes to drill their well to the
6 Atoka at a total depth of 12,600 feet. Where is that going
7 to get them?

8 A. I think that they may have somewhat thicker
9 limestone. I think that it's a high-risk long shot, and
10 substantially higher risk than trying to find production in
11 the Morrow.

12 Q. Is 12,600 feet going to be deep enough to
13 penetrate through and test the Morrow?

14 A. No, it will not penetrate the Morrow. It will
15 penetrate the Atoka in the very top of the Morrow
16 limestone, but will not be objective Morrow clastics zone.

17 Q. Will their well proposal fall short, then, of
18 testing in a major Morrow gas-producing interval in the
19 Gaucho area to the north?

20 A. Yes, it will.

21 Q. Approximately how many feet short have they
22 fallen?

23 A. Five hundred feet, 600 feet.

24 Q. Okay. Let's look at the analogy. If you'll take
25 a moment, let's pull out the A-A' cross-section. On this

1 cross-section, which is the best well, the one in the
2 middle?

3 A. Yes, sir, the Number 2-Y Gaucho unit.

4 Q. That's the big well that's cum'd, oh, 7.7 BCF?

5 A. That's correct.

6 Q. Is that level of productivity explained by the
7 thickness of the reservoir or not?

8 A. Well, certainly in part it's explained by the
9 thickness of the reservoir. Also by its structural
10 position.

11 Q. By analogy, you're hoping that you may have a
12 Grama Ridge sand member in Section 17?

13 A. Yes.

14 Q. Is there any available data at this point to
15 demonstrate to you that it would be of this quality or
16 thickness that we see in the Gaucho area?

17 A. No, the wells in Section 18 and 19 are
18 approximately comparable to the Number 5 Gaucho Unit well,
19 and we are hoping that the sand gets thicker and that it
20 gets thicker to the east of those two wells.

21 Q. And at this point, this would be the first
22 penetration of the Morrow in 17, Section 17?

23 A. Yes.

24 Q. There's certainly nothing in 16?

25 A. No, sir.

1 Q. And then in 20, the closest well in 20 is down
2 there in the northeast southeast?

3 A. Yes.

4 Q. All right. No doubt in your mind, Mr. Hulke,
5 that this is a substantial risk well that justifies the
6 maximum penalty?

7 A. Yes, it is.

8 MR. KELLAHIN: Move the introduction of Mr.
9 Hulke's Exhibits 12, 13 and 14.

10 EXAMINER STOGNER: Any objection?

11 MR. BRUCE: No.

12 EXAMINER STOGNER: 12, 13 and 14 will be admitted
13 into evidence.

14 MR. KELLAHIN: That concludes my examination of
15 Mr. Hulke.

16 EXAMINER STOGNER: Thank you, Mr. Kellahin.

17 Mr. Bruce, your witness.

18 CROSS-EXAMINATION

19 BY MR. BRUCE:

20 Q. Now, Mr. Hulke, you're not presenting an isopach
21 map here today?

22 A. No, I'm not.

23 Q. Is it usual at Santa Fe to drill Pennsylvanian
24 prospects without isopach maps?

25 A. No, not for the Morrow.

1 Q. Gaucho Unit is what, a state unit, I believe? Or
2 do you -- If you don't know, that's fine.

3 Were isopachs prepared for that unit before it
4 was drilled?

5 A. That was drilled before I went to work for Santa
6 Fe. It was discovered in 1996, and I didn't go to work for
7 Santa Fe until the middle of 1997.

8 Q. If isopachs were prepared before that unit was
9 drilled, or do you have an isopach for the Gaucho unit now?

10 A. Yes.

11 Q. I mean, couldn't you by analogy use that to look
12 to the south and predict what might happen?

13 A. Yes. The cross-sections show the entirety of our
14 concept. We believe that the wells in Section 18 and 19
15 are similar to the well in Section 5. They are -- The
16 wells in 18 and 19 are marginal to a sand thick, an alleged
17 sand thick.

18 Q. Now --

19 A. That --

20 Q. Go ahead.

21 A. We believe that that sand thick may be somewhere
22 to the east of the wells in 18 and 19. It could be to the
23 west of them.

24 Q. Now, just eyeballing it from your Exhibit 14, the
25 trend up in the Gaucho unit would be pretty narrow, would

1 it not?

2 A. It's about a mile and a half wide, yes.

3 Q. And there was a Morrow thickness in the well -- I
4 believe that was a BTA well in the northwest quarter of
5 Section 18?

6 A. Yes, it's on cross-section B-B'.

7 Q. Wouldn't it make sense to move a little closer to
8 that well than to move farther away, over into Section 17?

9 A. I think that if the prospect ends up being
10 drilled and, as I hope, it is like the Gaucho accumulation
11 in all respects, the sand, the thickest part of the sand,
12 will be between a half mile and a mile east of the well in
13 Section 18, and the best wells will be in the most
14 northerly wells.

15 Q. Okay, but my question is, wouldn't it be
16 preferable to drill closer to the known data point in the
17 Northwest quarter of Section 18 first, rather than stepping
18 out to Section 17?

19 A. Not necessarily. The well in Section 18 was too
20 thin to achieve commercial production. I don't want to
21 snuggle up to a noncommercial well.

22 Q. Now, looking at the Gaucho unit, there's a well
23 just outside the unit in -- I guess it's in the Bell Lake
24 Unit, Section 32?

25 A. Yes.

1 Q. Is that a poor well?

2 A. It is -- You'll have to tell me what a poor well
3 is.

4 Q. Is it going to be noncommercial?

5 A. It appears that it will be commercial. It will
6 not be as good as the best wells in the Gaucho unit.

7 Q. When was it completed?

8 A. Early this year, February, March.

9 Q. What is its current producing rate?

10 A. It's producing about 2.5 million a day, I think.

11 Q. Okay. Now, you said you wanted to get updip. If
12 that's the case, why wouldn't you move your well to, say, a
13 location 660 feet from the north line? Wouldn't you gain
14 structure doing that?

15 A. Yes, we would gain a little bit of structure
16 doing that.

17 Q. Then why aren't you doing that?

18 A. We wanted to be in a position to help prove up
19 additional locations further to the south. We don't want
20 to drill at the very northern -- We don't want to drill 660
21 feet from the northern limit of our acreage block. We want
22 to drill closer, further to the south, so we can help
23 locate wells in the -- further to the south.

24 Q. Wouldn't you want the best location for the first
25 well?

1 A. Yes. I don't see that there's a substantial
2 difference, technically, between the two location we're
3 talking about.

4 Q. I think just one final question. If you'll look
5 at -- Well, you said you don't have an isopach of the
6 Morrow down in, you know, Section 17 and 18. But if you
7 look at your Exhibit 13 --

8 A. Yes, cross-section B-B'.

9 Q. -- running through the Grama Ridge Morrow you
10 have a thickness interval. Where is this thickness
11 inferred from?

12 A. From the producing analog depicted on cross-
13 section A-A'.

14 Q. Well, I mean, isn't this, in effect, an isopach?

15 A. It's a cross-section depiction. We know that the
16 wells in 18 and 19 are too thin to be commercial. That
17 sand package must thicken to get commercial production.

18 Q. Could you compare the porosities between the
19 Number 1 Gaucho Unit well and the BTA well in the northwest
20 quarter of Section 18?

21 A. Porosity where? In the Grama Ridge sand?

22 Q. Yes.

23 A. Okay, that would be the yellow sand interval and
24 then the --

25 Q. Yes, sir.

1 A. In the Number 1, in the Grama Ridge sand, that
2 porosity averages 10 to 12 percent through that zone.

3 And in the BTA well, is your question?

4 Q. Yes, sir.

5 A. In the BTA well it averages -- well, in the top
6 lobe it averages perhaps 12 percent. The bottom lobe is a
7 lot tighter, it's about 8 percent.

8 Q. So except for the thicknesses, these logs look
9 pretty similar, don't they?

10 A. The Number 1 Gaucho compared to the BTA?

11 Q. Yes, sir.

12 A. The Number 1 well is substantially thicker, so I
13 guess that's correct.

14 Q. Okay.

15 A. I'm not quite sure what you're asking me.

16 Q. And what has the Number 1 Gaucho Unit produced?

17 A. It has cum'd nearly 5 BCF, 4.87.

18 Q. Okay, I can't read the well numbers on your map,
19 I'm sorry for asking that.

20 A. The Number 1 is in the northeast of 29.

21 MR. BRUCE: Okay. That's all I have, Mr.

22 Examiner.

23 EXAMINER STOGNER: Thank you, Mr. Bruce.

24 Any redirect, Mr. Kellahin?

25 MR. KELLAHIN: No, sir.

EXAMINATION

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BY EXAMINER STOGNER:

Q. In referring to Exhibit Number 14, the date you have on this one is May 1st. Is that an update off an existing map that you have in this area?

A. Yes, I have a regional map, which covers many townships.

Q. Okay. Prior to the May 1st, or this edition, what was the previous edition?

A. It was probably updated when there was a well drilled early this year, around February.

Q. And that was -- Is that well depicted on here?

A. That was -- Yes, I think that's the Section 17 well, the Gaucho Number 6 well in Section 17. It's in the southeast of 17, way to the north.

Q. Okay. So off of that map -- What I was getting at, as far as the depiction of the geological interpretation in the southern part, in the immediate area of -- I guess we'll call this the Baywatch versus the White Dove well controversy -- has that changed any, based on that information that you got off the --

A. No, no.

Q. Okay.

A. That information has not changed for some time. And I can virtually assure you that it will change again

1 when this well is drilled.

2 Q. If I was to fold this exhibit in half --

3 A. Which one, sir?

4 Q. Exhibit Number 14.

5 A. Okay.

6 Q. -- where would I find Santa Fe properties?

7 Because Santa Fe did not take in Section Number 17, as I
8 understand it, until the 1st of December; is that correct?

9 A. Yes.

10 Q. Okay, where would be the nearest Santa Fe
11 properties in the southern portion of this exhibit?

12 A. I can't answer that without the land plat.

13 Q. Okay. So Exhibit Number 1 would depict that,
14 would that be right? Mr. Smith?

15 MR. SMITH: Yes, the question?

16 EXAMINER STOGNER: This depicts Santa Fe
17 properties?

18 MR. SMITH: Yes, it does.

19 EXAMINER STOGNER: So that would be a Santa Fe
20 well in Sections 18 and 19, depicted on Exhibit Number 14?

21 MR. SMITH: No, they were drilled by, I believe,
22 BTA and Conoco.

23 EXAMINER STOGNER: Okay. But now they belong to
24 Santa Fe -- or at least Santa Fe has got interest?

25 MR. SMITH: We have acquired term assignments.

1 We have four different term assignments covering the
2 acreage depicted upon that plat before you, and some -- and
3 various fee leases as well.

4 EXAMINER STOGNER: Mr. Smith, while I've got you
5 up, just a clarification. Exhibit Number 11, that was
6 submitted as the last exhibit when you were up?

7 MR. SMITH: That is the approved -- the first
8 page of our APD that was faxed to us by Armando, indicating
9 approval of the APD.

