

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

**APPLICATION OF ENERQUEST RESOURCES, LLC.
FOR STATUTORY UNITIZATION, LEA COUNTY,
NEW MEXICO.**

CASE NO. 12845

**APPLICATION OF ENERQUEST RESOURCES, LLC.
FOR APPROVAL OF A WATERFLOOD PROJECT
AND QUALIFICATION OF THE PROJECT FOR
THE RECOVERED OIL TAX RATE PURSUANT
TO THE ENHANCED OIL RECOVERY ACT,
LEA COUNTY, NEW MEXICO.**

CASE NO. 12846

02 APR 17 AM 8:20
C-01-12845-12846

**ENERQUEST RESOURCES, LLC.'S
RESPONSE TO KEY FAMILY GROUP'S MOTION TO DISMISS**

The Key Family Group, through its attorney, asks the Division to Dismiss the applications of EnerQuest Resources, L.L.C. ("EnerQuest") for statutory unitization based on its contention that EnerQuest has violated the Statutory Unitization Act. The facts as represented by the Key Family Group are either incomplete or untrue. The standards and procedures which the Group contends apply to this matter are the creation of their counsel and not found in either statute or rule. The Motion to Dismiss must be denied.

RELEVANT FACTS

1. To determine the most prudent course of action for developing the remaining reserves in the San Andres formation in the East Hobbs San Andres Pool, EnerQuest prepared a Unit Waterflood Feasibility Study in the fall of 2000. This study concludes that the most effective way to recover the remaining reserves in this pool is through unitization and waterflood operations. Affidavit of Tim M. Dunn, paragraph 3.

2. Because of the advanced state of depletion of the East Hobbs-San Andres Pool and the fact that substantial drainage was occurring from properties in the proposed unit area to a tract operated by Lynx Operating Co., Inc. (especially the Laney and Laney A leases in which the Key Family Group own working interest), EnerQuest

decided in early 2002 to unitize 920 acres in Lea County, New Mexico and implement a waterflood project on the unitized lands. Affidavit of Tim M. Dunn, paragraph 4.

3. On February 7, 2002, EnerQuest wrote the Key Family Group and others and sought their voluntary participation in the proposed East Hobbs (San Andres) Unit and waterflood project. EnerQuest offered to respond to any questions and to provide information concerning this proposal. Affidavit of Tim M. Dunn, paragraph 5.

4. On February 22 White Star Royalty LLC ("White Star") contacted EnerQuest and advised EnerQuest that it represented the Key Family Group. It requested information on the proposed unit and waterflood project. On that date, EnerQuest provided White Star with the Unit Waterflood Feasibility Study and offered to meet with White Star to discuss the proposed unit and waterflood. Affidavit of Tim M. Dunn, paragraph 6.

5. On February 22, 2002 EnerQuest sent an AFE to the Key Family Group for the proposed waterflood. Affidavit of Tim M. Dunn, paragraph 7.

6. On March 11, 2002 EnerQuest filed the applications which are the subject of the above-referenced cases. Affidavit of Tim M. Dunn, paragraph 8.

7. In mid-March 2002, EnerQuest was contacted by T. Scott Hickman, consulting petroleum engineer, concerning the proposed statutory unitization and waterflood project. Mr. Hickman advised EnerQuest that he represented the Key Family Group. Affidavit of Tim M. Dunn, paragraph 9

8. On March 26, 2002, representatives of EnerQuest met with Mr. Hickman for approximately two hours and reviewed the Unit Waterflood Feasibility Study with him and responded to questions concerning the proposed statutory unitization and waterflood project. EnerQuest provided additional data to Mr. Hickman on that date and offered to meet again to discuss and to consider any other matter, including the proposed unit participation formula, proposed by the Key Family Group. Affidavit of Tim M. Dunn, paragraph 10.

9. At the March 26, 2002 meeting, Mr. Hickman requested additional information on the proposed unit and waterflood project. This information was delivered to Mr. Hickman's office, by EnerQuest. Affidavit of Tim M. Dunn, paragraph 11.

