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 GREAT WESTERN DRILLING COMPANY FOR COMPULSORY POOLING, LEA COUNTY, NEW MEXICO	)	CASE NOS. 12,956
APPLICATION OF DAVID H. ARRINGTON OIL AND GAS, INC., FOR COMPULSORY POOLING, LEA COUNTY, NEW MEXICO	)	and 12,942
	)	(Consolidated)

REPORTER'S TRANSCRIPT OF PROCEEDINGS

EXAMINER HEARING

BEFORE: DAVID K. BROOKS, Hearing Examiner

November 14th, 2002

Santa Fe, New Mexico

This matter came on for hearing before the New Mexico Oil Conservation Division, DAVID K. BROOKS, Hearing Examiner, on Thursday, November 14th, 2002, at the New Mexico Energy, Minerals and Natural Resources Department, 1220 South Saint Francis Drive, Room 102, Santa Fe, New Mexico, Steven T. Brenner, Certified Court Reporter No. 7 for the State of New Mexico.

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I N D E X

November 14th, 2002
Examiner Hearing
CASE NOS. 12,956 and 12,942 (Consolidated)

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* * *

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* * *

WHEREUPON, the following proceedings were had at 11:00 a.m.:

EXAMINER BROOKS: Okay, we'll call the hearing back to order.

At this time we'll call Case Number 12,956, Application of Great Western Drilling Company for compulsory pooling, Lea County, New Mexico.

Call for appearances.

MR. OWEN: Paul Owen of the Santa Fe law firm of Montgomery and Andrews, appearing on behalf of Great Western Drilling Company.

MR. FELDEWERT: May it please the Examiner of the law firm of Holland and Hart. I'm here on behalf of David H. Arrington Oil and Gas, Inc., who is the Applicant in Case 12,942.

EXAMINER BROOKS: Okay. Now, do you all have any witnesses?

MR. OWEN: Yes, Mr. Examiner, I have two witnesses in this matter.

And I -- moving on the tail of Mr. Feldewert, I do point out that it's my understanding that at the conclusion of the October 10th, 2002, hearing you consolidated Case Number 12,942 with this case and continued it till today.

EXAMINER BROOKS: I don't recall, and I don't have the transcript here in front of me, so -- as to whether I actually did consolidate it or not.

My intention was to consolidate it and issue a single order, since as I understand it the granting of either Application would preclude the granting of the other.

And so if I have not done so, at this time we will consolidate Cases Numbers 12,942 and 12,956, and it's contemplate that a single order will be entered disposing of both cases.

I believe that the evidentiary presentation in 12,942 was made at the previous hearing; is that correct, Mr. Feldewert?

MR. FELDEWERT: That's correct, Mr. Examiner. I do not have a witness here today, and I don't know whether we're going to have any evidentiary presentation here today.

EXAMINER BROOKS: Very good. Mr. Owen, would you have your witnesses stand to be sworn, please?

(Thereupon, the witnesses were sworn.)

EXAMINER BROOKS: Okay, as the Applicant in Case Number 12,956 you may proceed, Mr. Owen.

MR. OWEN: Thank you, Mr. Examiner. I call Mr. Mike Heathington.

MICHAEL S. HEATHINGTON,

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

DIRECT EXAMINATION

BY MR. OWEN:

Q. Would you please tell us your full name and where you live?

A. My name is Mike Heathington. I reside in Midland, Texas.

Q. Who do you work for?

A. I work for Great Western Drilling Company.

Q. And what do you do for Great Western?

A. I'm the land manager for Great Western.

Q. Have you previously testified before this Division?

A. Yes, I have.

Q. At the time of that testimony were your credentials as a petroleum landman accepted and made a matter of record?

A. Yes, I believe they were.

Q. Are you familiar with the Application filed in this case?

A. Yes.

Q. Are you familiar with the lands in the subject area?

A. Yes, I am.

MR. OWEN: Mr. Examiner, are the witness's qualifications acceptable?

EXAMINER BROOKS: The witness is qualified.

Q. (By Mr. Owen) Mr. Heathington, are you aware that David H. Arrington Oil and Gas, Inc., has sought to have the same lands pooled and dedicated to a similar well with Arrington to be named as operator?

A. Yes, I am.

Q. Are you aware that Arrington's Application has been assigned Case Number 12,942 and was heard by the Division on October 10th, 2002?

A. Yes.

Q. Were you present at the time of that testimony?

A. Yes, I was.

Q. Since that hearing, have you reviewed the exhibits offered by Arrington in the October 10th hearing?

A. Yes.

Q. Have you also reviewed the transcript from that hearing?

A. Yes.

Q. Does Great Western seek a different well location than that discussed by Arrington in Case Number 12,942 at the October 10th hearing?

A. No, we're in agreement with the location, but we

do seek a different well name.

Q. Okay.

A. We'd like to call it the Lovington Federal Number 1.

Q. All right. And does Great Western propose to drill to a different formation or horizon than that proposed by Arrington?

A. No, we do not.

Q. Okay. Are you prepared to explain why Great Western should be designated the operator of the subject well, instead of Arrington?

A. Yes.

Q. All right. Why don't you give us a brief statement about what Great Western seeks with this Application?

A. Great Western seeks an order pooling all of the mineral interest underlying the east half of the north two-thirds of Section 1 in Township 16 South, Range 34 East, of Lea County, New Mexico, in the following manner:

We seek to pool all formations and/or pools developed on a 320-acre spacing within that vertical extent, including but not limited to the Undesignated Townsend-Morrow Gas Pool;

We also seek all formations developed on 160-acre spacing underlying the northeast quarter of said Section 1;

All formations developed on 80-acre spacing underlying the east half, northeast quarter;

And all formations developed on 40-acre spacing underlying the northeast northeast quarter.

Such spacing and proration units are to be dedicated to Great Western's proposed Lovington Federal Number 1 well, to be drilled at a standard location in the northeast quarter of Section 1.

Q. All right. Why don't we go ahead and turn to Great Western Exhibit Number 1? Could you please explain that for the Examiner?

A. What that exhibit is, is an outline of the proposed 328-acre proration unit that we seek to pool here. This section is an irregular section that is composed of specific eight lots, described more specifically as Lots 1, 2, 7, 8, 10, 15 and 16, or it could be described -- in some of our files we have a description of the east half of the north two-thirds of Section 1, Township 16 South, Range 34 East. It encompasses 328.34 total acres. It is a federal oil and gas lease.

Q. And does this exhibit indicate the proposed well location?

A. Yes, it does. It also shows the -- the dot, that we would like to drill.

Q. Is that the same well location that was discussed

by Arrington in the October 10th, 2002, hearing?

A. Yes, it is. We've since had our production foreman basically go out and look at that, and we think it is acceptable for geological reasons and surface reasons.

Q. Okay, what's the primary objective of the proposed well?

A. It's a dual primary objective of the Atoka and the Morrow.

Q. Is that in the Undesignated Townsend-Morrow Gas Pool?

A. Yes, it is.

Q. Okay. Let's turn to Great Western Exhibit Number 2. Could you please review that for the Examiner?

A. This is an exhibit that shows the represented ownership of the parties. This is also a part of our joint operating agreement that we have prepared and sent to all parties. It shows, like I said, the represented ownership to be Great Western, 32.238 percent; Davoil, Inc., 17.762 percent; and David H. Arrington Oil and Gas, 50 percent. We would like to discuss this ownership in a little more detail at a later time in this testimony?

Q. Do we, in fact, have a couple of assignments dealing with Arrington that we're going to discuss in a little bit?

A. Yes.

Q. All right. And what percentage of the acreage is voluntarily committed to the well, naming -- with Great Western as the operator?

A. We have voluntary commitments from 50 percent of this proration unit.

Q. How many owners does that represent?

A. That represents two out of the three owners involved in this proposed proration unit?

Q. Would that be Davoil and Great Western?

A. That is Davoil and Great Western Drilling Company.

Q. Okay. How is Davoil committed, and how is Great Western committed to Great Western's proposal?

A. Great Western, like I said, formally proposed a proposed joint operating agreement to all parties, and we have received the signatory joinder, voluntary joinder, of Davoil, Inc., to our proposed AFE and to our joint operating agreement.