10 EXAMINER STOGNER: What is the approval date by
11 the BLM?

12 MR. SMITH: May 17th.

13 EXAMINER STOGNER: Okay, so that is a "7"?

14 MR. SMITH: Yes, it is. It was --

15 EXAMINER STOGNER: Does yours look as funny as
16 mine does, that number "7"?

17 MR. SMITH: Faxes can do that, but that is --
18 yes, it's -- It was approved yesterday.

19 EXAMINER STOGNER: That was approved yesterday.

20 Okay, I have no other questions of Mr. Smith or
21 Mr. Hulke.

22 Is there any other questions of these witnesses?

23 MR. KELLAHIN: No, sir.

24 EXAMINER STOGNER: Okay, you may be excused.

25 Let's take about a five-minute recess, Mr. Bruce.

1 (Thereupon, a recess was taken at 11:45 a.m.)

2 (The following proceedings had at 12:00 noon.)

3 EXAMINER STOGNER: Hearing will come to order.

4 Mr. Kellahin, is there anything further on Santa
5 Fe Snyder?

6 MR. KELLAHIN: Yes, sir, I have Exhibit 15, which
7 is our certificate of mailing --

8 EXAMINER STOGNER: Okay.

9 MR. KELLAHIN: -- of notification. We move the
10 introduction of Exhibit 15, Mr. Examiner.

11 EXAMINER STOGNER: Any objection?

12 MR. BRUCE: No, Mr. Examiner.

13 EXAMINER STOGNER: Exhibit Number 15 will be
14 admitted into evidence.

15 MR. KELLAHIN: And that concludes our
16 presentation.

17 EXAMINER STOGNER: Thank you, Mr. Kellahin.

18 Mr. Bruce?

19 SAMUEL G. THOMPSON,

20 the witness herein, after having been first duly sworn upon
21 his oath, was examined and testified as follows:

22 DIRECT EXAMINATION

23 BY MR. BRUCE:

24 Q. Would you please state your name and city of
25 residence for the record?

1 A. Sam Thompson, landman. I reside in Katy, Texas.

2 Q. Who do you work for?

3 A. I'm employed by Southwestern Energy Production
4 Company, which is a wholly owned subsidiary of Southwestern
5 Energy Company, which is a 70-year-old utility out of
6 Arkansas.

7 Q. Have you previously testified before the Division
8 as a landman?

9 A. Yes.

10 Q. And were your credentials as an expert accepted
11 as a matter of record?

12 A. Yes, sir.

13 Q. And are you familiar with land matters involved
14 in this case?

15 A. I believe I am.

16 MR. BRUCE: Mr. Examiner, I tender Mr. Thompson
17 as an expert petroleum landman.

18 EXAMINER STOGNER: Any objection?

19 MR. KELLAHIN: No objection.

20 EXAMINER STOGNER: Mr. Thompson is so qualified.

21 MR. BRUCE: By way of introduction, I think it's
22 already been said, Mr. Examiner, that Southwestern seeks an
23 order pooling the west half of Section 17.

24 Q. (By Mr. Bruce) Mr. Thompson, what is Exhibit 1?

25 A. Exhibit 1 is Southwestern's land position in this

1 particular prospect. We have other acreage on this map
2 that we did not color because it's not germane to the
3 prospect. You can see a map behind me that shows our
4 acreage position in the neighborhood.

5 This is our acreage that pertains to this
6 prospect, but we do own an interest in this acreage.

7 EXAMINER STOGNER: Okay, what you're saying is
8 being recorded so --

9 THE WITNESS: Okay.

10 EXAMINER STOGNER: -- when you say "this acreage"
11 and refer to "this", it's not going to come across. So
12 you'll need to describe it, if you will.

13 THE WITNESS: Yes, sir.

14 Q. (By Mr. Bruce) Mr. Thompson, in this particular
15 immediate area, you have acreage in the north half of 17
16 and the north half of 18, 23-34 --

17 A. Yes --

18 Q. -- 23 South, 34 --

19 A. -- yes, we do.

20 Q. Okay. And on Exhibit 1 is just sketched in the
21 proposed west-half unit that Southwestern has proposed?

22 A. Yes, sir.

23 Q. Now, Mr. Smith testified about leasehold
24 ownership. Do you agree with his statements about
25 leasehold ownership in Section 17?

1 A. Steve was right on point on all the land issues
2 as they relate to their acreage plot and to their
3 perception of what their ownership is and was.

4 Q. Okay. I'm going to ask you to refer to Exhibit 2
5 and discuss the chain of events here, but maybe first could
6 you discuss Southwestern's efforts to acquire an interest
7 in this area and get a well drilled?

8 A. Yes, sir. March of 1999, Southwestern entered --
9 March 15th, for the record, Southwestern entered into a
10 joint venture agreement with a company called Concho, who
11 bought Penwell, and it covered, among other lands, Section
12 9, 16 and 17, where we own jointly on a 50-50 basis all
13 lands that were in those sections that were owned either by
14 Concho or Southwestern. In addition to that, we created an
15 AMI that covered additional lands.

16 The purpose of that joint venture was to drill a
17 Morrow well in Section 9.

18 The lands in 17, we earned in that joint venture
19 by cross-assignment, term assignment, and ended up with a
20 half interest in the north half of 17. The lease runs out,
21 I believe, in 2006, but our term assignment with Concho was
22 short.

23 Q. When did the term assignment initially run out?

24 A. The initial expiration of the term assignment was
25 about July 15th of this year.

1 Q. So was a well drilled over in Section -- what, 9?

2 A. Yes, we drilled a well.

3 Q. Okay. And Southwestern is still actively looking
4 to drill in this area?

5 A. We're looking hard, we take deals. We've been in
6 this area for five years, fortunately, by virtue of making
7 a joint venture with Santa Fe in 1995. We are working it
8 hard, we have a full-time staff that works this
9 neighborhood, two geologists, two geophysicists and one and
10 a half landmen.

11 Q. Why don't you move on to your Exhibit 2, and it's
12 a pile of correspondence that starts -- The earliest
13 correspondence is at the back of this exhibit. And move
14 forward and tell the chain of events regarding the
15 Southwestern proposal and Santa Fe's proposal.

16 A. Well, Santa Fe proposed a well on or about
17 December 9th for a north half Morrow well, and that was the
18 first evidence that we had that Concho was no longer
19 purporting to be our partner. I pulled out the contracts
20 that we had with Concho, and exhibit to the joint venture
21 agreement created a multi-area operating agreement. And
22 that agreement was to be constructed on a well-by-well
23 basis and, in fact, was, when we drilled the west half of
24 Section 9.

25 So I wrote Concho on December 14th, some exhibit

1 there, and told them that we didn't honor their sale
2 because, one, we were joint venture partners and didn't
3 know that we no longer were going to be. And two, they had
4 violated the maintenance of uniform interest, which is
5 standard language in the 1982 AAPL model form operating
6 agreement, and sent a copy to Steve for his information.

7 Subsequently --

8 Q. Did you -- Go ahead.

9 A. -- in March of 2000, we had mapped the area for
10 our own benefit and came up with a prospect for the Atoka,
11 and only for the Atoka, and therefore proposed an Atoka
12 well as a west-half unit, because I hope that our maps show
13 that one well in the west half of Section 17 would possibly
14 drain an Atoka well, which in this neighborhood the average
15 Atoka well is 3 BCF. And when you run economics on a 3 BCF
16 well and risk it, you probably only want to drill one well,
17 unless it's tight and you need another well to get the rest
18 of the gas.

19 Therefore, we proposed a well in the northwest
20 quarter as a west-half unit, because it made economic
21 sense.

22 Q. And our next witness will discuss the geology of
23 a west-half unit?

24 A. (Nods)

25 Q. Now, there was still that issue, and that

1 proposal -- looking at your letters, on March 6th, you did
2 send a proposal to Concho, and then --

3 A. Yes, sir.

4 Q. -- then you also sent one to Santa Fe Snyder?

5 A. Yes, we did.

6 Q. There was still an issue regarding the
7 maintenance of uniform interest provision, was there not?

8 A. Yes, sir. I do believe that Santa Fe bought
9 their interest in good faith, and I do believe they asked
10 the right questions.

11 And I do believe the Concho landman, who did not
12 prepare the joint venture, because he did not work for
13 Concho at the time, erred. He pulled a file that did not
14 have the joint venture agreement in it. It had the
15 operating agreements that covered one well.

16 And in the interest of time, him working on 900
17 different projects, he did what he could. And he made a
18 tactical error. He didn't pull the right file, and he
19 didn't disclose the right information. And if it's not
20 disclosed -- Now, we don't file an operating agreement for
21 record. A lot of folks file the tax lien language. We
22 choose not to, because we choose to find partners that we
23 don't think are going to go broke. So we don't file a
24 memorandum to the operating agreement.

25 We chose Concho, we thought they were a good

1 partner, plus they had acreage that we wanted. And as it
2 turned out, we had acreage they wanted. Unfortunately, we
3 drilled a dry hole in the Morrow. And when you drill a dry
4 hole the joint ventures tend to go away, unless you're in
5 it for multi-well and you're willing to stay in and drill
6 four or five Morrow wells. And that's my perception of
7 what happened in this case.

8 Q. Okay.

9 A. They lost interest in the area, after we drilled
10 a dry hole in the Morrow, and chose to sell. Basically,
11 they sold out, and they didn't look at their files and
12 their obligations to us.

13 Q. But it wasn't Southwestern's fault that the JOA
14 wasn't announced to Santa Fe?

15 A. I don't know how it can take the blame for that.
16 I mean, you can argue that we should have filed a
17 memorandum, but we don't. We've chosen not to because
18 there are companies that we deal with, and when you're
19 selling deals and you bring in an investor that may not
20 meet Dun and Bradstreet's definition of a billion-dollar
21 company, some of them get antagonistic when you say, You
22 have bad credit, so we're going to file a financing
23 statement. And we have to look for partners on most deals
24 we do, so we tried to get good partners and treat them
25 right.

1 Q. In your practice as a landman, is it normal for
2 you to go look at the other company's files when you're
3 purchasing an interest from them?

4 A. Well, yes, it is in most cases. I could have
5 made the same tactical error, because if you know the
6 person you believe in him. And the person that Santa Fe
7 was dealing with is believable, he's a good landman, and he
8 just didn't know.

9 Q. As a result of the snafu regarding the operating
10 agreement, was an agreement reached between Southwestern
11 and Concho to terminate the old operating agreement with
12 respect to the north half of Section 17?

13 A. Yes, sir, on April 7th, after tedious
14 negotiation, we got Concho to agree to extend our term
15 assignment from July 15th of 1999 to March 15 of 2000,
16 because of complications and the timing of getting a well
17 drilled.

18 And in exchange for that, we agreed to actually
19 terminate the operating agreement altogether, which
20 obviously wouldn't eliminate the maintenance of uniform
21 interest. That was April 7th.

22 Q. And that letter is part of the Exhibit 2 package?

23 A. Yes, sir.

24 Q. And part of that agreement was, if this
25 termination was made effective -- what, November 30,

1 1999 --

2 A. Mike had made an assignment, term assignment,
3 whatever the date was, and we chose to, in the interest of
4 time, not to have to make him go back and file an amended
5 term assignment. So I said just go by that one. That way
6 you don't have to send it, get it signed, write it, file
7 it, pay for filing fees, and then -- That's a courtesy, if
8 you will, in the land profession, if you don't make the
9 other landman do too much paperwork. They may owe you a
10 favor down the road.

11 Q. Even though the operating agreement was
12 terminated effective November 30th, 1999, did you intend
13 that to validate Santa Fe's well proposal in December of
14 1999?

15 A. No, sir. We believe in our prospects, we feel
16 like we proposed it honestly at first, and had we known
17 that there was something coming, we probably would have
18 proposed it a little sooner, but we weren't quite ready to
19 act. We were still doing stuff in about the eight sections
20 offsetting the drill site, because of the risk.