10. The legal counsel for EnerQuest has agreed to request the Division schedule this matter for hearing on a special hearing date after a reasonable time for review of the data and preparation for hearing.

11. Although EnerQuest voluntarily produced all requested information and documents to Mr. Hickman, and although EnerQuest had expressed its willingness to engage in further meetings and/or discussions as might be useful to Mr. Hickman

concerning this project, the only response from the Key Family Group was the Subpoena Duces Tecum Dated April 3, 2002. This subpoena sought much of the data that had already been produced to Mr. Hickman. Additional data has been produced pursuant to this Subpoena. Affidavit of Tim M. Dunn, paragraph 12.

ARGUMENT

Before a unit can be formed pursuant to the Statutory Unitization Act, the operator must make “a good faith effort to secure voluntary unitization within the pool or portion thereof directly affected.” NMSA 1978, Section 70-7-6 (1975). Contrary to the assertions of the Key Family Group, EnerQuest has made a good faith effort to secure their voluntary participation in the proposed East Hobbs (San Andres) Unit.

The Key Family Group announces certain specific requirements that must be met to “demonstrate a good faith effort.” These requirements are not found in any statute or rule. Instead, they have been crafted by the legal for the counsel for the Key Family Group for the purposes of this argument.

The Statutory Unitization Act and the rules of the Division are silent on what is required to meet the test of good faith because what is required is dependant on the particular facts and circumstances surrounding the individual unit. What EnerQuest has done in its good faith effort to obtain the voluntary participation of the Keys Family Group and others is set out above. EnerQuest provided the Keys Family Group with the Unit Agreement, an AFE, the Unit Waterflood Feasibility Study, met with their consulting petroleum engineer to review the study and answer questions, supplied additional data on March 26, 2002, and additional data was supplied thereafter at his request. EnerQuest has also produced additional data pursuant to the Subpoena obtained from the Division. EnerQuest has repeatedly made offers to meet and consider whatever the Keys Family Group would like to propose. This is “a good faith effort to secure voluntary unitization within the pool or portion thereof directly affected.”

This proposal is not like the large units where there are hundreds of interest owners to be contacted. Here, through EnerQuest’s efforts, 81.37% of the working interest has been voluntarily committed to the proposed unit and waterflood project. Only the Keys Family Group who stand to reap substantial benefit from the unit and waterflood and Lynx Operating Co. which is draining reserves from offsetting owners – including the Keys Family Group -- are still in opposition to the plan. Their concerns will not be addressed until there is a hearing on the merits and an order is issued pursuant to the Statutory Unitization Act.

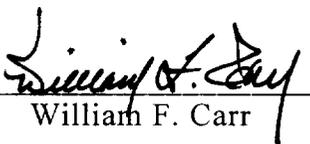
Good faith is a two-way street. This Motion to Dismiss and the Subpoena previously issued on the request of the Keys Family Group are not attempts to gain additional time to review and discuss the merits of the proposals or to obtain more data. They have only one purpose, that is to avoid a prompt resolution of the issues by the Division through frivolous procedural maneuverings

For example, the Keys Family Group lists what it contends is required to demonstrate a good faith effort and states that these things were not done by EnerQuest. The Key Family Group is simply wrong. They say EnerQuest did not prepare a feasibility study and did not provide one to the working interest owners. These statements are not only incorrect, it is inconsistent with other portions of their Motion to Dismiss (In Page 2, paragraph 7 the Keys Family Group admits that it received the Feasibility Study). The Keys Family Group working interest owners were not allowed time to study the feasibility study. In their Motion to Dismiss the Keys forget the study was presented to them on February 22nd and fail to disclose that this study was reviewed with their consulting petroleum engineer by EnerQuest on March 26th and that there have been no questions to EnerQuest from their expert since the March 26th meeting. They overlook the agreement to approach the Division for a special hearing date after there has been a reasonable time to review the data and prepare for hearing.