Q. Now, is that proposed joint operating agreement comprising Great Western Exhibit Number 3?

A. Yes, I believe it is.

Q. Why don't you review that exhibit for the Examiner, please? The JOA?

A. The JOA? Well, it's a Model Form 610, 1989 model form joint operating agreement. It covers the lands we've

discussed, and basically it's been -- You know, it basically does not have a lot of extra provisions at all to the model form. We like to keep it pretty simple of what AAPL has recommended. It covers all matters of operations and liabilities and billings of the parties to this proposed operation.

Q. Now, in the back couple pages of that exhibit are some signature pages. What do those signature pages indicate?

A. Basically that Davoil, Inc., has voluntarily joined in this proposed joint operating agreement.

Q. Okay. Does that JOA treat loss of title?

A. Yes, it does.

Q. Does it treat subsequent operations?

A. Yes, it does.

Q. Does it treat removal of the operator?

A. It treats that issue.

Q. Does it treat liabilities between the parties to the JOA?

A. Yes, it does.

Q. Does it treat reworking and plugging back of wells?

A. It addresses that.

Q. Does it treat termination of the operations on the land?

A. Yes, it does.
Q. Does it treat joint accounting?
A. It treats all joint interest accounting matters.
Q. Okay. Have you seen any compulsory pooling orders from this Division? Are you familiar with the typical compulsory pooling order from this Division?
A. Yes, I am.
Q. Do those orders treat subsequent operations?
A. Not to my knowledge.
Q. Do they treat joint accounting?
A. No, I don't believe they do.
Q. Do they treat liabilities between the parties?
A. I don't believe they do, no.
Q. Do they treat failure of title?
A. No.
Q. Do they treat plugging back and reworking wells?
A. Not to my knowledge.
Q. Okay. Let's turn to Great Western Exhibit Number 4. Can you please tell us what that exhibit is? Mr. Heathington, it might help if you take the butterfly clip off.
A. Okay. Lots of paper here. Yes, Exhibit Number 4 is our AFE to this proposed well.
Q. What well location were you proposing with this AFE?

A. This AFE was the original proposal that we made prior to discovering that we had some surface -- prior to it being discovered that we had some surface issues out here. We originally proposed a 1200 feet from the north line and 1335 from the east line of Section 1 location for this well, and that was done in September sometime.

Q. Was that September 30th, 2002?

A. I believe it was a little earlier than that. Yes, that's correct, September 30th.

Q. That's when you sent it to the other interest owners?

A. That's when all interest owners received this well proposal.

Q. Including Davoil and Arrington?

A. Yes.

Q. Okay. Then let's turn to Great Western Exhibit Number 5. Can you tell me what that is?

A. That is an amended AFE that was prepared after discovering the surface issues for the first location, and it shows a revised location of 1200 feet from the north line and 1665 from the east line.

Q. So you moved the proposed well location 300 feet to the west?

A. Yes, to accommodate features on the surface that probably would be expensive to build a location on.

Q. When did you submit this AFE to the other interest owners in the well?

A. This was resubmitted as an amended AFE on October 21st, 2002.

Q. October 21st?

A. Yes, October 21st.

Q. Okay. Why did you submit this second AFE?

A. Well, basically anytime you have a revised proposal, when there's a change of location a revised AFE needs to be proposed showing the correct well location.

Q. Okay. Let's turn to Great Western Exhibit Number 6. Can you tell me what that is?

A. That is David Arrington Oil and Gas's AFE for the proposed well.

Q. Okay. What well location does this AFE indicate?

A. It shows the 1200 feet from the north line and 1665 from the east line of Section 1 well location.

Q. Is that the location which Arrington requested during the October 10th, 2002, hearing?

A. Yes, it is.

Q. Was this AFE with the 1665 location ever sent to you?

A. This AFE has never been submitted to Great Western, or Davoil to my knowledge.

Q. All right. Does Exhibit Number 5, Great

Western's amended AFE, and Great Western's Exhibit Number 4, the original AFE, do those AFEs reflect Great Western's estimate of overhead and administrative costs while drilling and operating the well?

A. Those are reflected in our joint operating agreement.

Q. In the JOA?

A. For the most part, yes.

Q. And was that JOA submitted to both Davoil and Arrington?

A. Yes.

Q. What are the proposed estimated overhead and administrative costs?

A. We seek a drilling well overhead cost of $6000 per month and a producing well overhead rate of $600 per month.

Q. Have you ever received a proposed JOA from Arrington?

A. No, we haven't.

Q. Have you ever received any proposed overhead and administrative costs from Arrington?

A. None that I'm aware of.

Q. Okay. Are the costs that Great Western proposes in its JOA in line with what's being charged by other operators in this area?

A. Yes, I believe they are.

Q. Do you recommend that those figures be incorporated into any order that results from this hearing?

A. Yes, I would.

Q. Looking back at Exhibit Number 5, what's the total for -- Great Western's total for a completed well?

A. A total completed well cost we estimate to be $1,503,200,.

Q. What's the estimated dryhole cost?

A. The estimated dryhole cost is $950,700.

Q. And the estimated completion cost?

A. The completed well cost is $552,500.

Q. And that results in the $1.5-million figure you've indicated?

A. Yes, it does.

Q. Are those costs in line with what's been charged by other operators in the area for similar wells?

A. We believe them to be very competitive estimated cost.

Q. Are they in line with the AFE and the figures reflected on the AFE that Arrington proposed during the October 10th, 2002, hearing?

A. They're in line. The comparison is, our estimated dryhole cost is $60,000 less than the AFE proposed by Arrington, with his completion-cost estimate

being $26,000 less than our estimated completion cost.

Q. Okay, what's the -- Is there a significant difference between the completed well costs?

A. The total completed well cost, the estimated difference is $34,000.

Q. Who proposes to charge more?

A. Arrington's estimate is higher.

Q. Do you consider that a significant difference in light of the $1.5 million?

A. In a well like this, no, I do not consider it a significant difference.

Q. Okay. Now, I want you to -- After talking about Exhibit Number 6, Arrington's AFE, I want to ask you about Great Western's involvement with any other wells operated by Arrington. Has Great Western ever been involved in any other wells operated by Arrington?

A. We've been involved with four other wells as a nonoperator where Arrington Oil and Gas has been the operator.

Q. Okay. In those wells, how did Arrington's actual expenditures compare to their estimated expenditures, as reflected by their AFEs in those wells?

A. The average -- I'm going to give the specifics here, but basically we were in four wells. One of them was called the Beet Head Hare's Ear Number 41. Arrington Oil

and Gas was two percent under its estimated AFE cost. In the Beet Head Emerger Number 65 well he was 23 percent over his AFE cost. In the Beet Head Scud Number 53 well he was 109 percent over his AFE estimated cost. In the Beet Head Stone Fly 41 well he was 185 percent over his estimated AFE cost. And these were shallow, 6000-foot, pretty much bread-and-butter wells on the eastern shelf of the Permian Basin.

Q. In light of that, how accurate do you think that Arrington's estimated well costs as reflected on their AFE are?

A. Based on our past experience, we have to really wonder.

Q. Okay. Now, the difference between Great Western's Exhibit Number 4 and Great Western's Exhibit Number 5 has to do with the moving of the well location; is that right?

A. Yes, that's right.

Q. Okay. I think you indicated you were present during the October 10th hearing; is that correct?

A. Yes.

Q. Did you hear Mr. Dale Douglas represent that Arrington had reached agreement with the surface owner for this well?

A. I don't recall whether he did or not. I don't

really recall that specifically. There was testimony about them staking the well, and possibly talking to the surface owner, I believe, yes.

Q. Okay. Do you remember whether or not counsel for Mr. Arrington represented that agreement had been reached with the surface owner?

A. It could be possible, I don't remember specifically.

Q. Have you spoken with the surface owner?

A. We have had contact with the surface owner. To our knowledge, as of about two weeks ago, there's been no contact from Arrington regarding obtaining access to the location and settling damages. He had not -- We do know damages have not been settled.

Q. Did you discuss damage settlement, surface damage settlement, in the event that Great Western is named as operator?

A. Yes, we have. We entered into tentative negotiations subject to the outcome of this order to obtain an agreement to enter the property and get this well drilled.