21 Q. And because of the problems involved in this, as
22 I said, snafu, you in return got an extension of your
23 term --

24 A. Yes, sir --

25 Q. -- of your term assignment?

1 A. -- we did.

2 Q. So at least as of this point there's no real
3 immediate deadline or need to drill this well, say, by
4 June?

5 A. There's no deadlines other than districts and
6 teams have goals that need to be met quarterly and
7 annually. If you don't drill wells, you don't stay
8 employed. So in the interest of drilling wells and finding
9 production and adding value, yeah, we want to drill a well
10 this year.

11 Q. In your opinion, has Southwestern made a good-
12 faith effort to obtain the voluntary joinder of Santa Fe in
13 Southwestern's proposed well?

14 A. It's my personal opinion that we have, and we
15 tried, and we may continue to try, because it's a small oil
16 patch and you need partners. And if you don't have them --
17 It's just tough to drill 100-percent wells.

18 Q. Southwestern has been in a number of wells with
19 Santa Fe?

20 A. Yes, sir.

21 Q. Okay. Would you move on to your Exhibit 3 and
22 identify that for the Examiner?

23 A. This is Southwestern's opinion of what it costs
24 to drill an Atoka well, prepared by Jim Tully, who's our
25 drilling engineer in Houston, showing a dry hole of about

1 \$1.1 million and a completed well of about \$1.3 million.

2 And that's projected...

3 Q. And this is the AFE that was sent to Santa Fe?

4 A. I believe it is.

5 Q. Now, when Southwestern prepares AFEs -- I don't
6 know how to phrase this -- do they like to put forth what
7 they think will be the maximum cost of a well?

8 A. Again, when we do an AFE, we don't like to do a
9 supplemental. Our engineers have chosen to run high on the
10 actual AFE itself. They have a bonus plan that if they
11 come in for the year under AFE, they have the right to a
12 bonus.

13 But more than that, when we do bring in a partner
14 I'm not real keen on sending a supplemental AFE saying that
15 we told you it's going to be \$1 million, but here it is
16 \$1.8 million, sign here and believe us next time. So we do
17 run them -- We're high. We believe that AFE is high, yes,
18 sir.

19 Q. What has been the results of Southwestern's
20 drilling with respect to AFE costs? Have they come in high
21 or low or what?

22 A. Across the country, they've come in low. And
23 those engineers have been fortunate in their drilling
24 program. And we've drilled out in New Mexico and so far
25 have come in under AFE.

1 Q. By what percentage, roughly?

2 A. The best one, 20 percent. The worst one is in
3 the five-to-six-percent-under-AFE range.

4 Q. Okay. So part of the reason you do this is
5 simply to let your drilling partners know what the maximum
6 cost should be?

7 A. That's part of it, and the other part is
8 reservoir engineering. They do everything they can to risk
9 these projects. And by adding more cost, obviously, the
10 risk goes up. So if it meets all their criteria of high
11 dollars still works and risk still works, then management
12 will buy into drilling a well.

13 Q. Okay. In your opinion, is the cost proposed on
14 your AFE reasonable and in line with the costs of other
15 wells drilled to this depth in this area of New Mexico?

16 A. Yes, sir.

17 Q. And does Southwestern request that it be
18 designated operator of the well?

19 A. Yes, sir.

20 Q. Now, Mr. Smith recommended overhead rates of
21 \$6000 and \$600 per month. Does Southwestern have any
22 problem with those rates?

23 A. That's a reasonable rate.

24 Q. And to be escalated according to COPAS, like Mr.
25 Smith requested?

1 A. Annually, it would escalate based on inflation.

2 Q. Mr. Thompson, is Exhibit 4 simply my affidavit of
3 notice of the hearing to Santa Fe?

4 A. Yes, it is.

5 Q. Now, Mr. Thompson, of course you've become aware
6 of the federal regulation regarding the forming of a well
7 unit on a single federal lease?

8 A. Yes, sir, for the last five years out here,
9 Southwestern Energy has primarily been a nonoperator, and a
10 lot of the wells have been drilled with Santa Fe. And we
11 admit to being rookies, and the letter I got from Steve was
12 the first evidence I had that, in fact, they were going to
13 require that a well be drilled on one specific federal
14 lease for whatever reasons when, in fact, the geology may
15 tell you to do something else.

16 So knowing that on May 11th, I forwarded the maps
17 behind me. I forwarded our geology to Alexis Swoboda by
18 Fedex and told her, in fact, to call me or my geologist Jim
19 Denney if she had any questions, and that we would be glad
20 to come through Roswell on the way to Santa Fe to tell our
21 story.

22 Q. At this point, Southwestern hasn't heard back
23 from the BLM regarding its proposed west-half unit?

24 A. Only through Santa Fe. Apparently they have been
25 awarded the permit.

1 Q. But you have not gotten any letter from the BLM
2 stating that the BLM --

3 A. No, sir.

4 Q. -- does not approve a west-half unit?

5 A. I don't have anything, but I've been gone too.

6 Q. Southwestern has gone and staked its location out
7 there --

8 A. Yes, sir.

9 Q. -- has it not? Commenced the proceeding to file
10 an APD?

11 A. Yes, sir.

12 Q. Okay.

13 A. And found Santa Fe farther along and knew that
14 this Application would come here to this area, so we
15 haven't, admittedly, done as thorough a job as Santa Fe has
16 on attempting to get the APD. We hoped that our evidence
17 that we display for the Atoka well would reward us with the
18 opportunity to drill a west-half unit, that they at that
19 time would apply.

20 Q. Okay. Were Exhibits 1 through 5 prepared by you
21 or under your supervision, or compiled from company
22 business records?

23 A. Yes, sir.

24 Q. And in your opinion, is the granting of
25 Southwestern's Application in the interests of conservation

1 and the prevention of waste?

2 A. We think it is.

3 MR. BRUCE: Mr. Examiner, I'd move the admission
4 of Santa Fe's Exhibits 1 through 5.

5 EXAMINER STOGNER: Any objection?

6 MR. KELLAHIN: No, sir.

7 EXAMINER STOGNER: Exhibits 1 through 5 will be
8 admitted into evidence at this time. Thank you, Mr. Bruce.
9 Mr. Kellahin, your witness.

10 CROSS-EXAMINATION

11 BY MR. KELLAHIN:

12 Q. Mr. Thompson, when did you first become aware of
13 the Bureau of Land Management Rules and Regulations
14 concerning the consolidation of multiple leases, pursuant
15 to a communitization agreement?

16 A. The actual rule, whatever the date that Steve
17 sent me, the ruling. Prior to that time, in conversations
18 with Steve, that's been helpful. He's implied that they
19 tend to favor drilling on a lease if the BLM has a 320 that
20 they'd rather have you drill on it for convenience.

21 Q. You weren't aware of this until Mr. Smith brought
22 it to your attention?

23 A. The actual order itself and the numbers?

24 Q. The process or the procedure or the letter from
25 the BLM that's been introduced into evidence.

1 A. I believe that's true, yes.

2 Q. Okay. So how long have you been a landman?

3 A. It will be 31 years next year.

4 Q. How much of that activity has been in New Mexico?

5 A. Well, I started with ARCO in 1974 in Midland.

6 Q. How much of that involves federal leases?

7 A. Well, I worked on the entire Abo unit in 1974 for
8 ARCO, and over a period of 30 I've probably got ten years
9 of New Mexico experience.

10 Q. And you weren't aware of their policy and
11 practice concerning communitization of multiple leases and
12 the preference for a single lease --

13 A. I'm going to have to say no.

14 Q. -- did not know that?

15 A. When I was working with ARCO, the engineering
16 department handled that sort of thing, and it didn't
17 pertain to me.

18 Q. What caused you to send the May 11th letter,
19 then, to the BLM?

20 A. Well, Steve's letter to, and Jim Bruce's, advised
21 me to do that. so...

22 Q. So you did?

23 A. Yes, sir.

24 Q. And what specific geologic data did you submit to
25 the BLM in support of your company's position for a west-

1 half orientation? What did you send them?

2 A. Well, it would be the maps that my geologist
3 presents, but the maps are on the wall behind me.

4 Q. Those are --

5 A. Those are the maps that were submitted to
6 Roswell?

7 Q. And that was it?

8 A. I believe that was it, yes, sir.

9 Q. By Federal Express on May 11th?

10 A. Yeah.

11 Q. And you understood the purpose of that was to
12 provide your geologic position to the BLM so that they
13 could make a decision about which way they wanted to orient
14 this spacing unit for the Atoka and for the Morrow, right?

15 A. Well, she told me -- and I'll repeat it, and I
16 have -- Send me what you've got, I will present it to
17 Armando. If he has any questions we will call you. If we
18 deem it necessary to come to this hearing, we will.

19 And I haven't heard back from them.

20 Q. I'm correct in understanding your belief though,
21 that the purpose for submitting the Data to the BLM was so
22 the BLM could make a decision about the orientation of the
23 spacing unit?

24 A. Okay.

25 Q. Right, isn't that what it was for?

1 A. I would think so.

2 Q. That's what your letter says, right?

3 A. Yes, sir.

4 Q. You're advancing a west-half orientation?

5 A. I still am.

6 Q. Are you aware that the Bureau of land management
7 has decided that issue against your company?

8 A. You told me that it has.

9 Q. Yes, sir, have you seen that approved APD that
10 approves the north half for the Atoka and the Morrow?

11 A. I've seen evidence that it has --

12 Q. Yes, sir.

13 A. -- but I thought that the geology might prevail
14 over some rule.

15 Q. Apparently it didn't, did it?

16 A. Well, I'm not sure what their unit --

17 Q. Well, they have data, their decision after
18 receipt of your geologic data, right?

19 A. Okay.

20 Q. Okay.

21 A. Then we'll pursue it further.

22 Q. All right. The AFE that you've submitted in the
23 hearing, Exhibit Number 3 --

24 A. Uh-huh.

25 Q. -- it was your testimony a while ago that, in

1 your opinion, this is a fair and reasonable AFE for this
2 type of well?

3 A. You know what? It's presented by my drilling
4 department.

5 Q. Yes, sir, it's what for what? \$1.3 million?

6 A. And I've testified that that's all I've got to go
7 on. Do I have a personal opinion?

8 Q. No, sir, I'm just asking you if this is the AFE
9 that you sent --

10 A. I have testified that that's the AFE that my
11 company has represented that we will live with.

12 Q. All right. And if I understood you correctly,
13 this is the AFE that you attached to your March 9th letter
14 when you're proposing the Southwestern well and its
15 location to Mr. Smith and to Santa Fe Snyder, correct?

16 A. It should be.

17 Q. All right, sir.

18 A. I have several like these.

19 Q. All right, sir. The Exhibit Number 2 that you've
20 introduced is a composite of correspondence. Would you
21 flip through with me and find the letter that represents
22 Southwestern's proposal? Have you found it?

23 A. My Exhibit 2 is a letter from Santa Fe to --

24 Q. Yes, sir, skip past --

25 A. -- Southwestern.

1 Q. There are a whole bunch of these stapled
2 together.

3 A. Oh, there are?

4 Q. Yes, sir. Exhibit 2 --

5 A. Let me get my file.

6 Q. If you'll flip to the fifth page down on your
7 Exhibit 2 --

8 A. Okay, I'm pretty familiar with it.

9 Q. All right, sir, I've got your March 9th letter.
10 This is your letter to Mr. Smith. This is the first
11 proposal that Southwestern is making for a well in 17,
12 correct?