Perhaps, the Key Family Group should talk to their engineer and lawyer and compare notes. If they would, they would discover that studies and supporting data have been provided by EnerQuest, that meetings have occurred, additional data voluntarily shared, and additional time allowed to evaluate this proposed project. Maybe they would discover what was really going on, they would also find that EnerQuest has made a good faith effort to obtain their voluntary participation in this unit.

EnerQuest requests that the Oil Conservation Division deny the Motion to Dismiss of the Key Family Group and in so doing find that, in the context of this particular proposed unit, EnerQuest has met the good faith standard of the Statutory Unitization Act by (1) preparing and providing to the Key Family Group the Unit Waterflood Feasibility Study, (2) meeting with the representative of the Key Family Group to review the report, answer questions about the proposed unit and waterflood project, (3) voluntarily providing data on the unit and proposed waterflood on at least five occasions, and (4) agreeing to select a special hearing date after a reasonable time has passed to review all data and prepare for the hearing.

Respectfully submitted,
Holland & Hart LLP

By: 
William F. Carr

ATTORNEYS FOR ENERQUEST
RESOURCES, LLC

**STATE OF NEW MEXICO
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LEA COUNTY, NEW MEXICO.**

CASE NO. 12846

AFFIDAVIT OF TIM M. DUNN

STATE OF TEXAS)
)
COUNTY MIDLAND)

Tim M. Dunn, being first duly sworn on oath, states as follows:

1. My name is Tim M. Dunn. I reside in Midland, Texas. I am the Vice President of EnerQuest Resources, L.L.C. ("EnerQuest"). My responsibilities with EnerQuest include supervision of technical activities of this company.

2. I am responsible for supervision of the efforts of EnerQuest to unitize the East Hobbs (San Andres) Unit pursuant to the New Mexico Statutory Unitization Act.

3. To determine the most prudent course of action for developing the remaining reserves in the San Andres formation in the East Hobbs San Andres Pool, in the fall of 2000 EnerQuest prepared a Feasibility Study. This study concludes that the most effective way to recover the remaining reserves in this pool is through unitization and fieldwide waterflood operations.

4. Because of the advanced state of depletion of the East Hobbs-San Andres Pool and the fact that substantial drainage was occurring from properties in the proposed unit area to a tract operated by Lynx Operating Co., Inc. (especially the Laney and Laney A leases in which the Key Family own their working interest), it was decided in early 2002 to proceed with the formation of the proposed unit and implementation of a waterflood project on 920-acres in Lea County, New Mexico.

5. On February 7, 2002, EnerQuest wrote the Key Family Group and others and sought their voluntary participation in the proposed East Hobbs (San Andres) Unit and waterflood project. EnerQuest offered to respond to any questions and to provide information concerning this proposal.

6. On February 22, 2002, the Feasibility Study was sent to White Star Royalty, LLC which advised EnerQuest that it represented the Key Family Group in this area. EnerQuest offered on that date to provide additional information or answer questions concerning the study and our plans to unitize and implement waterflood operations in this pool.

7. On February 22, 2002, EnerQuest sent an AFE to the Key Family Group for the proposed waterflood.

8. The applications in these consolidated cases were filed on March 11, 2002.

9. In mid-March 2002, EnerQuest was contacted by T. Scott Hickman, consulting petroleum Engineer from Midland Texas, concerning the proposed statutory unitization and waterflood project. Mr. Hickman advised EnerQuest that he represented the Key Family Group.

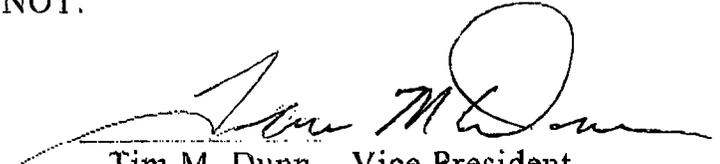
10. Chris Bezner met with Mr. Hickman for approximately two hours on March 26, 2002, reviewed the Feasibility Study with him and responded to questions about the proposed unitization and waterflood project on behalf of EnerQuest. EnerQuest provided additional data to Mr. Hickman on that date and offered to meet again to discuss and to consider any other matter, including the proposed unit participation formula, proposed by the Key Family Group.