Q. Did that surface owner indicate that he would not enter into an agreement with Great Western?

A. No, not at all.

Q. Have you obtained a permit from the BLM to drill

this well?

A. No, we haven't. We understand on October 21st Arrington Oil and Gas did receive a federal permit on this well.

Q. Are you familiar with the process required for transferring that permit to Great Western as the operator?

A. As I understand, that's done by some type of sundry notice, pretty simple procedure.

Q. Is Great Western going to be required to submit a separate application for a permit?

A. Not to my knowledge, no.

Q. Okay, and is Great Western going to be required to conduct an archaeological survey?

A. As I understand it, that will not have to be done again.

Q. Okay, let's move on a little bit. I want to take a look at Arrington Exhibit -- Well, actually, let's talk a little bit about your negotiations with the other parties in the case. Can you summarize for me the efforts made to obtain the joinder of all the working interest owners in this proposed spacing unit?

A. Well, as we have stated, we obtained voluntary joiner of two of the three owners in this proposed proration unit. We've also attempted as of last Friday -- we did put a call in to Dale Douglas of Arrington Oil and

Gas in an attempt to settle the issues involved in these Applications, and we propose a couple of different ways that we might go forward without continuing this process here, which were rejected by Arrington Oil and Gas.

Q. Who advanced those proposals in an effort to get voluntary joinder?

A. Those were advanced by Great Western's management.

Q. Has Arrington contacted you to try to get joinder, get Great Western's joinder in this well?

A. No.

Q. Now, Arrington did propose the well to Great Western; is that right?

A. Yes.

Q. They proposed that through an AFE?

A. Yes.

Q. Have they proposed it any other way?

A. No.

Q. They didn't give you a JOA, did they?

A. We have not seen a proposed joint operating agreement.

Q. Okay.

A. We have not seen an actual well location.

Q. In your opinion, have you made a good-faith effort to obtain the voluntary joinder of David H.

Arrington Oil and Gas, Inc.?

A. I believe we have.

Q. Okay. And what efforts has Arrington made to obtain Great Western's joinder?

A. None to my knowledge.

Q. Well, let's look at Exhibit Number 7, Great Western's Exhibit Number 7. What is that exhibit?

A. Well, that's where he did send out an AFE showing the original location, that was amended thereafter. That's where he originally proposed a well, by AFE only.

Q. What was amended?

A. The actual drilling location has been moved.

Q. Has Arrington proposed the -- moved the new location?

A. We have not seen the amended AFE proposals, no.

Q. Okay. Have there been any other contacts from Arrington to Great Western with regard to this case?

A. No.

Q. All right. Now, you indicated at the outset of this case that we had some assignments you wanted to talk about. I want you to take a look at Great Western Exhibit Number 8. Can you tell me what that is?

A. Okay, that is a term assignment from Hunt Oil Company covering about -- roughly 35 percent of the operating rights on this federal lease, that was made to

Dale Douglas in Midland, Texas.

Q. What's the date of that assignment?

A. I think it was effective March 1. March 1 of 2001.

Q. What's Mr. Douglas's association with David H. Arrington Oil and Gas, Inc.?

A. I think he is their land consultant.

Q. Okay. All right, now I want you to -- Does this lease cover the acreage that's involved in this case?

A. Yes, it does.

Q. Or this term assignment, pardon me?

A. Yes, it does. It covers an interest in this acreage, yes.

Q. Okay, I want you to turn to Great Western Exhibit Number 8a. Can you tell me what that exhibit is?

A. That is an instrument where Mr. Douglas assigned to David H. Arrington Oil and Gas all of his right, title and interest acquired in the term assignment we just mentioned.

Q. When was that signed?

A. That was signed, according to the notary, on the 4th of October, 2002. It's our understanding it was filed in the county records late yesterday afternoon.

Q. In fact, on the second page of that exhibit is there a recording stamp?

A. Yes, there is.

Q. And what does that recording stamp --

A. It was filed on November 13th, 2002.

Q. Okay. Does this assignment assign the same interests that were covered in Great Western Exhibit Number 8?

A. Yes.

Q. Okay. I want you to turn to Great Western Exhibit Number 9. Can you tell me what that is?

A. That is a letter in favor of David H. Arrington Oil and Gas, a farmout-agreement letter, from Tom Brown, Inc., who owns 14 percent, approximately 14 percent of the operating rights on the federal lease covered by this Application.

Q. What's the date of that letter?

A. September 27th, 2002.

Q. And what is -- Does that letter agreement and the farmout cover any of the acreage involved in this case?

A. Yes, it does, roughly 14 percent.

Q. All right. I want you to turn to Great Western Exhibit Number 9a. Can you tell me what that is?

A. That is the Application of David H. Arrington Oil and Gas for pooling of the interest in this acreage we're talking about.

Q. Okay. And on the upper right-hand corner there's

a sideways stamp, a file stamp. Can you tell me what the date of that stamp is?

A. Yes, that -- Does that say September 18th?

Q. I don't know, that's why I'm asking.

A. I believe it says September 18th, 2002, when that was filed.

Q. All right. On the bottom of that first page there's a statement with a number 1. Can you read that statement please?

A. Number 1 represents -- it says "Arrington is a working interest owner in the E/2 of irregular Section 1 and has the right to drill thereon."

Q. When did Arrington acquire its interests from Dale Douglas?

A. Apparently October 4th, 2002, and it was recorded of record in Lea County on November 13th, 2002.

Q. When did Arrington acquire its interests from Tom Brown, Inc.?

A. According to this paperwork, on September 27th, 2002.

Q. At the time that this Application was filed, did Arrington own any interest in this acreage?

A. Not from the paperwork of record and what's been furnished.

Q. Has Great Western undertaken a search of the Lea

County records?

A. Yes, we have.

Q. Has Great Western -- As a result of that search, have any other assignments or conveyances into David H. Arrington Oil and Gas of this acreage been uncovered?

A. There's actually nothing of record, other than the assignment that was filed yesterday afternoon.

Q. All right. Mr. Heathington, is Great Western Exhibit Number 10 an affidavit from myself indicating that notice of this hearing was given to David H. Arrington Oil and Gas, Inc.?

A. Yes, it is.

Q. Does Great Western seek to be designated operator of the proposed well?

A. Yes, we do.

Q. All right. Now I want to ask you the million-dollar question in this case, Mr. Heathington. Why does Great Western object to Arrington's operation of this well?

A. Well, we have previously discussed our direct experience with Arrington Oil and Gas as an operator in King County, Texas, and based on that experience and the actual cost overruns and other operational factors that we have experienced, Great Western has a significant concern whether or no Arrington Oil and Gas has the personnel on staff and the ability to properly drill, complete and

produce a well of this magnitude.

And based on the experience on these four wells in King County, we believe that Arrington Oil and Gas creates significant unnecessary joint account expense by utilizing expensive consultants for numerous engineering, geological and land functions that most operators cover under the normal overhead provisions of a joint operating agreement. They have the in-house staff not to bill these people out directly as a direct cost to the joint account.

Q. You mean most other operators have those staff?

A. Most operators with any kind of realistic staff do not bill those kind of fees to the joint account.

Q. Does Arrington?

A. Arrington has, yes.

Q. Okay.

A. He has extensively.

We believe that Arrington has failed to comply with a joint operating agreement in King County by not allowing Great Western Drilling Company access to that joint account when we had questions about his cost overruns and extensive use of consultants. In fact, we were forced in our great reluctance to file a lawsuit, just to try to complete a normal joint interest audit of those particular wells. And even after the lawsuit was filed, Great Western was continued -- was still not allowed enough access to the

records of those wells to complete an audit of those wells.

Q. Is there any right of access under the joint operating agreement?

A. You bet, I mean, there's express -- I mean, that's just a normal thing to -- you know, normally to be able to audit the joint account.

Q. Does Great Western view Arrington's refusal to allow access to the joint accounts as a failure to comply with the joint operating agreement?

A. Without question.

Q. Are there any other instances of which you're aware that Arrington has failed to comply with a joint operating agreement?

A. Yes, sir, there is. I mean, there were a couple of other significant instances in the King County process where the operating agreement was not complied with, in our opinion. A well was plugged, that we had an interest in as a nonoperator, without any kind of notification. It was a producing well that was just plugged without notification to us, to allow us, you know, to either take the well over or continue producing it.