13 A. Yes, it is.

14 Q. All right. Explain to me, sir, how you were able
15 to send the March 9th letter, which included an AFE,
16 proposing this well to Santa Fe, when the AFE says it
17 wasn't prepared until the following month?

18 A. Well, like I said, there's all kinds of AFEs that
19 we had. That may not be the right AFE.

20 Q. Well, that's my question. What AFE did you
21 submit with your well proposal?

22 A. The costs that are on that AFE should be the
23 costs that Steve received. Whether that's the actual AFE
24 or not, those are the actual costs.

25 Q. Will you agree with me that an April 6th AFE

1 could not possibly have been the AFE proposed in the March
2 9th letter?

3 A. It could be, that's -- it doesn't make --

4 Q. It's got to be, right?

5 A. Sure.

6 Q. Have you looked at Mr. Smith's Exhibit Number 5,
7 in which he attaches a copy of your March 9th letter?

8 A. Okay.

9 Q. Do you have that?

10 A. No, but what does it say?

11 Q. Well, I'm going to give it to you. Attached to
12 that is an AFE that's dated January 31st by your company
13 for \$1.5 million.

14 A. To what?

15 Q. What?

16 A. To what zone?

17 Q. To the Atoka at 12,700.

18 A. Okay.

19 Q. 12,600.

20 A. Okay.

21 Q. Take a look at that. My question, Mr. Thompson,
22 is, what AFE are you circulating in your well proposal that
23 proposes the estimated well cost for the well?

24 A. The AFE that Steve has --

25 Q. Yes, sir.

1 A. Steve has a better file, probably, than I do,
2 because he does a very thorough job. The AFE that Steve
3 has and received is the correct AFE.

4 Q. So what do I do with Exhibit Number 3 that you
5 now tell me is the correct AFE?

6 A. Well, if it were I, I would substitute the one
7 that we're going to drill with, which is the Baywatch, that
8 Steve has attached to the letter that I sent him, because
9 that's the one we'll be drilling under.

10 Q. All right. So Exhibit Number 3 is not the right
11 AFE?

12 A. No, sir.

13 Q. Okay. Let's talk about Santa Fe's position.
14 Santa Fe's got a term assignment from Concho Resources
15 that's made effective December 1st, 1999. You saw that in
16 the stuff that Steve introduced, didn't you, Mr. Thompson?

17 A. Yes.

18 Q. Okay. There is no doubt in your mind, is there,
19 sir, that the parties can sign a document and agree to an
20 effective date that either precedes or post-dates the date
21 of the document, correct?

22 A. Yes, you might.

23 Q. You do it all the time, don't you?

24 A. You bet.

25 Q. In fact, you've done it in this case too, haven't

1 you?

2 A. Yes.

3 Q. Okay. So on December 1st of 1999, there is
4 simply no doubt that Santa Fe has an interest in the north
5 half of Section 17, correct?

6 A. Say that again?

7 Q. Yes, sir. So on December 1st, 1999, because of
8 the term assignment, there is simply no doubt that Santa Fe
9 has got a 50-percent interest in the north half of 17,
10 right?

11 A. Not in my opinion.

12 Q. Not in your opinion?

13 A. Not in my opinion?

14 Q. You don't think -- They don't think they have an
15 interest?

16 A. When they received notice that there was an
17 operating agreement --

18 Q. Uh-huh.

19 A. -- and that there was maintenance involved --

20 Q. Uh-huh.

21 A. -- in my judgment, they should get that waived,
22 no matter what the date of the term assignment was, because
23 the term assignment that was done on that day was invalid.

24 Q. Well, let's keep the sequence straight. The
25 interest is December 1st, 1999.

1 A. Uh-huh.

2 Q. You're contending now, after you've told me that
3 the joint operating agreement, which was not of record, and
4 for which Santa Fe had no knowledge as a good-faith
5 purchaser, is now still bound and obligated by that
6 agreement? Is that your position?

7 A. Uh-huh. Yeah, I believe that any time you enter
8 into any contract, that you're bound by all prior
9 contracts, whether it be gas contracts or contracts that
10 you're not aware of, and subsequent to that, that you're
11 surprised when you find out you're bound by a 20-percent
12 gas contract that you didn't know about, you're still bound
13 by it.

14 Q. Well, let me understand your position. Your
15 position is, Santa Fe is bound by that joint operating
16 agreement, despite the fact it's not of record, correct?

17 A. Uh-huh.

18 Q. Despite the fact that you could have put it of
19 record, "you" being Southwestern, right?

20 A. Which we never do.

21 Q. Yeah, or you could have put a memorandum of that
22 agreement of record to put him on notice, right?

23 A. Which we didn't need to do.

24 Q. None of that was done?

25 A. Because we were joint-venture partners with one

1 company.

2 Q. So Santa Fe, as a good-faith purchaser, which you
3 have admitted --

4 A. Uh-huh.

5 Q. -- with no knowledge of the existence of this
6 operating agreement, is now bound by this agreement? Is
7 that your position?

8 A. That's the -- Yeah, that's the one we stay with.

9 Q. Yeah. What is your definition of a good-faith
10 purchaser?

11 A. What is it?

12 Q. Yes, sir.

13 A. That he checks everything with due diligence and
14 buys it in good faith. But if, in fact, there is a
15 contract out there that he's not aware of, it's certainly
16 not the seller's fault, and he's certainly bound by it
17 until it is either violated or it goes away.

18 Q. And you raised that issue with Concho about their
19 failure to maintain the uniform interest provision under
20 the operating agreement, right?

21 A. Yes.

22 Q. Yeah, you raised that issue with them. And in
23 exchange for that and other things, you got an extension of
24 your term agreement, right?

25 A. We do.

1 Q. And you did that by a settlement letter with
2 Concho, didn't you?

3 A. Yes, we did.

4 Q. Did you have authority to sign that settlement
5 agreement?

6 A. I've got authority, yes.

7 Q. All right, sir, let's look at the settlement
8 agreement. It's an April 7th letter, you've just
9 introduced it. Shall we find it? It's Exhibit Number 2.

10 A. Okay.

11 Q. Have you got it in front of you?

12 A. Sure.

13 Q. I don't see you looking at it, Mr. Thompson.

14 A. Well, you know what it says, though.

15 Q. No, sir, I want to make sure you know what it
16 says. If you'll turn to page 3, let's look at it. Have
17 you got one?

18 A. Okay. What date is it?

19 Q. April 7th, year 2000.

20 A. Okay, I've got it here.

21 Q. All right, sir. Two-page letter, signed by
22 Michael Gray, landman for Concho, and that's agreed to and
23 approved by someone that says they're a vice president of
24 exploration for Southwestern Energy, right?

25 A. Richard Lane?

1 Q. I guess that's Lang; is that what that signature
2 says?

3 A. Right.

4 Q. Do you have the signature page there?

5 A. Yeah.

6 Q. One of the things being discussed, if I've read
7 this correctly -- Did you negotiate this?

8 A. Yes, I did.

9 Q. All right, and it was signed off by Mr. Lane,
10 right? --

11 A. Uh-huh.

12 Q. -- on behalf of your company, but you negotiated
13 it?

14 A. Yes, I did.

15 Q. All right. When you look on page 2 and you look
16 at number 6 --

17 A. Okay.

18 Q. -- it says "From and after the date hereof, but
19 effective as of November 30, 1999 -- "

20 A. Uh-huh.

21 Q. " -- the JOA shall be deemed to be terminated in
22 all respects as to all lands other than the east half of
23 9..." Right?

24 A. Uh-huh.

25 Q. We are releasing the operating agreement from the

1 north half of 17 by this settlement. True?

2 A. True.

3 Q. And we're doing so retroactive, for all purposes.

4 A. Does that make the proposal retroactive?

5 Q. Sir?

6 A. The well proposal that was done in December, does
7 that mean that thing is invalid in your judgment?

8 Q. Yes, sir, you have terminated your operating
9 agreement November 30th, 1999, and thereby have validated
10 the Santa Fe Snyder Corporation's well proposal of December
11 9th by your own action, right?

12 A. In your opinion.

13 Q. Yes, sir.

14 A. In your opinion.

15 Q. You could have, had you believed otherwise, added
16 a paragraph 7 which would have preserved that issue for
17 you, couldn't you? You could have done that?

18 A. We didn't feel like we needed to.

19 Q. Now, you talked about this area of interest.
20 There was a well that you drilled to earn an interest, and
21 that was in what? Section 19, was it?

22 A. Nine.

23 Q. Nine, in Section 9.

24 A. Uh-huh.

25 Q. Show me the well on one of these maps that

1 drilled to earn the interest. Where is it?

2 A. Well, first of all, we cross-assigned -- we had
3 acreage in 9, they had acreage in 16 and 17.

4 Q. Yes, sir.

5 A. We had the acreage, we cross-assigned the acreage
6 before -- we already owned the interest, we didn't -- we
7 didn't earned the interest in 16 and 17. Nobody owned the
8 interest in 9.

9 Q. All right, so Section 9 is northeast of 17 that
10 we're fussing about, right?

11 A. I'm not fussing about 9, that doesn't have
12 anything to do with this --

13 Q. No, sir, in 17, the controversy in question today
14 is 17, right?

15 A. Yes, sir.

16 Q. Are you with me?

17 A. Uh-huh.

18 Q. Section 9 is to the north and east, correct?

19 A. Yes, sir, it is.

20 Q. The well that earned the interest is in the
21 northwest quarter of 9, true?

22 A. Uh-huh.

23 Q. Okay. Was that well drilled by southwestern.

24 A. Drilled by Concho.

25 Q. Drilled by Concho?

1 A. Uh-huh.

2 Q. Are there any of these Morrow or Atoka wells on
3 this map that are drilled or operated by Southwestern?

4 A. On the size of your map, I don't think so.

5 Q. On the size of your map?

6 A. There's not a well on any of those maps that's
7 operated by --

8 A. A well operated by us --

9 Q. Yes, sir.

10 A. -- to the Morrow?

11 Q. Yes, sir.

12 A. I'm going to defer to my geologist.

13 Q. You don't know if you operate any of those wells?

14 A. Santa Fe operates the Gaucho Unit.

15 Q. I believe you told me in direct testimony that
16 you didn't find any fault with Mr. Smith and how he went
17 about checking for possible burdens on the north half of
18 17. Is that a fair way to characterize it?

19 A. Yes, it is.

20 Q. And that had you been in his position you would
21 have probably ended up in the same place he's in right now;
22 is that not true?

23 A. Knowing the players, yes.

24 Q. Yes, sir. Who's the player at Concho that you
25 were dealing with for whom you had faith in this deal?

1 A. Mike Gray was the landman that was handling that
2 in the end. Van Rogers was the gentleman that I made the
3 joint venture with in 1999.

4 Q. Okay. Your well proposal of March 9th of the
5 year 2000 was your first proposal for a well in 17,
6 correct?

7 A. Yes, sir.

8 Q. You acquired an interest in 17 the year before,
9 true?

10 A. Yes, we did.

11 Q. And it took you an entire year to make a
12 proposal, correct?

13 A. To re-map after drilling a dry hole in the
14 Morrow, yes.

15 MR. KELLAHIN: Yes, sir. No further questions.

16 EXAMINER STOGNER: Thank you, Mr. Kellahin.

17 Mr. Bruce, redirect?

18 REDIRECT EXAMINATION

19 BY MR. BRUCE:

20 Q. Mr. Thompson, regarding the AFE, apparently there
21 was a mixup, but if you look at the AFE in Santa Fe's
22 package, is it your opinion that that AFE is fair and
23 reasonable for the Baywatch well?