11. At the March 26, 2002 meeting, Mr. Hickman requested additional information on the proposed unit and waterflood project. This information was delivered to Mr. Hickman's office in Midland, Texas by EnerQuest.

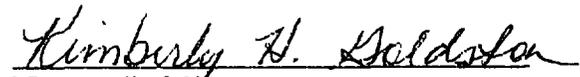
12. Although EnerQuest had voluntarily produced all requested information and documents to Mr. Hickman, and although on March 26, 2002,

EnerQuest had expressed its willingness to engage in further meetings and/or discussions as might be useful to Mr. Hickman concerning this project, the only response from the Key Family Group was the Subpoena Duces Tecum Dated April 3, 2002. This subpoena sought much of the data that had already been produced to Mr. Hickman. Other data has been produced pursuant to this Subpoena.

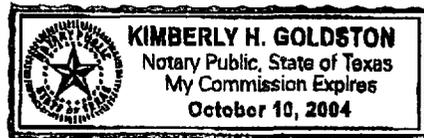
FURTHER AFFIANT SAYETH NOT.


Tim M. Dunn - Vice President

SUBSCRIBED AND SWORN before me on this 16 day of April 2002.


Notary Public

My Commission Expires:
Oct. 10, 2004



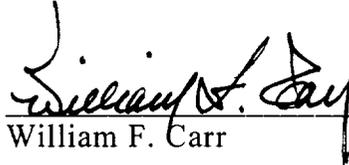
CERTIFICATE OF SERVICE

I certify that on April 17, 2002, I served a copy of the foregoing document to the following by

U.S. Mail, postage prepaid
Hand Delivery
Fax

W. Thomas Kellahin, Esq.
Kellahin and Kellahin
117 North Guadalupe
Santa Fe, New Mexico 87504-2265

Stephen Ross, Esq.
Oil Conservation Division
Energy, Minerals, and Natural
Resources Department
1220 S. Saint Francis Drive
Santa Fe, New Mexico 87504



William F. Carr

KELLAHIN AND KELLAHIN

ATTORNEYS AT LAW

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117 NORTH GUADALUPE

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SANTA FE, NEW MEXICO 87504-2265

TELEPHONE (505) 982-4285
TELEFAX (505) 982-2047

W. THOMAS KELLAHIN*

*NEW MEXICO BOARD OF LEGAL SPECIALIZATION
RECOGNIZED SPECIALIST IN THE AREA OF
NATURAL RESOURCES-OIL AND GAS LAW

JASON KELLAHIN (RETIRED 1991)

April 12, 2002

HAND DELIVERED

Ms. Lori Wrotenbery, Director
Oil Conservation Division
1220 South Saint Francis Drive
Santa Fe, New Mexico 87505

02 APR 12 AM 10:01
CALL CENTER DIVISION

MOTION TO DISMISS

Re: Case 12845
Application of EnerQuest Resources, LLC
for statutory unitization, Lea County, New Mexico

Re: Case 12846
Application of EnerQuest Resources, LLC
for approval of a waterflood project,
Lea County, New Mexico

Dear Ms. Wrotenbery:

On behalf of the Key Family Group, working interest owners in Tract 5 and 6 of EnerQuest proposed Statutory Unit, we request that the reference cases set for hearing of the Examiner's docket for April 18, 2002, be dismissed.