Q. Was there notification required in the joint operating agreement?

A. Yes, there is. We also think Arrington failed to comply with the operating agreement. We had a special in

this particular deal that anytime cost overruns exceeded 20 percent of a proposed completion or drilling operation, he was required to notify the nonoperators, and we were entitled to an additional election at that point of whether or not we wanted to continue with that particular operation. When only two of the four wells were drilled, he was definitely over -- 20 percent over the cap that was spelled out in the operating agreement. We received no notice, we just continued ahead with those things and spent a lot of money that we may not have elected to do.

We have serious reservations about the in-house staff and his willingness to comply with the terms of the joint operating agreement we had in that case. We do know that he can use consultants extensively and deny access to the joint account. But other than that, we do have reservations about him operating.

Q. You've indicated some things that Great Western thinks are in noncompliance with the joint operating agreement. Do those factors -- or those facts, have anything to do with your opinion about whether Arrington can prudently operate the acreage in this case?

A. Based on our direct experience of them, they certainly have something to do with that.

Q. And what is your opinion about whether Arrington will be a prudent operator of the acreage in this case?

A. We think there's some real questions there because of the limited staff that he has, limited field office staff, and the excessive use of consultants in drilling wells.

Q. Do you think that Arrington will be a prudent operator of the acreage in this case?

A. In this case, we think Great Western would be the more appropriate operator.

Q. How long have you been in the oil and gas business, Mr. Heathington?

A. Twenty years.

Q. How many wells have you been involved in, indirectly or directly, through your employer.

A. Probably close to a thousand.

Q. In the course of that experience have you developed an understanding of what a prudent operator is?

A. I believe I have.

Q. In your opinion, is Arrington a prudent operator?

A. Based on our experience, we don't believe him to be so.

Q. Why should Great Western be designated the operator instead of Arrington?

A. Well, Great Western is an experienced and capable operator of a well -- To me, we are an experienced and capable operator of a well in this trend or any other trend

that might be involved in the Permian Basin operations. Two out of the three interest owners in this particular proration unit desire Great Western to operate. Great Western has drilled one of the original discovery wells in the Townsend trend in the 1970s. Great Western has a field office in Lovington --

Q. Let me ask you about that well in the 1970s. Is that well still in operation?

A. That well is still producing, very prolific well.

Q. Is it from the same horizon as the proposed well in this case?

A. It is from one of the primary objectives, yes.

Q. Is Great Western still the operator of that well?

A. Yes, we are.

Q. Has Great Western been the operator continuously since the drilling of that well?

A. Yes, we have.

Q. Have you ever had any complaints from the other interest owners in that well?

A. No, sir, we have not.

Q. Have you ever been accused of imprudent operations by the other interest owners in that well?

A. No, we have not.

Q. All right, I interrupted you. You were talking about your field personnel, I believe?

A. I think it's a significant point in considering which party needs to operate this. Great Western does have a field office located 10 miles from this proposed location. We have a drilling superintendent that would be supervising all operations of a well, if we are designated the operator, that has over 30 years' experience in drilling wells in the Permian Basin. We have production foremen out of that Lovington Office, so we would not have to use consultants in the operation of this well.

Q. Let me ask you about that. You indicated that Arrington bills consultants and other operators don't. What effect does that have on the operation of the well?

A. Well, I don't want to say that other operators don't ever use consultants. Consultants are used. It's the -- Most companies with reasonable staffs utilize their engineers and their geologists at a considerably reduced cost, typically, than, you know, consultants, consultants that have to be used for every function. And when you use consultants not only in the drilling and completion of a well but in the operation -- the production of a well, you can considerably run up the cost of the joint account.

Q. In your opinion, does that have any reflection on the accuracy of Arrington's estimated cost for drilling and producing the well?

A. It could, yes.

Q. What effect would that be?

A. It could increase it.

Q. Okay. I interrupted you when you were talking about these outside consultants.

A. Well, what I was wanting to add, besides our -- you know, like I said, to my knowledge Arrington Oil and Gas has no such field office located this close to the property.

Great Western also has the in-house engineering expertise, without having to use some of these consultants, whereas Arrington, we believe, would make extensive use of engineering, geological and land consultants. We certainly would provide our partners access to any joint account questions that they may have concerning any of the bills or the operations that we may do on this particular well. We would provide total access to those records.

In our opinion -- You know, we like to treat our nonoperators like we like to be treated as a nonoperator. In our opinion, there's no question that Great Western should operate this well.

Q. All right. Are you familiar with an April 5th, 1995, memo from David Catanach to Bill LeMay?

A. Yes, I am.

Q. Does that memorandum comprise Great Western's Exhibit Number 11?

A. Yes, it does.

Q. All right. Does that memorandum purport to set forth suggested guidelines to be utilized when deciding competing force pooling applications?

A. Yes, it does.

Q. Mr. Heathington, were Exhibits 1 through 11 prepared by you or compiled under your direction and supervision?

A. Yes, they were.

MR. OWEN: Mr. Examiner, I move the admission of Exhibits 1 through 11, specifically including Exhibits 8a and 9a.

EXAMINER BROOKS: Any objection?

MR. FELDEWERT: No, Mr. Examiner.

EXAMINER BROOKS: One through 11 are admitted.

MR. OWEN: That concludes my examination of this witness.

EXAMINER BROOKS: Mr. Feldewert?

MR. FELDEWERT: If I may, Mr. Examiner.

CROSS-EXAMINATION

BY MR. FELDEWERT:

Q. Mr. Heathington, what's the relationship between Davoil and Great Western?

A. There's no relationship. It's an independent corporation.

Q. There's no relationship whatsoever?

A. Not as of this date.

Q. Didn't you testify -- Did you testify previously before this Commission that Davoil was a spinoff of Great Western?

A. They were a spinoff 25 years ago from Great Western Drilling Company, yes, sir.

Q. Okay, do they gave common principals?

A. No, sir.

Q. Do they share the same lease areas in New Mexico?

A. Up until 1977 they do, they do share similar lease positions.

Q. Do they share similar lease positions in New Mexico today?

A. Only those assets acquired prior to 1977.

Q. Okay, and this was one of those assets?

A. Yes, it was.

Q. Okay. Is it -- In this particular area, then, you and Davoil commonly share interests; is that correct?

A. I'm sorry?

Q. So in this particular area --

A. Yes, we do.

Q. Okay. And do you routinely participate in projects as a group?

A. They make their own independent evaluations and

decisions, but we do tend to get along with each other, yes.

Q. Okay, have they ever disagreed with a position taken by Great Western for properties in New Mexico, in which you share a leasehold interest?

A. Sure.

Q. When?

A. They would sometimes participate, and -- We sometimes participate in projects and they don't, they will farm out our lease.

Q. Can you point to any in New Mexico?

A. Yes, we have a Grayburg Deep Unit, I believe it is, where we've drilled several Morrow wells with Phillips and EOG west of Loco Hills, and Davoil has not participated with their interest, whereas Great Western has participated as a working interest owner.

Q. Okay, and how far is that from this particular area?

A. It's in Eddy County, it's 30, 40 miles away.

Q. Okay. Now, you have been a lease owner in this area for over 30 years; is that right?

A. Yes. Just about 30 years, I guess it is. It's coming up on 30 years.

Q. And you referenced a Morrow well that you all had drilled in the 1970s; is that right?

A. Yes.

Q. Okay, how close is that well to this particular area?

A. It's about two and a half miles southeast of here.

Q. Okay, and does it produce from the same pool that is the target of the well that you propose today?

A. I believe it is.

Q. It does?

A. Yes, sir.

Q. So you've had a well in this particular pool in this area for over 30 years, and you haven't proposed the drilling of an additional well until today

A. Well, it's over two and a half miles away. It's certainly not the same exact geology.

Q. Okay, all right. Is that the only Atoka-Morrow well that Great Western has drilled in Eddy or Lea County?

A. No, sir. I mean, we've participated just a mile east of here as a significant nonoperator with a couple of --

Q. Let me focus my question.

A. Okay.

Q. Is that the only Atoka-Morrow well that Great Western has drilled in Eddy or Lea County?

A. No, sir.

Q. You have drilled another well?
A. Yes, sir.
Q. Which well is that?
A. Five or six miles north of here we've taken wells to the Morrow in the Cleveland area within the last 10 or 12 years, yes, sir.
Q. These are wells that you have drilled?
A. Yes, sir.
Q. As the driller and operator?
A. Yes, sir
Q. Okay, I thought you testified that those wells to the north were completed in the Wolfcamp?
A. They were completed in the Wolfcamp, but they went to the Morrow.
Q. Did they ever produce in the Morrow?
A. No, they -- May have a little bit. They weren't significant producers in the Morrow, no.
Q. And when were those wells drilled?
A. Those were drilled in the mid-1980s.
Q. How many?
A. I believe there were three.
Q. And it's your recollection that they went to the Morrow, or you think they went to the Morrow?
A. I know at least one of them went to the Morrow.
Q. Okay. So as you sit here today, you can testify

that Great Western has drilled one well to the Atoka-Morrow in the 1970s and one well to the Morrow in the 1980s?