24 A. The AFE that I know that we have that's relative
25 to this drill site is the one that Steve has, and it is

1 \$1.1 million, and I apologize for that, but it is \$1.1
2 million dry and it is \$1.5 million completed.

3 Q. And again, that would be the maximum cost, and
4 you anticipate a lower cost than that?

5 A. It's the maximum cost that my engineering
6 department anticipates on this well.

7 Q. Now, Mr. Kellahin just said it took you an entire
8 year to make a well proposal in Section 17. Of course,
9 Southwestern was out there drilling other wells, was it
10 not?

11 A. Yes, we were.

12 Q. So this was not the first well proposal under the
13 Concho operating agreement?

14 A. Under the Concho joint venture, the only well
15 that was drilled so far was in Section 9, under the Concho
16 deal. We have other deals to the north that we have
17 drilled, and one of them was just for the Atoka.

18 Q. Okay.

19 A. And it's called our Tin Cup, in Section 25 to the
20 north.

21 Q. So this Section 17 isn't the only well that
22 Southwestern is interested in, in this township or in this
23 general area?

24 A. No, sir.

25 Q. I think you said if it had been you, in the

1 exercise of due diligence you probably would have gone over
2 and looked at Concho's file regarding this prospect, would
3 you not?

4 A. I don't think I would have had time, but I would
5 have probably sent some contract landman over and perused
6 the prospect file, just for the sake of -- that my
7 immediate boss would make me.

8 Q. Due diligence?

9 A. Where I come from, you kind of go by gentleman's
10 agreements, and if somebody like Mike Gray told me that
11 there wasn't one, and it was my decision -- and it wasn't,
12 because I worked for somebody else -- I would have probably
13 said, Okay, fine.

14 Q. And finally, on the April 7th letter terminating
15 the JOA, that clearly states in there that as of that March
16 7th, the JOA is effective as to Section 17, does it not?

17 A. Yes.

18 Q. So Concho recognized at that point that that JOA
19 was effective?

20 A. At that point.

21 MR. BRUCE: That's all I have, Mr. Examiner.

22 EXAMINER STOGNER: Mr. Bruce.

23 EXAMINATION

24 BY EXAMINER STOGNER:

25 Q. A few clarifications here. As far as the

1 ownership, since we are seeking to force pool the west
2 half, I want to make sure I'm clear on the ownership of the
3 west half. Who is Southwest seeking to force pool?

4 A. According to my records, Santa Fe owns three-
5 fourths of the southwest -- I mean, the west half. And we
6 own one quarter.

7 I don't know the relationship, what Conoco backs
8 in for or gets, but I believe that Santa Fe does have a
9 trade made with them that gives them that interest under
10 some arrangement.

11 Q. Okay, so the southwest quarter of Section 17 is
12 100 percent Santa Fe; is that correct?

13 A. According to my records.

14 Q. Okay.

15 A. The land map will show that Continental Oil, now
16 Conoco, has that HBU.

17 Q. But you're not force pooling Conoco?

18 A. No, sir.

19 Q. You're force pooling Southwest --

20 A. Yes, sir.

21 Q. -- I mean, I'm sorry --

22 A. Santa Fe.

23 Q. -- Santa Fe.

24 And the northwest quarter is still 50-50 Santa
25 Fe-Southwestern?

1 A. Yes, it is.

2 Q. Has an APD been filed with the BLM for this
3 Baywatch well?

4 A. It has not been filed.

5 Q. And when will that be filed?

6 A. Well, to me it's academic. If you don't have the
7 right to drill it, there's no reason to file it. We don't,
8 as a rule at Southwestern, just do stuff and then knowing
9 that there's some chance we have it protested at hearing --
10 Why spend the money? We've proposed the well, we've staked
11 it, we've spent money on it to get to that point. But
12 knowing that we were coming to this hearing, my engineers
13 chose not to file an APD.

14 Q. Okay. So is a -- Seeing that there is a May 17th
15 approval by the BLM for the APD, who has jurisdiction of
16 processing APDs, is Southwest's plans -- do they plan or
17 have they filed an appeal or an objection to that APD?

18 A. I don't have formal notice. If that constitutes
19 formal notice, when would I have filed?

20 Q. What do you consider formal notice? Do you mean
21 to you personally, or to public record?

22 A. To our company. They dragged in a fax, and the
23 first time I heard about it was today. When would I have
24 filed my appeal? During the recess?

25 Q. That's what I'm asking you, sir. Do you plan to

1 file an appeal if this is based on public record? I'm
2 asking you that, sir.

3 A. I plan to take that back to my company and ask
4 them. I don't have authority to appeal anything.

5 Q. Okay, so you don't know at this point?

6 A. No, sir.

7 EXAMINER STOGNER: Mr. Bruce, do you want to
8 restate your motion to change this case again to me, what
9 modifications need to be done?

10 MR. BRUCE: Excuse me, Mr. Examiner?

11 EXAMINER STOGNER: Whenever we called Case
12 12,423, I asked for some verification, and there was
13 something missing in this particular case, and you said
14 there was, and you made a motion to strike some of the
15 things you were requesting. Do you want to repeat that
16 again?

17 MR. BRUCE: I may have misspoken, Mr. Examiner.
18 I think we would be seeking -- Since the well is in the
19 northwest quarter, we would be seeking to pool 320-acre
20 units, 160-acre units and 40-acre units, although the
21 Application neglected to seek an unorthodox oil well
22 location in the event that a shallow oil zone was
23 encountered.

24 EXAMINER STOGNER: Okay, so what we need to do in
25 this particular instance is to readvertise and seek an

1 unorthodox oil well location for the 40-acre tracts; is
2 that correct?

3 MR. BRUCE: That is correct, sir.

4 EXAMINER STOGNER: And you are prepared today,
5 since we're hearing it, to justify this ten foot off of a
6 quarter quarter section line in which we had referenced
7 earlier in a Conoco matter. The same similar situation, or
8 is there some difference?

9 MR. BRUCE: Yes, it is, Mr. Examiner. As I said,
10 I think the geologist will say that the chances of oil are
11 unlikely. I would also point out that the northwest
12 quarter is entirely one federal lease with common interest
13 ownership throughout that northwest quarter, in fact, the
14 entire north half.

15 But if the Division chooses not to grant an
16 unorthodox location, we would understand. The location is
17 based on the Atoka.

18 EXAMINER STOGNER: Okay, no other questions of
19 this witness. You may be excused.

20 Mr. Bruce?

21 JAMES J. DENNEY, JR.,

22 the witness herein, after having been first duly sworn upon
23 his oath, was examined and testified as follows:

24 DIRECT EXAMINATION

25 BY MR. BRUCE:

1 Q. Would you please state your name and city of
2 residence for the record?

3 A. My name is James J. Denney, Jr., and I live in
4 Houston, Texas.

5 Q. How do you spell your last name, for the court
6 reporter?

7 A. D-e-n-n-e-y.

8 Q. Who do you work for and in what capacity?

9 A. I'm a geologist employed by Southwestern Energy
10 Production Company.

11 Q. Have you previously testified before the
12 Division?

13 A. No, I have not.

14 Q. Would you summarize your educational and
15 employment background for the Examiner?

16 A. I've got a bachelor's degree and a master's
17 degree from Stephen F. Austin State University in
18 Nacogdoches, Texas, and I've been working in the oil
19 business for about 20 years.

20 Q. Okay. How long have you been working for
21 Southwestern?

22 A. About five years.

23 Q. Does your area of responsibility at Southwestern
24 include southeast New Mexico?

25 A. It does.

1 Q. And are you familiar with the geologic matters
2 involved in these two Applications?

3 A. Yes, I am.

4 MR. BRUCE: Mr. Examiner, I'd tender Mr. Denney
5 as an expert petroleum geologist.

6 EXAMINER STOGNER: Any objection?

7 MR. KELLAHIN: No objection.

8 EXAMINER STOGNER: So qualified.

9 Q. (By Mr. Bruce) Mr. Denney, in your opinion, what
10 is the primary objective for a well in the northwest
11 quarter of Section 17?

12 A. It would be the Atoka.

13 Q. Would you please refer to your first exhibit,
14 Exhibit 6, and if it helps you, stand up at your Exhibit 6.
15 Be sure when you're pointing out wells or any other
16 pertinent information to note the section for the court
17 reporter.

18 A. Very good. This is a map, a structure map, done
19 on a marker at the top of the producing Atoka interval.
20 There's a type log section along the right-hand side of
21 this map, which shows five different porosities which
22 produce in this trend. I've got them broken out by the "A"
23 porosity at the top, "B" porosity, "C" porosity, "D"
24 porosity and "E" porosity at the base of this interval.

25 On the map is a large red-shaded area which

1 indicates the overall main trend of Atoka production in the
2 area. This trend has produced something over 100 BCF of
3 reserves, very significant. Each of the wells that are
4 colored red on that map represents production from the
5 Atoka. There are production cums posted by each well that
6 was productive out of the Atoka interval. An average well
7 on this trend is something on the order of about 3 BCF and
8 60,000 barrels.

9 And the one thing that I would hope that viewers
10 of this exhibit will get would be that the Atoka trend
11 passes over closures, and it also extends through a low
12 area, and that it is not controlled by structure.

13 Our acreage position in Section 17 is shown
14 shaded in yellow, the north half of that section.

15 Our proposed location is shown at a location of
16 1310 from the north and the west line of that section.

17 Our proposed TD is 12,600 feet, approximately.

18 And also, our recommended unit, 320-acre unit
19 that we would like to form up is shown in the green
20 outline, which indicates a west-half orientation for that
21 unit.

22 Also shown on the map in Section 9, the northwest
23 quarter of Section 9, is the Concho Caballo well, which was
24 completed in the Atoka. It did make some gas out of the
25 Atoka.

1 Q. Was that well drilled to the Morrow?

2 A. That well was, in fact, drilled to the Morrow,
3 and it was unsuccessful. That was one of my personally
4 generated prospects that we sold to Concho, but it failed
5 in the Morrow.

6 And we did make an Atoka well, approximately a
7 million ninety-nine, and that's what actually got me
8 started looking at this Atoka trend, and it kicked off a
9 fairly lengthy Atoka study that I've completed.

10 Q. Is that part of the reason you don't think the
11 Morrow is productive in Section 17?

12 A. Well, this geology stands for the Atoka. I have
13 worked the equivalent sands, the three main producing
14 intervals that Steve Hulke showed on his cross-sections. I
15 have extensive mapping with those sands also. The Morrow
16 is -- We are playing the Morrow in the area. I essentially
17 cannot show a Morrow prospect there. My isopaching mapping
18 does not support a prospect, which is why I'm not here to
19 promote a Morrow well.

20 Q. Why don't you move on to your Exhibit 7, which I
21 believe is your gross interval isopach, and discuss its
22 contents for the Examiner?

23 A. Okay. Let's see, the gross interval isopach is
24 Exhibit 7?

25 Q. Yes.

1 A. Okay, I don't have mine numbered up here, Mr.
2 Examiner, I'm sorry.

3 This is an isopach over approximately Township 22
4 South, 34 East, and 23 South, 34 East, which is an isopach
5 of the overall producing interval, which contains these
6 five porosities. And I'd refer you back to this exhibit,
7 the structure map. It's these five porosities, it's this
8 interval right here.