Very truly yours,



W. Thomas Kellahin

cc: David K. Brooks,
Division Attorney
Michael E. Stogner, Examiner
James Bruce, Esq.,
Attorney for Lynx
William F. Carr, Esq.
Attorney for Enerquest Resources, LLC
T. Scott Hickman

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

**IN THE MATTER OF THE APPLICATION
OF ENERQUEST RESOURCES, LLC
FOR STATUTORY UNITIZATION
LEA COUNTY, NEW MEXICO**

CASE NO. 12845

**IN THE MATTER OF THE APPLICATION
OF ENERQUEST RESOURCES, LLC
FOR A WATERFLOOD PROJECT
LEA COUNTY, NEW MEXICO**

CASE NO. 12846

**KEY FAMILY GROUP'S
MOTION TO DISMISS APPLICATION**

Comes now Hugh B. Key, II, Julie Ann Hopkins Trust, Mark Collver Hopkins Trust, Anne Key Davis, Kite Royalty Co., LLC, White Star Royalty, LLC. ("Key Family Group"), by its attorneys, Kellahin and Kellahin, enters its appearance in this case as an interested party in opposition to the applicant, EnerQuest Resources, LLC. ("EnerQuest") and moves the New Mexico Oil Conservation Division ("Division") to dismiss Case 12845 because the applicant has violated NMSA (1978) Section 70-7-6(5) by prematurely instituting an application for Statutory Unitization.

And in support states:

BACKGROUND

(1) Enerquest Resources, LLC is seeking approval of a statutory unit and an waterflood project for a certain unit area. **See Exhibit "A"**

(2) The Key Family Group represents approximately 20% and 27.6% of the working interest owners plus a royalty interest in Tracts 5 and 6 on Exhibit A.

(3) On February 26, 2002, EnerQuest filed an application for Statutory Unitization with the Division requesting a hearing on March 21, 2002 and alleging that:

"(8)(e) EnerQuest Resources, LLC, as operator, has made a good faith effort to secure voluntary unitization within the portion of the East Hobbs-San Andres Pool affected by this application."

(4) Nineteen days before filing its application, on February 7, 2001, EnerQuest's commence its only effort to obtain voluntary agreement from the Key Family Group by sending a letter asking them to ratified the unit agreement and unit operating agreement. **See Exhibit "B"**

(5) Four days before filing its application, on February 22, 2002, EnerQuest send the Key Family Group an AFE and advised that EnerQuest had altered its plan. **See Exhibit "C"**

(6) Enerquest Resources did not provide any data to justify this proposed change of plans or change in cost.

(7) In the same mailing, EnerQuest enclosed their waterflood feasibility study that the Key Family representative has requested, which was received by the Key Family Group about the same time as the application was filed with the Division.

(8) At no time prior to filing its application did EnerQuest voluntarily provide to the Key Family Group, as working interest owners, the necessary data for the original project or revised project to:

(a) demonstrate the secondary recovery potential of the project;

(b) demonstrate the appropriation of the proposed unit boundary;

(c) show the basis for participation parameters;

(d) justification for EnerQuest's participation formula;

(e) justification for capital requirements;

(f) provide any reservoir, petroleum engineering data geological maps, economic evaluations;

(g) any means to evaluate EnerQuest project;

(9) At no time prior to filing its application did EnerQuest call a working interest owners meeting.

ARGUMENT

Contrary to the custom and practice before the Division and in violation of NMSA (1979) Section 70-7-6(5), EnerQuest has instituted action to obtain a Statutory Unitization Order without first making a "good faith" effort to form a voluntary unit. NMSA (1979) Section 70-2-6(5) is very specific in its requirement that as a "matter to be found by the Division precedent to issuance of unitization order" the applicant must demonstrate:

"(5) that the operator has made a good faith effort to secure voluntary unitization within the pool or the portion thereof directly affected;"

As the Division knows for its own experience with other statutory unitization case, the applicant does the following to demonstrate a good faith effort:

- (1) prepare a feasibility study
- (2) provide the study to the proposed working interest owner
- (3) after provide time to review the study, it calls a meeting of the working interest owners to discuss the project and if necessary form a working interest owners "technical committee" to develop participation parameters

(4) the working interest owners then meet and discuss, revise and adopt the technical committee's report and then discuss and debate the participation parameters and adopt a formula.