A. In this particular area that's probably true.

Q. Okay. You were present at the -- Well, you've been present at a number of hearings, or at least two or three hearings before the Division in the last two months, correct, where you've discussed the development of this area?

A. I've been present in one other hearing, yes.

Q. Okay, and you're aware from those hearings that Arrington has drilled over 15 Morrow gas wells in and around the Lovington area in the last five years; is that right?

A. Yes.

Q. Okay. Let me ask you, Mr. Heathington, since Great Western drilled one well in the 1970s and, as you testify here today, one well to the Morrow in the 1980s, when you compare that to the fact that Arrington has drilled 15 deep gas wells in this area, would you agree with me that Arrington, in this particular area, has substantially more experience with drilling Atoka-Morrow wells than Great Western?

A. Not necessarily. I would like to refer to a pending application before this Division, less than a mile of here, where 13 significant New Mexico operators have

supported Great Western Drilling Company as an operator of a very similar type of test well in this area. So they apparently think that we have more ability to get that well drilled than Mr. Arrington.

Q. Well, when did Great Western decide to dust off its geology in this area and update its records and examine the development of this particular area? When did that happen?

A. Oh, probably the first of this year, after receiving a farmout request from Yates Petroleum.

Q. So the only reason that you became interested in any prospect in this area is because you received a farmout proposal from Yates?

A. That was what initially got us looking at this area, yes.

Q. Okay, and what did that area cover?

A. This federal lease covers several different tracts throughout this area, and they were trying to acquire interest in two or three sections in this particular area.

Q. Was Yates trying to acquire an interest in the east half of Section 1, which is the subject of the hearing today?

A. Yes.

Q. Okay. Were they trying to acquire an interest in

Section 34 to the northeast?

A. Yes.

Q. And were they trying to acquire an interest in Section 33 to the northwest?

A. I believe so.

Q. Okay. And up to the time that you received a farmout from Yates, you at Great Western didn't pay much attention to this area whatsoever, did you?

A. We had not looked at it, no, in detail.

MR. FELDEWERT: Okay. Let me approach, if I may, the witness.

EXAMINER BROOKS: You may.

Q. (By Mr. Feldewert) Mr. Heathington, I've handed you what was marked as --

MR. OWEN: Mr. Examiner, I would note that copies of an exhibit have been handed around. I don't have whatever has been out or reviewed, what's in front of Mr. Heathington.

EXAMINER BROOKS: Okay, has there been a copy -- Do you have a copy?

MR. OWEN: I don't --

Q. (By Mr. Feldewert) Mr. Heathington, I've handed you what was marked as Exhibit Number 3 to -- in Case Number 12,942. Have you seen this exhibit before?

A. Yes.

Q. Okay.

EXAMINER BROOKS: Okay, before you proceed with the examination, let's be sure that Mr. Owen has a copy of that.

Okay, are you ready to proceed, Mr. Owen?

MR. OWEN: Not quite, Mr. Examiner. All right.

EXAMINER BROOKS: Okay.

Q. (By Mr. Feldewert) Mr. Heathington, this exhibit represents that on January 31st David Arrington was staking an original location for the well that you have proposed here today, right?

A. Yes.

Q. Okay, and based on your testimony, at the time that Arrington is out there staking a location, obtaining an archaeological survey, obtaining an archaeological approval, Great Western is just starting to study this particular area because of the proposal they received from Yates; is that right?

A. That's probably about right.

Q. Okay. When did Great Western become interested in developing the east half of Section 1?

A. I'd like to defer to my geological witness on that, because we've acquired significant seismic data and done quite a bit of work in here over the last few months, so I'm not exactly sure.

Q. So you're not aware when Great Western became interested in developing the east half of Section 1?

A. It's been several months ago. I mean, several months ago is when we identified this as a potential location.

Q. Okay, let me ask you, when did you become aware that Great Western was interested in developing the east half of Section 1?

A. I believe last summer.

Q. Last summer when?

A. I don't recall exactly, Mike.

Q. Was it after you received the well proposal from David Arrington?

A. I'm not exactly sure.

Q. To your knowledge, was Great Western interested in developing the east half of Section 1 prior to July 23rd when they received a well-proposal letter from Arrington?

A. I'm sure we were looking at the area by then, yes.

Q. Okay. Now, you testified that you had never received what you marked as Great Western Exhibit Number 6, which is an AFE that was submitted by David Arrington. Is that your testimony, that you didn't receive Exhibit 6?

A. No, we received Exhibit 6 -- Yes, that is my testimony, with the amended location, that's correct.

Q. Well, let me ask you this. Did you -- In July of 2002, almost six months ago, didn't you receive an AFE from David Arrington that contained the cost estimates that are set forth in this Exhibit Number 6?

A. We received this AFE with an incorrect location of what this exhibit shows.

Q. Okay, and this exhibit is dated July 10th, 2002; is that right?

A. Uh-huh.

Q. And the only point you're making is that the location on this exhibit was changed from 1335 to 1665; is that right?

A. Right. I mean, and that point is because in a the situation where you have a valid joint operating agreement -- in this case we don't -- you don't have a valid well proposal --

Q. Well, let me ask you --

A. -- if the location is not correct.

Q. Okay. Is the only difference between the AFE that you received in July of 2002 and Exhibit 6 is location, up in the upper left-hand corner?

A. That's correct.

Q. Everything else is the same?

A. Right.

Q. Is that right?

A. That's right.

Q. Okay. Now, I think you testified that these costs that were submitted by Mr. Arrington in July of 2002, there's no substantial difference to the cost which you have estimated now, on October 10th of 2002?

A. There's a difference, but in my mind it's not significant.

Q. Okay. So you agree that the costs that you submitted on Exhibit 5 and the costs that Mr. Arrington -- on Exhibit 6, are reasonable in your mind?

A. The estimated costs seemed to be in line with each other.

Q. Okay, because I thought you testified that you were concerned that Mr. Arrington's AFE was not accurate. Did I misunderstand you?

A. But based on our experience as a nonoperator with Mr. Arrington in other wells, we have real concern whether or not he can live up to this AFE, yes.

Q. Well, let me ask you this. Do you believe today that the costs that are set forth on your Exhibit Number 6 and the costs that are set forth in your Exhibit Number 5, are they a reasonable estimate of the costs that you can expect from the drilling of this well?

A. Are you talking about our two AFEs, or both AFEs?

Q. Both AFEs.

A. Both AFEs. They are reasonable estimated costs.

Q. All right. Now, when Great Western finally got around to submitting a well proposal to the working interest owners, that was in -- the 1st of October, was it not?

A. End of September, I believe, yes.

Q. What was the date of your letter?

A. September 30th, I believe.

Q. Do you know when the working interest owners received your letter?

A. I assume shortly thereafter.

MR. FELDEWERT: If I may approach, Mr. Examiner?

EXAMINER BROOKS: You may.

Q. (By Mr. Feldewert) Mr. Heathington, I'm going to hand you what's been marked as Arrington Exhibit Number 4 in Case Number 12,942. That's your September 30th letter?

A. Yes, it is.

Q. Okay, and this is the first time you've submitted anything to the working interest owners in the east half of Section 1?