9 EXAMINER STOGNER: This interval right where?

10 THE WITNESS: Pardon?

11 EXAMINER STOGNER: This interval right where?

12 THE WITNESS: On the right-hand side of the
13 structure map.

14 EXAMINER STOGNER: Exhibit Number 6?

15 THE WITNESS: Exhibit Number 6.

16 EXAMINER STOGNER: I can't see anything without
17 my glasses far off, so I'm going to be looking at my
18 exhibit.

19 THE WITNESS: Okay. Well, it's a gross-interval
20 isopach on the interval on Exhibit 6. And essentially what
21 it shows, it shows the reason for the overall -- which I
22 believe to be the overall trend of the Atoka production in
23 the area.

24 And what I would hope you could see off of that
25 map is that generally the trend of the production would

1 parallel the isopach lines, which would indicate to me as a
2 geologist, that is a strike-oriented body. In other words,
3 this gross-interval isopach map is a map which is
4 representative of conditions that existed during the time
5 these units were possible, okay?

6 We use a map like this, or I use a map like this,
7 the gross-interval isopach map, to help me contour the
8 individual porosities, porosities "A", "B", "C", "D" and
9 "E".

10 In other words, if the main trend is strike-
11 oriented and you come up to the area which contains the
12 Concho Caballo well in the northwest of Section 9 and it
13 has production there, the logical place to look for this
14 production or another prospect involving that same similar
15 zone would be on strike or to the southwest of the Caballo
16 well in the northwest quarter of Section 17, 23 South, 34
17 East, our proposed location.

18 From the gross-interval isopach, Exhibit 7, I can
19 take you to Exhibit 8, which is a -- it's a net-porosity
20 map on our main objective, which is the "E" porosity, the
21 "E" porosity, which is located at the bottom of the type
22 log section back on Exhibit 6.

23 And what it shows is a progression of porosity
24 pods extending from, say, Section 26 in 22 South, 34, back
25 down to the southwest, through the Concho well, Caballo

1 well, in the northwest of Section 9, and on to the proposed
2 location southwest of there in the north half -- or the
3 northwest quarter of Section 17 in 23 South, 34 East.

4 And it also shows another trend which begins
5 somewhere in Section 14 of 23 South, 34 East, southwest of
6 there, on into Section 32 of 23 South, 34 East.

7 And essentially what we're looking for here at
8 this location in the northwest of 17 is a well similar to
9 the Shell well that was drilled in the northeast quarter of
10 Section 28. And I refer to the map here. That well had
11 approximately 24 feet of net porosity. And this well was
12 only perforated in the "E" porosity, and it has cum'd --
13 let's see, I believe it's 11.7 BCF and 152.4 thousand
14 barrels. Let me restate that: 152,400 barrels. Very good
15 well.

16 And we feel like we've got a case for a look-
17 alike of that well. And as the geology shows, it is
18 representative of a west-half of Section 17 productive
19 area.

20 Q. (By Mr. Bruce) Mr. Denney --

21 A. Yes.

22 Q. -- what you're saying is that the way you map it,
23 only the west half of Section 17 would be productive in the
24 Atoka?

25 A. That is correct.

1 Q. Okay. Now, overall -- and I think you've already
2 hit on this -- in looking at the Atoka in this area, do you
3 have to look at a regional trend?

4 A. Yes, sir, you do. And I'd like to point out at
5 this time that the Santa Fe structure map cuts off at
6 approximately the eastern edge of 16, Section 16 of 23
7 South, 34 East, and if you were going by just that map you
8 would have no idea about a 100-BCF trend sitting just off
9 to the east of it. It's a very large accumulation.

10 Q. Why don't you move on to your cross-section?

11 A. Okay, I'll refer to the line of section that is
12 posted on Exhibit 8, the isopach map of the "E" porosity,
13 and this line of section begins up in Section 4 of 23
14 South, 34 East, with the Rio Blanco well, the Santa Fe Rio
15 Blanco Well Number 1. It goes into the southwest quarter
16 of Section 4, the Rio Blanco Number 2 well. From there it
17 continues south into the northwest quarter of Section 9,
18 the Concho Caballo well. It then travels off to the
19 southwest, into the southwest quarter of Section 8.

20 And from there it goes through our proposed
21 location in the northwest of Section 17. It then traverses
22 westward into the BTA well located in the northwest quarter
23 of Section 18, and then finally it ends up through a well
24 in the northwest quarter of Section 19, of 23 South, 34
25 East.

1 And that Exhibit 9 is the cross-section itself.

2 The Rio Blanco well is located to the north.

3 And what this cross-section shows is the
4 development of where we believe the gas is coming from in
5 this Caballo well. And I say "where we believe it's coming
6 from", because the Caballo well is an open-hole completion.
7 It's completed open-hole from an approximate depth of
8 11,784, which is the base of the intermediate casing, to a
9 plugback depth of 12,250, an open-hole plugback.

10 And this completion was an effort to attempt to
11 save face from the Morrow dry hole that we had drilled.
12 And this well came on in May of 1999, making approximately
13 1.7 MCF -- Well, let's see. 1.7 million cubic feet a day,
14 31 barrels of oil and zero barrels of water.

15 It had a flowing tubing pressure of around 2300
16 pounds on a 14/64-inch choke. And during the past year,
17 the well has experienced numerous production problems, as
18 you might expect from your open-hole completion. It's only
19 been able to cum something on the order of 143 million
20 cubic feet, as best we can tell. We're not the operator of
21 the well, so my numbers may be a little bit behind, but
22 it's approximately that much.

23 And what it -- Back to the cross-section, Exhibit
24 9, what it shows is, the porosity development that occurs
25 here. We've basically developed, by my map, by my isopach

1 map, at our location in 17. The porosity is absent in the
2 well in 19 of 23 South. It's absent in the well in 18 of
3 23 South, 34 East. It's also absent in Section 8 of 23
4 South, 34 East, and also absent in Section 4 of 23 South,
5 34 East.

6 It is present, it would appear to be present, in
7 the Number 1 Rio Blanco well. And this is currently a zone
8 of interest for Santa Fe and ourselves, by virtue of a
9 recent recompletion proposal that we received from them
10 to --

11 Q. Santa Fe operates Rio Blanco Number 1?

12 A. Yes, they do.

13 Q. And they have proposed a recompletion of that
14 well?

15 A. That's correct.

16 Q. In what zone?

17 A. In this particular interval, inclusive of that
18 interval.

19 Q. In the Atoka?

20 A. Yes, in the Atoka.

21 And I guess that would be all I would have to say
22 about that.

23 Q. Okay. Based on your geologic study -- And by the
24 way, your maps were not made expressly for this hearing,
25 were they?

1 A. No, they were not. I've added some things, you
2 know, to it, to show -- to update our position and
3 everything.

4 But these maps were actually used to drill
5 another prospect located -- If we went back to Exhibit 6,
6 in the southwest quarter of Section 25 of 22 South, 34
7 East, there's a well there called the Southwestern Energy
8 Number 1 Tin Cup. It's shown as an open circle. And we're
9 currently attempting a Wolfcamp completion in that well
10 right now. This well failed for the Atoka. It was drilled
11 as an Atoka prospect.

12 And I've personally been involved in this area
13 since the -- actually before the drilling of the Concho
14 well, but I would repeat again that we've been looking at
15 the Atoka in here since we made that completion in the
16 Concho Caballo well in Section 9 of 23 South, 34 East. I
17 think we can demonstrate a history in here, at least.

18 Q. Based on your study, do you believe it's
19 reasonable to drill only to the Atoka rather than to the
20 Morrow?

21 A. That's correct.

22 Q. One other thing, Mr. Denney. Regarding potential
23 uphole -- And this location was based -- the location you
24 picked, the 1310 from the north line and from the west
25 line, was based on the Atoka, was it not?

1 A. It was not only based on the Atoka, but it was
2 based on my best Atoka location.

3 Q. Okay.

4 A. I believe that's the way a prospect ought to
5 happen. I give the land department my best location.

6 Q. Regarding uphole zones from the Atoka -- and in
7 particular, uphole oil zones -- is there much in this area
8 that has been producing?

9 A. I haven't done a whole lot of mapping concerning
10 the shallow producing intervals, but at an early time
11 during my involvement in this area I familiarized myself
12 with the first objectives in the area, and the Bone Spring
13 produces some in the area, the Delaware produces some. But
14 it would not seem to me to be a viable target.

15 So I would say no, I'm not expecting anything
16 shallow.

17 Q. Okay. Do you agree with Mr. Hulke that drilling
18 these deep gas wells in this area is a risky prospect?

19 A. Yes, I do.

20 Q. And you don't have any problem with the maximum
21 cost-plus-200-percent risk penalty proposed by Mr. Hulke,
22 do you?

23 A. No, I do not.

24 Q. Were Exhibits 6 through 9 prepared by you or
25 under your direction?

1 A. Yes, they were.

2 Q. And in your opinion, is the granting of
3 Southwestern's Application in the interest of conservation
4 and the prevention of waste?

5 A. Yes.

6 MR. BRUCE: Mr. Examiner, I'd move the admission
7 of Southwestern Exhibits 6, 7, 8 and 9.

8 EXAMINER STOGNER: Any objection?

9 MR. KELLAHIN: No, sir.

10 EXAMINER STOGNER: Exhibits 6, 7, 8 and 9 will be
11 admitted into evidence at this time.

12 Thank you, Mr. Bruce.

13 Mr. Kellahin, your witness.

14 MR. KELLAHIN: Thank you, Mr. Stogner.

15 CROSS-EXAMINATION

16 BY MR. KELLAHIN:

17 Q. Mr. Denney, the net isopach in the Atoka, this
18 net "E" Atoka --

19 A. Yes, sir.

20 Q. -- having the greatest thickness of net "E" Atoka
21 sand is a primary objective of yours in locating a well,
22 true?

23 A. It is one consideration.

24 Q. All right. When we consider the minimum number
25 of net "E" Atoka sand necessary to make a commercial well,

1 do you have a standard for a minimum?

2 A. Well, the performance of porosities throughout
3 the trend varies, and I would like to refer back to Exhibit
4 8 to give reference to that.

5 On the isopach map, Exhibit 8, there is a well
6 which is located in the northwest quarter of Section 11, 23
7 South, 34 East, and the way I have it --

8 Q. You've 22 feet in there, right?

9 A. Yes, that's correct.

10 Q. All right, and was that a commercial well?

11 A. Yes, it was.

12 Q. Do we have other Atoka wells on your map that are
13 commercial with less than 22 feet?

14 A. Yes, I'd say so.

15 Q. All right. What is the minimum number of Atoka
16 clean net sand that is necessary for a commercial well?

17 A. Repeat the question, please, Mr. Kellahin.

18 Q. Yes, sir. Do you have a minimum number, as a
19 cutoff, above which you're necessary to have sufficient
20 sand quality to be a commercial well?

21 A. Well, Mr. Kellahin, I was about to point out that
22 just because you have thickness doesn't guarantee a very
23 good well. And if you'd just let me continue here, this
24 well I was referring to in the northwest quarter of Section
25 11, 23 South, 34 East, has 22 feet of thickness. It has a

1 somewhat limited extent mapped.

2 And the reason why it has a limited extent is
3 that it is -- some of the control around there, there's
4 some zero points. This well is a very similar section to
5 the Shell well. However, it only produced about 1.5 B's.