EnerQuest did not do any of the foregoing. But instead, filed its application asking the Division to exercise its authority and compel involuntary participation. The Division can only exercised this authority in those instances where the parties have not agreed to voluntarily unit their interests for a specifically proposed project. In this case, the Key Family Group was never provided information about the project before EnerQuest filed its application.

It is impossible to have exhausted a good faith effort to reach a voluntarily agreement in less than 19 days after sending notice of its intention to form a unit. EnerQuest made no effort to inform the working interest owners about the project. EnerQuest's action simply ignores the requirements of NMSA (1979) Section 70-2-6(5) and will encourage others to use statutory unitization as a negotiating weapon rather than as a remedy of last resort.

EnerQuest's application must be dismissed. Unless this application is dismissed the Division will be establishing a precedent which will allow applicants to avoid complying with NMSA (1979) Section 70-2-6(5).

WHEREFORE the Key Family Group requests that the Division Hearing Examiner grant this motion and dismiss Oil Conservation Division Case 12845.

Respectfully submitted,



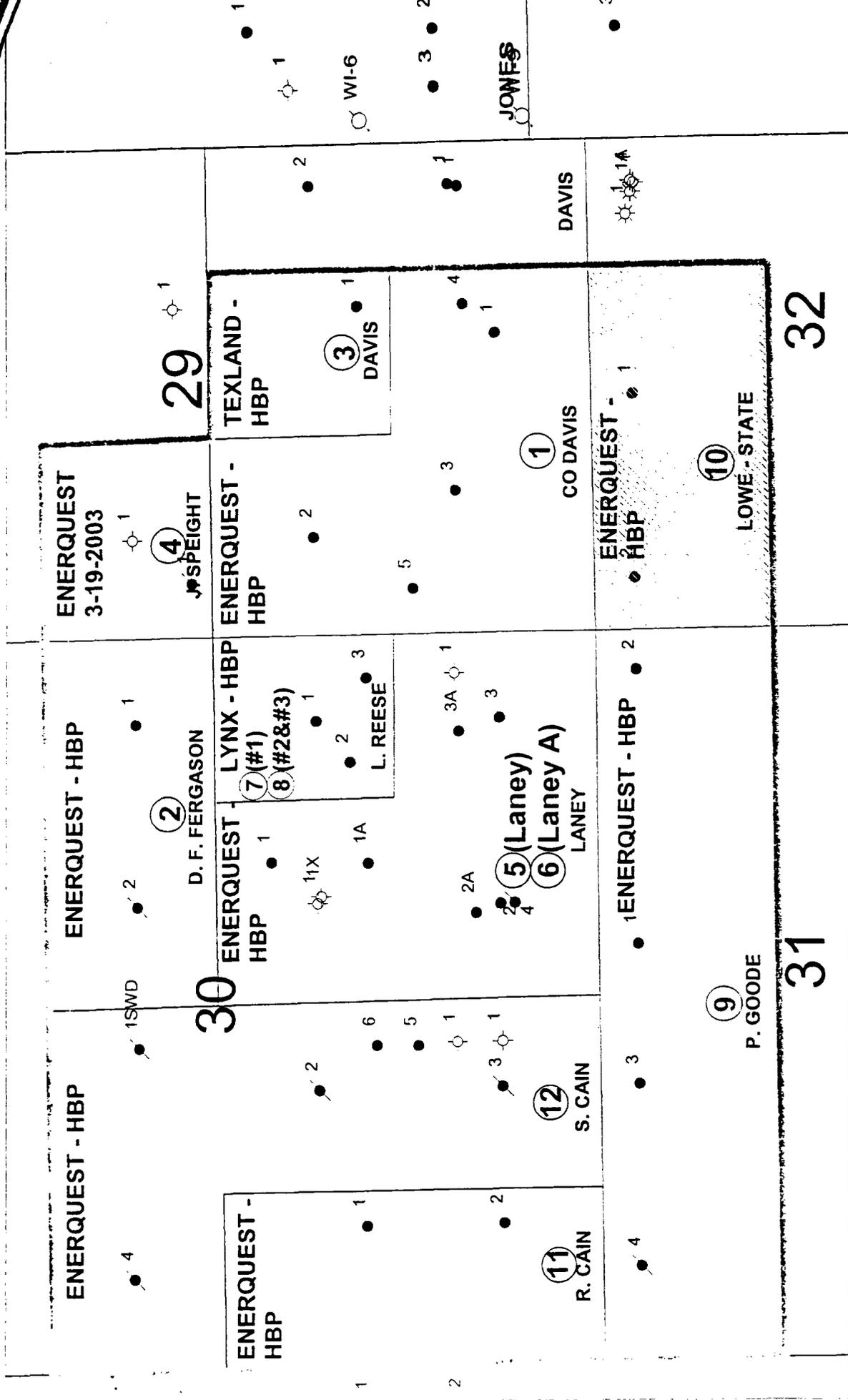
W. Thomas Kellahin
P. O. Box 2265
Santa Fe, New Mexico 87504