A. Yes, it is.

Q. Okay, and this indicates that it was received by Mr. Arrington on October 7th; is that right?

A. It went by certified mail, that's what the stamp says.

Q. Okay. Now, the letter that you sent out in September, what's the location?

A. It was the original location that Mr. Arrington proposed back in July.

Q. Okay, so it was 1335?

A. Yes.

Q. Prior to sending out this letter, did you send anybody out to the field to examine the proposed well site?

A. At that time we had not.

Q. Okay. Now, this letter in the first paragraph, which is the first time that you sent out a letter proposal to the working interest owners, it says that a well is going to be drilled to an approximate depth of 1400 and the proposed spacing unit for the well will be the east half of Section 34. Do you see that?

A. Yes, I do. It looks like a typo.

Q. Okay. So in your haste to get something out at the last minute, it looks like you just kind of cut and paste from a well proposal that you had sent out in Section 34; is that right?

A. I believe it's described correctly in the reference.

Q. Well, how did the east half of Section 34 get in there?

A. That's a typo.

Q. Prior to sending out this particular letter, did Great Western stake the well location for the property that it proposes to drill a well on today?

A. No.

Q. Has Great Western -- since sending this letter, has it been out there to stake a well site for the well that it proposes today?

A. We have had a production foreman out there to survey the access into the staked location.

Q. When did that happen?

A. Oh, it was within the last 30 days.

Q. Is that the first time you sent a well production foreman out there?

A. Yes, it is.

Q. Prior to sending out this September 30th letter, did you conduct an archaeological survey for the well that you had proposed?

A. We didn't think we needed to. Those do not have to be duplicated on federal permit applications.

Q. You didn't do one?

A. No.

Q. Okay, have you done one since?

A. We don't have to. I mean, the one's been done.

Q. Who did it?

A. David Arrington.

Q. Okay, so you're just -- you're going to rely on his archeological survey if you're named operator?

A. Yes.

Q. Okay. When did Great Western become aware that there were surface impediments at the footage location that you proposed in your September 30th letter and for which you advertised for a hearing here today?

A. At the hearing last month where Arrington put on his Application.

Q. So you didn't know that there was a problem at the 1335 location until Arrington told you at the hearing last month; is that right?

A. No, we did not.

Q. Now, you testified about the surface owner of this property. Do you know who that person is?

A. Yes, it's Mr. Dan Fields.

Q. Did you speak with him?

A. Yes.

Q. When?

A. Right after the hearing last month with Arrington. We've spoken a couple times.

Q. Have you spoken with him recently?

A. Yes, within the last two weeks, we've spoken to Mr. Fields.

Q. Okay. Now, at the hearing on October 10th, Mr.

Arrington's landman testified that Arrington had obtained a surface agreement with this particular surface owner. Do you recall that testimony?

A. If you say that's right, Mike, then that was made.

Q. Okay. Do you have any reason to believe that's not correct?

A. That's not what Mr. Fields has told us.

Q. Do you have anything other than your recollection of what Mr. Fields told you? Do you have any other evidence?

A. No, I do not. He just told us that he had not made a deal on this location with Arrington.

Q. Okay, can you testify here today that Mr. Arrington does not have an agreement with Mr. Dan Fields, who's the surface owner --

A. I certainly could not. All I can do is testify that Mr. Fields told us that he did not.

Q. Does Great Western have a surface-damage agreement with Mr. Fields?

A. We do not. We've entered into tentative negotiations with him, preliminary negotiations, pending the outcome of what goes on here.

Q. Has Great Western -- Prior to sending out your letter in September of 2000, did you apply for a permit

from the Bureau of Land Management?

A. No, sir.

Q. Have you, since sending this letter out in September of 2002, applied for a permit from the BLM?

A. No.

Q. Are you aware that Arrington has applied for that permit and that they expect approval of that permit by the end of this week?

A. I believe I testified that that shows to be approved, as of October 21st, there is an approved permit for this location.

Q. And that's issued to Mr. Arrington; is that right?

A. Yes, it is.

Q. Okay. Mr. Heathington, what do you understand the procedures to be that a working interest owner must follow before filing a pooling application with the Division?

A. As I understand it, one of the important things they like to hear is the efforts made to obtain voluntary joinder of the parties.

Q. Does Great Western believe that it can decide to drill a well one day and then file a pooling application with the Division the next?

A. (Shakes head)

Q. I'm sorry, you have to answer --

A. To protect our reserves, yes, yes, I mean, that's what we're talking about he felt like we had to do.

Q. But if Great Western was wanting to propose a well, Mr. Heathington, what procedures would you follow? Can you outline those for me?

A. Well, we haven't had any pooling applications in New Mexico. We typically obtain voluntary joinder of all the parties and go drill the well.

Q. Well, I understand your testimony that you have not proposed a well in this area for quite some time. But my question is, do you understand what procedures a working interest owner must follow --

A. Yes --

Q. -- before filing a pooling application?

A. Yes, I do, right.

Q. Can you outline those for me, please?

A. You must propose a well to the interest owners --

Q. Okay.

A. -- and attempt to obtain voluntary joinder.

Q. How long do you attempt to obtain voluntary joinder before you file your pooling application?

A. I don't think there's any set time for that.

Q. Okay. Are you of the opinion that you can propose your well to the working interest owners one day

and file your pooling application the next?

A. Apparently you can. Mr. Arrington filed his pooling Application without having an interest in the property.

Q. So you're of the opinion that Great Western can go out and propose a well to the working interest owners on a Monday and file a pooling application on a Wednesday; is that your testimony?

A. No, sir it's not. Great Western would never do that. But as I understand it, some parties do.

Q. Okay. And is that because Great Western believes that such an approach would not constitute diligent efforts to reach an agreement with the parties?

A. No, sir.

Q. Why is that?

A. I'm sorry, Mike, could you explain the question again?

Q. Okay. Well, let me ask you this. Does Great Western believe that it's proper procedure to receive a well proposal from a working interest owner in July and then do nothing for over two months, until the pooling hearing in October? Do you think that's proper procedure, Mr. Heathington?

A. We were hoping that there could be some discussions to get this worked out. And when there were no

fruitful discussions, we felt compiled to file our Application.

Q. Well, do you think it constitutes diligent efforts to pursue an alternative drilling plan when you receive a well proposal in July and do nothing until October? Do you think that constitutes diligent efforts to pursue an alternative drilling plan?

A. Yes, I do.

Q. You do?

A. Uh-huh.

Q. Okay. Do you think that constitutes good-faith efforts by Great Western to reach a voluntary agreement with the party that proposed the drilling plan?

A. Yes, I believe we've made the efforts to receive -- We've made the efforts to obtain voluntary agreement from the parties here, Arrington has not.

Q. What does Great Western generally do when they receive a well proposal in the mail from a working interest owner?

A. Basically evaluate it geologically to determine if we'd like to participate in a proposal.

Q. Okay, do you have any contacts with the party proposing the well?

A. We typically do our own geological evaluation.

Q. Do you respond to the party that's proposing a

well in any fashion?

A. Typically, yes.

Q. How do you do that?

A. If we desire to participate -- It depends on what election we wish to make. I mean, if we want to make a farmout, we would start farmout negotiations. If we'd like to participate and we deemed the party to be an acceptable and prudent operator, we would start the negotiation of a joint operating agreement.

Q. What about if you think the party proposing a well is not a prudent operator, what do you do?

A. We file a competing pooling application.

Q. Okay, and how soon do you file that competing pooling application, typically?

A. I don't see a timetable there that's relevant.

Q. All right. Now, Mr. Heathington there's no debate here, is there, that Arrington was the first working interest owner to propose a well in the east half of Section 1?

A. There's no debate that he proposed a well, not the current well that he's proposing to drill. He still has not proposed the current location that he proposes to drill.

Q. Is any debate that Arrington owns the single largest interest in this well?

A. No.

Q. Okay. And you're aware that because of that, Arrington will be responsible for paying the largest share of the costs of the well; is that right?

A. Yes.

Q. And you're aware that Arrington has a term assignment that's expiring in March of 2003?

A. Yes, I am.

Q. Okay. Mr. Heathington, let me ask you, under what circumstances is Great Western willing to accept Arrington as an operator of a well in which Great Western has a working interest?