6 So there are some lateral-extent issues that are
7 also in control of reserves. The height of your reservoir
8 is not the only factor affecting whether or not your well
9 is commercial, how much reserves you're going to get out of
10 it.

11 Q. Are there commercial wells on the map with less
12 than 22 feet? And if so, where are they?

13 A. Well, I'm not -- a particular awareness of your
14 question. I can look back and forth between my production
15 figures and the "E" map, if you want to --

16 Q. Well, let's try it this way. On Exhibit 8, if I
17 go to the northwest of 17 and I'm looking at your proposed
18 location --

19 A. Yes.

20 Q. -- find me the nearest Atoka well that's a
21 commercial Atoka well.

22 A. I would say it's kind of a toss-up between --
23 well, let me -- I want to make sure about the term
24 "commercial".

25 Q. Yes, sir.

1 A. "Commercial" to me means that it's worth
2 producing.

3 Q. Well, let's put it a different way. Let's put it
4 a different way.

5 A. A well --

6 Q. "Commercial" to me would be a well that is
7 sufficient enough to pay for its costs.

8 A. Okay, very well.

9 Q. Okay?

10 A. I would say the well in Section 11 would perhaps
11 be a well like that.

12 Q. Be the nearest one that you can find --

13 A. Might be the nearest one, yeah.

14 Q. All right, so we've got to go one, two, almost --
15 what, three miles to the west southwest to get to our
16 location from that well?

17 A. I'd say that's approximately correct.

18 Q. All right. But you admit that you're using net
19 thickness as a criteria to pick your well location?

20 A. I would say it's one consideration. I would say
21 that its position on my gross interval isopach map, which
22 would be Exhibit 7 --

23 Q. Yes, sir.

24 A. -- would be another strong consideration.

25 I would also tell you that besides thickness,

1 staying in trend, I would also want to be as close as,
2 perhaps, I could get to the Caballo well.

3 Q. All right, anything else?

4 A. No.

5 Q. All right, let's look at those criteria in the
6 Section 17, and if I'm looking at maximum net thickness as
7 one of the components, then by your map Santa Fe Energy's
8 proposal is better than yours, true?

9 A. Actually, that's not true.

10 Q. Well, let's look at your map.

11 A. Well, it loses out on two of the criteria issues
12 that I just previously stated.

13 Q. You're jumping ahead of my question, sir. If
14 you'll stay with the criteria we're focusing on --

15 A. Okay.

16 Q. -- which is the net thickness in this sand
17 member, which you tell me is one of them, true?

18 A. Yes, sir.

19 Q. Applying that alone, right?

20 A. Yes.

21 Q. Looking at your map, Santa Fe's location is
22 better than yours?

23 A. Yes, yes, by my map.

24 Q. All right. We're going to use the other
25 criteria, we're going to use at gross-thickness

1 relationship. Let's look at the gross map, okay?

2 A. Okay.

3 Q. When we look at the gross map, your location
4 falls north and west of the 200-foot thickness contour
5 line, true?

6 A. Yes.

7 Q. The Santa Fe location is south and east of the
8 200-foot line, and it's going to be thicker than your
9 location, true?

10 A. Yes, it could be.

11 Q. All right, now, let's look at the third criteria.
12 The third criteria is structure, right? Yes?

13 A. No.

14 Q. Is structure a criteria?

15 A. No, sir, it's not.

16 Q. Structure is not a criteria?

17 A. No, sir. I thought I demonstrated that on
18 Exhibit 6 with the overall trend of the Atoka production,
19 not -- It would not apparently be linked to structure.

20 Q. All right, so when we look at the structure map,
21 your conclusion from the structure as it underlies 17 is
22 that it doesn't matter to you about its structural
23 position?

24 A. Well, the structure is just what it is. It just
25 follows the structure map where it fell.

1 Q. I can accept that. My point is, there is not
2 much difference in structure --

3 A. No, I agree with that.

4 Q. -- between the two locations?

5 A. I agree with that.

6 Q. Okay. Let's look at trend, which was a criteria,
7 right?

8 A. Yes.

9 Q. When we look at the net "E" Atoka map, the trend
10 I see in here, Mr. Denney, is a trend to drill wells that
11 have zero net "E" Atoka sand within this vicinity of
12 Section 17. Is that the trend you want me to see?

13 A. I'm not sure I understand your question.

14 Q. All right, sir, let's look at 17. When I look at
15 17 and I look north in Section 8, the Continental well, the
16 Bell Lake Unit well, it's zero, right?

17 A. That's correct.

18 Q. All right, and I go west of 17 into 18, and I've
19 got the BTA well that's zero, right?

20 A. That is also correct.

21 Q. We're down to the southwest offset in 19.
22 Continental Oil well in the northwest quarter is another
23 zero line, right?

24 A. It is another zero point.

25 Q. Zero point.

1 A. Yes.

2 Q. I move over to 20, and the only point of control
3 I have in 20 is another zero, right?

4 A. Section --

5 Q. -- 20?

6 A. -- 20?

7 Q. Yeah, the northeast southeast?

8 A. Okay, yes --

9 Q. Right?

10 A. -- there's a zero posted there.

11 Q. You've got no control in 17, right?

12 A. No.

13 Q. No control in 16, right?

14 A. That's correct.

15 Q. So other than inference or speculation, what
16 caused you to draw a contour in excess of 10 feet within
17 this area of 17 that you've located your well?

18 A. I would state that that proposed location which I
19 have made and the recommendation I have made to my
20 management, based on my reputation of a geologist, which is
21 -- who puts viable prospects together --

22 Q. I'm looking at the well control, Mr. Denney.

23 A. Yes.

24 Q. I don't see anything in this area that justifies
25 you putting a contour in excess of 10 feet within the pod

1 that you're trying to hit for the Atoka well.

2 A. Well --

3 Q. Why did you do that?

4 A. -- Mr. Kellahin --

5 Q. Yes, sir.

6 A. -- this production I'm referring to up in Section
7 26, in the southeast quarter of that section, the northeast
8 quarter of Section 34, 22 South, 34 East, the northwest
9 quarter of Section 35 of 22 South, 34 East, and the Concho
10 well, as -- and also the Santa Fe well, if that -- I'm
11 sorry, but I -- that is a trend, and --

12 Q. All right, let's look at the trend.

13 A. -- that is a trend which currently -- currently,
14 and I say "currently", stops at the Caballo well.

15 Q. Let's look at your trend. Take 34, and let's
16 look at the trend to the south and southwest. The trend
17 goes into Section 4, right? The trend you have mapped is
18 not in excess of 10 feet, right? And the trend continues
19 down, by your interpretation, down into 17, where you now
20 put a 20-foot thickness. Why, is the question.

21 A. I thought I that I had stated that earlier. I
22 stated in my earlier testimony that we are looking for a
23 look-alike to the Shell well, located in the northeast
24 quarter of Section 28, 23 South and 34 East.

25 I would also point out that the Shell well, with

1 24 feet of porosity in it, is the only well with 24 feet of
2 porosity in that little trend, in that separate trend. We
3 are looking for a look-alike to that.

4 Q. All right. But my point is, there is no direct
5 data within the trend to the west of that well that
6 supports your interpretation of a thickness greater than 10
7 feet?

8 A. It is an inference based on my experience and my
9 ability to get wells drilled for my company.

10 Q. All right. And you have chosen not to present
11 any of the maps that would deal with the Morrow, true?

12 A. I have chosen not to present any of the maps that
13 dealing with the Morrow, because I don't believe it's a
14 viable target here. It's not pertinent to our request.

15 Q. How many additional feet would you have to drill
16 the Atoka well in order to test the concept of Morrow
17 production?

18 A. I think it's something like 1000 feet. I think
19 you have hit on it earlier. That's accurate, I agree with
20 that.

21 Q. And what are the costs associated for the
22 additional 1000 feet? Do you know, sir?

23 A. No, I do not. But a common-sense approach would
24 tell you that to go 1000 feet deeper costs more money. I
25 mean --

1 Q. If the Examiner grants Santa Fe Energy's
2 Application to compulsory pool a spacing unit consisting of
3 the north half for a well to be drilled as Santa Fe
4 proposes, would you recommend to your management that you
5 go nonconsent, or would you participate?

6 A. Mr. Kellahin, I cannot answer that question at
7 this time, and the reason why I cannot is that I have
8 presented to my management a location at 1310 out of that
9 corner, and I do not have authority to answer that question
10 at this time.

11 Q. When we look at your criteria for showing your
12 location, am I correct in understanding that that criteria
13 improves in all instances if we use the Santa Fe location?

14 A. No, sir, you're incorrect.

15 Q. All right, tell me which of the four criteria is
16 not satisfied or improved upon at the Santa Fe location.

17 A. The first one would be -- We're at a projected
18 thickness in the northwest of 17 that would be more like
19 the producing well. That would be the first thing.

20 The second thing would be that the rule I gave
21 you about balancing thickness and positioning in the trend
22 as staying close to the production in the Caballo well, the
23 Santa Fe well doesn't exactly measure up on those two
24 criteria, or the Santa Fe proposal.

25 Q. Apart from proximity to the Caballo well and the

1 trend interpretation, Santa Fe's location satisfies the
2 rest of the criteria in your package, true?

3 A. Yes.

4 MR. KELLAHIN: No further questions.

5 EXAMINER STOGNER: Thank you, Mr. Kellahin.

6 Mr. Bruce, redirect?

7 MR. BRUCE: Just a couple of follow-up questions.

8 REDIRECT EXAMINATION

9 BY MR. BRUCE:

10 Q. Mr. Denney, Mr. Kellahin was questioning why --
11 how can you extend the Atoka trend to justify well
12 location, wasn't he? Or to justify a well, period?

13 A. Yeah.

14 Q. Well, you've seen -- you've looked at the Morrow
15 in this area too, haven't you?

16 A. I have, and Greg did too.

17 Q. And you've seen Santa Fe's Morrow map?

18 A. I have.

19 Q. Regarding a Morrow well in this area, was the
20 Morrow productive in Section 19, to the southwest of this
21 well?

22 A. Not to my knowledge. I think Steve had indicated
23 that that was a show well.

24 Q. What about the well to the west, in the northwest
25 quarter of 18? Did that well produce in the Morrow?

1 A. That was nonproductive in the Morrow.

2 Q. And then the Caballo well, I believe it is, in
3 the northwest quarter of Section 9?

4 A. That was a Morrow failure.

5 Q. So the three closest Morrow wells were dry in the
6 Morrow?

7 A. They were all failures.

8 Q. And the nearest production from the Morrow is
9 what, about four miles north in the Gaucho unit?

10 A. The nearest Grama Ridge production is, yes, sir.

11 Q. Meanwhile, you do have evidence of the Atoka, not
12 only just from the trend, but in the Caballo well in the
13 northwest quarter of Section 9?

14 A. That's correct, a little over a mile away.

15 Q. So the closest production you have is in the
16 Atoka?

17 A. That's correct.

18 Q. And that obviously played into why you want an
19 Atoka well here?

20 A. That sure helped support my prospect.

21 Q. Would you rather rely on a well that's a mile
22 away or a well that's four miles away?

23 A. I want the closer control.

24 Q. And all the close Morrow control is dry?

25 A. That's correct.

1 Q. And therefore you think drilling to the Morrow is
2 unreasonable?

3 A. I think it represents a much longer extension
4 than what I'm proposing.

5 Q. You're extending about a mile, and for Santa Fe's
6 well you'd have to extend what? Four miles?

7 A. Yes, sir.

8 Q. And so drilling an extra thousand feet is going
9 to cost extra money to drill to something that, by all
10 nearby evidence, is dry?