CERTIFICATE OF SERVICE

I certify that a copy of the foregoing pleading was transmitted by facsimile this 12th day of April, 2002 to James Bruce, attorney for Lynx et al, and to William F. Carr, attorney for EnerQuest Resources, LLC



W. Thomas Kellahin



<input type="checkbox"/>	State Lands 80 acres (8.7%)
<input type="checkbox"/>	Patented Lands 840 acres (91.3%)

3 Tract Number Unit Outline



ENERQUEST RESOURCES, LLC

EAST HOBBS (SAN ANDRES) UNIT
 920 ACRES
 Lea County, New Mexico
 T18S - R39E

Date: 1 Jan, 2003
 Scale: 1"=1000'
 C.I.:

Project: Geologist:
 Area: Geophysicist:
 Prospect: Engineer:

32

31

February 7, 2002

To: Working Interest Owners

Re: East Hobbs (San Andres) Unit
Lea County, New Mexico

Ladies and Gentlemen:

EnerQuest Oil & Gas, Ltd. hereby proposes the formation of the East Hobbs (San Andres) unit to unitize the San Andres formation for the purpose of secondary operations. The proposed unit consists of 920 acres and covers parts of Section 29, 30, 31 and 32, Township 18 South, Range 39 East, Lea County, New Mexico. I have enclosed for your review and approval a unit agreement, unit operating agreement and ratification governing the implementation and development of the East Hobbs Unit.

Please review the agreements and if everything appears correct, execute the ratification in the space provided and return to me at the letterhead address. EnerQuest plans to have a hearing with the New Mexico Oil Conservation Division on this matter on March 7, 2002, therefore your prompt attention would be appreciated. Should you have any questions or require any additional information, please feel free to contact me at (915)685-3116.

Very truly yours,


M. Craig Clark
LandmanMCC/s
Enclosure

ENERQUEST

ENERQUEST OIL & GAS, LTD.

February 22, 2002

White Star Royalty Co
P.O. Box 18693
Oklahoma City, OK 73154

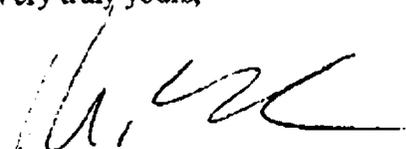
Re: East Hobbs Unit
Lea County, New Mexico

Gentlemen:

Pursuant to my telephone conversation with Mike Carr, enclosed please find a Phase I cost estimate for the above captioned unit as well as a feasibility report for the project. Please be advised that we have changed the development plans from the initial feasibility report as reflected on the reduced Phase I cost estimate.

Should you have any further questions, please let me know.

Very truly yours,


M. Craig Clark

MCC/s
Enclosure