A. Based on our past experience,I'm not sure there are any circumstances that we could accept him.

Q. Never?

A. As an operator.

Q. Never?

A. I wouldn't say never, but until his staff and personnel issues are addressed I don't see how we could.

Q. Now, you talked about his staff and you talked about his use of consultants. What consultants does Arrington use in New Mexico?

A. I don't know. I mean, just basically, the operators we talk to, you know, he just uses consultants for everything. I mean, he uses a land consultant. The

landman is actually billed to the joint account. We've never seen that with any other operator. I've been working for Great Western for 20 years; none of my services have ever been billed to the joint account.

Q. Now, Mr. Arrington uses a landman -- So the only consultant you're aware of is the landman?

A. No, he used extensive engineering consultants on the King County project.

Q. All right, now, let me back up. What consultants are you aware of that Arrington uses for his properties in New Mexico?

A. We have no direct experience with Arrington in New Mexico.

Q. So when you raise a concern about use of consultants by Arrington, you're not referencing any use of consultants by Arrington in New Mexico, are you?

A. Not any that I have direct knowledge of.

Q. Okay. Where's Arrington's office located?

A. Midland, Texas.

MR. FELDEWERT: That's all I have, thank you.

EXAMINER BROOKS: Redirect, Mr. Owen?

MR. OWEN: Yes, please.

REDIRECT EXAMINATION

BY MR. OWEN:

Q. Mr. Heathington, Mr. Feldewert handed you an

exhibit that has at the top "Arrington Triple Teaser Well Number 1". It was marked as Exhibit Number 3 in the October 10th hearing. Do you see that?

A. Yes.

Q. Now, you went through the instruments by which Arrington obtained title in this property; is that right?

A. Yes, I did.

Q. Okay, I want to refer to that Exhibit Number 3 from the October 10th hearing. The first date there is January 31st, 2002. It indicates that an original location for the Triple Teaser well was staked; is that right?

A. Yes, that is right.

Q. How much interest did Arrington hold in this acreage at that time?

A. According to the Lea County records, he owned no interest in this federal lease at that time.

Q. Well, not just according to the Lea County records, according to the instruments that you have by which he took title, what interest did he own on January 31st, 2002?

A. Arrington Oil and Gas owned zero interest in this property.

Q. What interest did Arrington Oil and Gas, Inc., own on February 28th, 2002?

A. He owned zero percentage in this federal oil and

gas lease as of that date.

Q. Is that true? The last date on there is September 17th, 2002. Did Arrington own any interest in this acreage at any time represented on this exhibit?

A. I don't believe Arrington had any interest as of September 17th on this exhibit.

Q. Okay. I want you to turn back to Arrington Exhibit -- I mean, pardon me, Great Western's Exhibit Number 9a. That's the Arrington Application.

A. Okay.

Q. The first statement on the bottom says that "Arrington is a working interest owner in the E/2 of irregular Section 1..." Was that a true statement at the time that Application was filed?

A. Based on the source of title documents that we've presented today in this hearing, that was not a true statement.

Q. Okay. Did Arrington have any right to propose a well in September, 2002?

A. It doesn't appear to me he had a right to do any of these things listed.

Q. Did he have the right to stake a well in January, 2002?

A. No, sir.

Q. Did have a right to pursue a BLM permit at any

time before September 27th, 2002?

A. Not a direct ownership right, now.

Q. Okay. How many proposals for voluntary joinder have you received from Arrington?

A. Zero.

Q. You received the AFEs, right?

A. Well, we received the AFE at the first location that has now been abandoned and move.

Q. Has Arrington made any other efforts to obtain your voluntary joinder?

A. He's made no efforts to my knowledge.

Q. How many communications have there been from Great Western to Arrington, attempting to obtain Arrington's voluntary joinder?

A. Well, as of last Friday our management decided to attempt to make a couple of proposals to Mr. Arrington, to hopefully obtain, you know, a voluntary joinder of this situation that we're hearing today. And we made a couple phone calls to Dale Douglas, and he did talk with Mr. Arrington, and informed us that those proposals were unacceptable.

Q. So you had the initial proposal from Great Western; is that right?

A. Yes.

Q. The original AFE?

A. Yes.

Q. And you had a joint operating agreement sent to Arrington?

A. Yes.

Q. And you had an amended AFE sent to Arrington?

A. Yes, we did.

Q. And you've contacted Arrington since that time?

A. Yes, we have.

Q. All right. And Mr. Feldewert asked you about the estimated costs on this well, and you agreed that the costs, the estimated costs submitted by both parties are reasonable estimated costs; is that correct?

A. Yes, it is, Paul.

Q. Based on your experience with David H. Arrington Oil and Gas, Inc., are the costs estimated by Arrington a reasonable estimate of the costs that Arrington will actually charge?

A. Based on our experience, that's a highly unlikely probability.

Q. Okay. Do you know what date Great Western's Application was filed in this case?

MR. FELDEWERT: I think it was the day of Arrington's pooling hearing.

THE WITNESS: You're probably going to have to help me with that exact date, Paul.

MR. OWEN: Mr. Examiner, I think we can stipulate that October 9th was the date that Arrington filed -- that Great Western filed its Application. Is that correct?

MR. FELDEWERT: I think that's right. It was either the day of the hearing or the day before.

MR. OWEN: It was October 9th, 2002.

Q. (By Mr. Owen) When did Great Western submit its well proposal to Arrington?

A. We submitted the original well proposal on September 30th, 2002.

Q. Did you file -- Did you submit a well proposal one day and file your Application the next?

A. No, we did not.

Q. Okay. Mr. Feldewert asked you if Arrington owns the single largest -- or if Arrington is the single largest interest owner in this tract; is that right?

A. Yes.

Q. And you indicated that Arrington is?

A. He is as of late -- November 13th, yesterday, Lea County Records, he appears to be the owner of a 50-percent interest.

Q. Was Arrington the single largest interest owner in January, 2002?

A. To our knowledge, Arrington did not own an interest in this property in January of 2002.

Q. Was Arrington the single largest interest owner when it filed its Application in September, 2002?

A. Arrington Oil and Gas did not own an interest in this federal lease when they filed that Application.

Q. Arrington Oil and Gas, Inc., didn't own any interest until September 27th, 2002, right?

A. That's correct.

MR. OWEN: Okay. That's all I have.

EXAMINATION

BY EXAMINER BROOKS:

Q. Okay. In the legal description -- I can't read Exhibit Number 1 very well. Can you give me those lot numbers again?

A. Yes, sir. Those are Lots 1, 2, 7, 8, 9, 10, 15 and 16.

Q. 1, 2, 7, 8, 9, 10, 15 and 16; is that correct?

A. I believe that's correct.

Q. Do you know which of those lots -- You've enumerated four units that you want created, a 320, a 160 an 80 and a 40. Can you give me the lot numbers for each of those four units?

A. Mr. Examiner, I'm having kind of a little bit of trouble also with some of these, but -- They are hard to see on our exhibit, but I believe the 160-acre unit would be Lots 1, 2, 7 and 8.

Q. 160 is Lots 1, 2, 7 and 8?

A. -- 7 and 8, yes. The 80-acre unit would be Lots 2 and 7.

Q. 2 and 7.

A. And the 40-acre unit would be Lot 2, it looks like.

Q. 2, okay. Do you know if the actual acreages of these lots vary at all from the standard 40 acres?

A. They do slightly, each one of them very slightly from the standard 40.

Q. Does your Application contain acreage figures for each of the lots?

A. No, it does not.

EXAMINER BROOKS: Okay, we will need that information in order to write an order in this case, so I'd greatly appreciate it, Mr. Owen, if you or Mr. Feldewert can furnish me with that information. Is it in your Application, Mr. Feldewert, do you know?

MR. FELDEWERT: I don't think so. No. We can get and break it down.

EXAMINER BROOKS: Okay, I appreciate that.

Q. (By Examiner Brooks) Have there been any negotiations between Arrington and Great Western on this issue of operations?

A. Yes.

Q. And can you describe, if you're familiar with them, what negotiations have occurred?

A. As I testified, last Friday we called Dale Douglas to discuss a couple of possible scenarios that would forego the necessity for this hearing, and they involved -- one of them involved -- Do you want the details of the discussion?

Q. Well, I don't need to know what you talked about in terms of proposals, I just need to know what negotiations took place and when.