11 A. That's correct.

12 MR. BRUCE: That's all I have, Mr. Examiner.

13 EXAMINER STOGNER: Any other questions of this
14 witness?

15 MR. KELLAHIN: (Shakes head)

16 EXAMINER STOGNER: No other questions, you may be
17 excused.

18 Closing statements at this time?

19 MR. BRUCE: Mr. Examiner, there are several
20 issues to address in this case. As we've stated in our
21 testimony, first, does Santa Fe have a valid Application?
22 The second issue regards BLM approval. And the third, tied
23 in with the second, is, whose Application should be
24 approved?

25 Southwestern still asserts that when Santa Fe

1 proposed a well it owned no interest in the well unit. The
2 Division has been stern, as you well know, on when a party
3 proposes a well ad when it comes to the Division for force-
4 pooling.

5 We would submit that at the time when Santa Fe
6 proposed its well, it did not own a valid interest, and, if
7 this is permitted, that anyone without an interest will be
8 able to propose a well, hope things shake out, and then
9 come to the Division after it acquires an interest. We
10 don't think that's proper, and we believe Santa Fe's
11 Application is invalid.

12 Secondly, BLM approval. Now, when the motion
13 hearing first came -- Mr. Kellahin has submitted as his
14 Exhibit 10 the letter from the BLM. At the motion hearing
15 he said, End of story, Southwestern can't get a west-half
16 unit, despite the fact that in that letter it says in
17 certain instances the BLM will approve a com agreement,
18 even in a situation such as this, in other words, a west-
19 half unit comprising parts of two 320-acre federal leases.

20 Santa Fe has submitted an approved APD. It's the
21 first we've seen of it. But we have not yet heard from the
22 BLM regarding our Application. The BLM and the OCD itself
23 have in the past approved multiple APDs on a well unit and
24 let the parties fight it out, and that's where we are
25 today. Until we hear from the BLM that they will not allow

1 a west-half unit, we think this matter is still up in the
2 air.

3 The final issue is whose Application to approve.
4 And in this instance I'm citing from Order Number
5 R-10,731-B. When there are contested or two contrary
6 pooling applications, the most important consideration in
7 awarding operations is geologic evidence.

8 We believe that the testimony shows that the only
9 reasonable prospect in the northwest quarter of 18 is the
10 Atoka. The Atoka is the only geology that shows a
11 reasonable chance of success. If you look at the Morrow,
12 it can't even be mapped. Nobody knows what's going to
13 happen, and all the surrounding Morrow wells are dry.

14 At least in this area, you have an Atoka show.
15 And based on trends in the area, the Atoka is a reasonable
16 prospect. Southwestern sees no need to spend the extra
17 money to go down to try out another dry hole in Section 17.

18 Another issue is good-faith negotiations. We
19 believe that the parties have traded letters back and
20 forth, and at this point -- As Mr. Thompson said, maybe
21 they'll negotiate further. But at this point they're at a
22 stalemate.

23 This issue gets back to the first issue I said.
24 If Santa Fe's initial proposal letter was invalid, we don't
25 know how it can be validated after the fact.

1 Other issues to consider are risk penalty. Both
2 parties agree that this is highly risky and that 200
3 percent is appropriate.

4 Which parties should have operations? Both
5 parties have Morrow-Atoka operations in this area. We
6 think Southwestern, based on its mapping of the geology,
7 should be awarded operations.

8 Finally, differences in AFEs. Santa Fe will
9 claim that its AFE is lower. The fact of the matter is,
10 once you factor in the lower AFEs that Southwestern has
11 been getting as a matter of fact on its wells, there's
12 really no difference in AFEs, or in fact the Atoka AFE will
13 be lower.

14 We believe if you look at all of those instances,
15 Southwestern's Application, the well location and
16 operatorship should be awarded.

17 Thank you, Mr. Examiner.

18 EXAMINER STOGNER: Thank you.

19 Mr. Kellahin?

20 MR. KELLAHIN: Mr. Stogner, Mr. Thompson applauds
21 Mr. Smith's efforts to be diligent, thorough and fair. Mr.
22 Smith goes through the process, he's diligent, he's
23 thorough, he's fair. Concho for whatever reason fails to
24 disclose to Mr. Smith the existence of a joint operating
25 agreement. Mr. Smith and his company are good-faith

1 purchasers without knowledge of that agreement.

2 Mr. Thompson acknowledges that. He says that if
3 he were Mr. Smith he would have done the same thing, and if
4 he did all he could do, it was fair and reasonable. It's
5 true, it's fair and reasonable.

6 It's fair and reasonable to assume that a company
7 that checks the records and finds no instrument of record,
8 that asks the seller and is told there are no operating
9 agreements, can rely upon all that.

10 It is undisputed that on December 1st, 1999,
11 Santa Fe Energy, Santa Fe Snyder Corporation, acquired an
12 interest in the north half of 17. Mr. Thompson admitted,
13 it is common, it is not unusual, to take an agreement and
14 post-date it or make it retroactive. And that's what's
15 done here. So nine days before Mr. Smith sends out his
16 well proposal, he has an interest.

17 And then what happens? Mr. Thompson claims that
18 the well proposal Santa Fe made is somehow not valid. And
19 how could it not be valid? Well, he claims their seller
20 has violated a provision of this unrecorded operating
21 agreement, which he admits could have been recorded, and
22 that it's somehow Santa Fe's fault.

23 Well, Ms. Hebert and I and Mr. Bruce all know,
24 this is not Santa Fe's problem, it's not their fault. They
25 are good-faith purchasers, and they made a valid well

1 proposal.

2 But you know, it's interesting that all that
3 disappears. Because on April 7th, the year 2000, Mr.
4 Thompson on behalf of his company negotiates with Michael
5 Gray a settlement letter.

6 And isn't it interesting, because they didn't
7 have to, but in that letter they agree to terminate the
8 operating agreement? They didn't terminate it effective
9 April 7th, 2000; they make it retroactive to November 30th.
10 They could have picked a different day. But they chose a
11 date that validates the Santa Fe well proposal. So if
12 there's any question about that, they have removed the
13 question by waiving the claim and changing and voiding the
14 contract.

15 Quite frankly, I don't think you have to do
16 anything about it. If Southwestern really thinks that's an
17 issue, they can go to the courthouse and we'll adjudicate
18 the contract down before some district judge.

19 We believe we're entitled to a force pooling
20 order because we made the first well proposal. We have a
21 substantial interest, we're going forward with this, we
22 would like to go forward with it.

23 The only landman in this room that's been
24 diligent has been Mr. Smith. He's got the drilling title
25 opinion, he's filed his APD. And guess what, the Bureau of

1 Land Management has approved his APD and his orientation,
2 and by doing so has denied Southwestern's request.

3 At the motion hearing two weeks ago, Mr. Bruce
4 waved the letter from the BLM at us and said, Wait a
5 minute, there is still an opportunity for the BLM to look
6 at the geology.

7 We said, All right, let's send them the geology.
8 And both companies were afforded the opportunity to send
9 their geology to the BLM. And guess what happened?
10 Yesterday the BLM approved Santa Fe's APD. And by doing
11 so, has asserted primary jurisdiction over this matter and
12 resolved any dispute about orientation.

13 So the only thing left for you to do, Mr.
14 Examiner, is to enter a compulsory pooling order awarding
15 to the operator or interest owner who first developed the
16 prospect, first proposed the well and is here prepared to
17 drill the well.

18 Isn't it interesting that Southwest comes before
19 you today with a west-half orientation? And look what
20 happens. All of a sudden, with 25-percent interest, they
21 want to force-pool 75 percent of the other interests? Why
22 shouldn't we leave it a north-half orientation? The BLM
23 has dictated that solution anyway. Both companies have a
24 50-50 percent share. And yet they think there's a
25 difference in location.

1 Look at the Atoka, look at Mr. Denney's maps.
2 Quite frankly, we satisfy most if not all his criteria,
3 despite his disagreement with me. Look at the maps. Our
4 locations had a better thickness on his own map. We follow
5 a gross trend that's thicker. If he cares about structure,
6 which he says is not important, we're equivalent.

7 We believe we're entitled to a force-pooling
8 order, Mr. Examiner, and we would ask that you enter one on
9 our behalf. Thank you.

10 EXAMINER STOGNER: Thank you, Mr. Kellahin.

11 Clarification, Mr. Bruce. With this matter
12 having to be readvertised, it won't be readvertised till
13 the June 15th hearing, this being a contested matter. Do
14 you foresee the need of any further witnesses or testimony
15 at that time?

16 MR. BRUCE: I don't think in this matter, Mr.
17 Examiner. Chances are, these same parties may be up here
18 again on a related matter, so if anything is necessary, if
19 you desire any more information. But at this point I don't
20 see any more need in this matter.

21 EXAMINER STOGNER: In that instance, this case,
22 even though it's going to appear on the June 1st, will be
23 continued and readvertised for June 15th.

24 Which brings us up to Case Number 12,393 at this
25 particular point. Do we take it under advisement or

1 continue it also?

2 MR. BRUCE: Mr. Examiner, I think there are still
3 two competing Applications. Until we get final word from
4 the BLM, I think one order should be entered on both cases.

5 EXAMINER STOGNER: Thank you, Mr. Bruce.

6 Mr. Kellahin?

7 MR. KELLAHIN: Mr. Examiner, it's my opinion that
8 we're finished with this case, and it's certainly within
9 your direction and control to deny Southwestern's
10 Application without readvertising, based upon the assertion
11 of primary jurisdiction by the BLM. If there's any
12 question about what Mr. Lopez or the BLM has done, I have
13 no reservations about you calling the BLM and asking them.

14 It's my understanding that it's definitive,
15 they've decided this matter, and the case is over with, so
16 we would like you to take it under advisement. But we
17 defer to your judgment, authority and discretion on how you
18 want to manage these cases.

19 (Off the record)

20 EXAMINER STOGNER: Mr. Kellahin, I'm going to
21 continue your case to the June 15th hearing.

22 Now, if for some oddball reason there is an
23 additional need for testimony, I'm not going to pass this
24 thing on to some other Examiner. If I'm here on the 15th,
25 I'll hear it. If I'm not here, then this matter will be

1 continued to June 28th. So bear that in mind.

2 So with that, this case, 12,393, will be
3 continued to the Examiner's hearing scheduled for June
4 15th, and Case Number 12,423, even though it will appear on
5 the June 1st docket, will be readvertised and called on the
6 June 15th docket.

7 With that, is there anything further in these
8 matters?

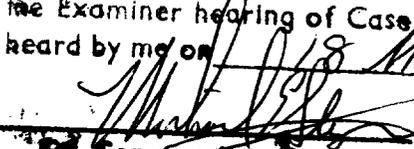
9 MR. KELLAHIN: No, sir.

10 MR. BRUCE: (Shakes head)

11 EXAMINER STOGNER: There being none, then this
12 hearing is concluded.

13 (Thereupon, these proceedings were concluded at
14 1:40 p.m.)

15 * * *

16
17
18 I do hereby certify that the foregoing is
19 a complete record of the proceedings in
20 the Examiner hearing of Case Nos. 12393 and 12423
21 heard by me on 18 May 2000.
22  Examiner
23 Oil Conservation Division
24
25