A. Okay, last Friday we made a couple of different proposals to solve this, last Friday, to allow this to go forward without a hearing.

Q. Were there any negotiations prior to last Friday?

A. No, there was not.

Q. Now, the AFE that was submitted by Arrington for the well 1335 from the east line, I believe you testified in response to Mr. Feldewert's question that that was the only difference between that AFE and the one that was admitted in evidence; is that correct?

A. I believe that's correct.

Q. Okay. And do I also understand your testimony that that is not -- that Great Western -- that's not material to Great Western in the sense that you also are proposing your own well at the new location also, 1665 --

A. Well, we proposed the original location that he proposed, and then of course it had to be moved because of surface reasons. And then he never re-proposed the actual location he proposes to drill, and we did. We went ahead and sent out an amended AFE, amended location.

Q. There's no disagreement about the location?

A. Not at this point, no, except that we haven't received that proposal from Mr. Arrington.

Q. Did you also testify that you are not familiar with any other operators who used consultants as extensively as Arrington?

A. We have not seen -- Operators, some small operators definitely use consultants. There's no question about that. And typically, the more established or larger the company, the less consulting uses are made. But small operators -- We have been in wells where small operators have used consultants, but not to the extent that we've seen here.

Q. Are you familiar with the way David Fasken operated prior to 1983?

A. A little bit. They used an engineering consulting firm, I believe, yes.

Q. Are you aware that David Fasken had no employees and used consultants for all functions?

A. I think they did, into the 1970s. I was aware of

that, yes.

EXAMINER BROOKS: Okay, thank you. No further questions.

Mr. Catanach?

EXAMINER CATANACH: Just one question.

EXAMINATION

BY EXAMINER CATANACH:

Q. Do you know what the association is between David H. Arrington and Dale Douglas?

A. As I understand it, he is kind of like -- He is not an employee, as I understand it, and he is just a preferred land consultant. He's the professional landman that does Mr. Arrington's land work.

Q. Now, he acquired the interest in this acreage on March 1st, 2001, from Hunt Oil Company; is that your understanding?

A. That's what the instruments show.

Q. Now, do you know if he acquired that interest on behalf of Arrington at that time?

A. It's possible that he did, since he's now, as of yesterday, assigned that to him. But I don't know exactly what the relationship was.

EXAMINER CATANACH: Okay, thank you. That's all I have.

MR. FELDEWERT: Mr. Examiner, if I may?

EXAMINER BROOKS: You may.

FURTHER EXAMINATION

BY MR. FELDEWERT:

Q. I didn't quite understand what you said. You said as of yesterday he assigned it to Mr. Arrington?

A. To Arrington Oil and Gas, yes.

Q. Are you basing that on Exhibit Number 8a? I'm trying to understand where you're getting that conclusion, Mr. Heathington.

A. Dale Douglas assigned an interest in this federal lease of record yesterday, it was filed yesterday of record in Lea County.

Q. It was filed in the records yesterday?

A. Yes.

Q. All right. What's the effective date of that assignment?

A. It looks like it was notarized on October 4th.

Q. What's the effective date of that assignment? Doesn't it say effective for all purposes as of March 1st, 2002?

A. Yeah, it has an effective date of that, yes.

Q. Okay, one other question. We asked about the -- You've made an issue about the footage location. Can you identify any records to me that Great Western has filed with the Division that identify a footage location of 665

[*sic*] feet from the east line?

A. 1665?

Q. Yeah --

A. For --

Q. I'm sorry --

A. Just in our Application.

Q. In your Application. Have you reviewed your Application?

A. Well, excuse me, I think we did refer to it as a legal location in the northeast quarter, yes.

Q. Okay. Can you point to any document that you have filed with the Division in which you have identified the footage location that you propose today?

A. Just the exhibits that we've talked about today.

Q. Which exhibits?

A. Our exhibit that has the 1665 location on it, the AFE.

Q. Okay, and that's the first time?

A. Yes.

Q. Okay. And you're aware that when Mr. Arrington filed his Application back in September, that he set forth in that Application a 1665 location, correct?

A. Yes.

Q. And he also advertised a 1665 location, correct?

A. Yes.

Q. All right. Have you advertised a 1665 location?
A. No.
MR. FELDEWERT: That's all I have.
EXAMINER BROOKS: No further questions.
MR. OWEN: That's all I have of this witness.
EXAMINER BROOKS: You may call your next witness.
MR. OWEN: Thank you. Call Mr. Russell Richards.

RUSSELL P. RICHARDS,

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

DIRECT EXAMINATION

BY MR. OWEN:

Q. Please tell us your name and where you live.
A. Russell Paul Richards, Midland, Texas.
Q. Who do you work for?
A. Great Western Drilling Company.
Q. What do you do for Great Western?
A. I'm their exploration manager.
Q. Have you previously testified before this Division or one of its Examiners?
A. Yes, I have.
Q. At that time were your credentials as a petroleum geologist accepted and made a matter of record?
A. Yes, they were.
Q. Are you familiar with the Application filed in

this case?

A. Yes, I am.

Q. Have you made a technical study of the area which is the subject of this Application?

A. Yes, I have.

Q. Are you prepared to share the results of that study with the Examiner?

A. Yes, I am.

MR. OWEN: Mr. Examiner, I tender the witness as an expert in petroleum geology.

EXAMINER BROOKS: So qualified.

Q. (By Mr. Owen) Mr. Richards, have you prepared exhibits for presentation in this case?

A. Yes, I have.

Q. Are you prepared to make a recommendation to the Examiner as to the risk penalty that should be assessed against the nonconsenting interest owners?

A. Yes, I am.

Q. What is that recommendation?

A. It is 200 percent.

Q. Are you going to explain the basis for that?

A. Yes, I will.

Q. All right. Let's turn to Great Western Exhibit Number 12. Can you review that for the Examiner, please?

A. Yes, Exhibit 12 is a structure map on the top of

the Morrow lime in the area around the proposed location. The Morrow lime is a readily correlatable horizon in the general area -- or actually, you know, over a broad area. It is a structural point that is right below the Atoka objective, and therefore, you know, it's a relative map datum.

Shown on the map is a -- color-coded symbols, based on production from -- zone of production. The blue are Atoka-Townsend wells, and the green wells are wells producing from the Morrow. The proposed location is shown in red.

The significance of structure for this location, in my mind, is that the proposed location is located within a southeast-to-northwest-trending structural re-entrant or paleo-valley, and it's my opinion that this was the control of deposition for the Atoka sand, which I'll talk about additionally later.

Q. Okay. Well, let's go ahead and turn to Exhibit Number 13. Talk about the Atoka sand.

A. Exhibit 13 is a gross sand isopach of what I refer to as the Atoka-Townsend sand. You can see that within the sand trend that the proposed location is within, there is one well producing, based on my interpretation, in the extreme southwestern portion of Section 6. That well has made a little over 100 million feet, and it's still

producing 270 MCF per day.

Also what gets our interest in the area for the Atoka is wells further to the east in what I interpret as a separate sand that either are or projected to be more economic wells. We're projecting in excess of 20 feet of gross Townsend sand at this location, based on nearby well control.

Q. Okay. And keeping specifically Exhibit Number 12 in front of you, why don't you turn to Exhibit Number 14 and review that for the Examiner?

A. Yes, Exhibit 14 is a cross-section depicting the two nearest wells to the proposed location. I will point out that this line of section is shown on Exhibit 12, B-B'. The left-hand well on the cross-section is the HNG Lovington Plains well, which is a direct southwest offset to the proposed location. And the well on the right-hand side of the cross-section is the Humble Elliott Federal well, which is a 40-acre northeast offset to the proposed well.

Just starting discussion about each of the two objectives and what these wells encountered when they drilled them, first in the HNG well, they encountered in excess of 30 feet of Atoka sand. They cored that entire interval in three different core sections. There was no further data released concerning those cores, but it is my

assumption and interpretation that they feel like they did not have reservoir quality in that interval to attempt a completion.

Going to the Humble Elliott Federal well, I give that well 24 feet of gross Atoka sand. A couple of indicators of reservoir quality there in that well. First, I've highlighted in red the microlog separation, which we use as an indicator of permeability. It's on these older logs. It's really kind of the best tool to look at.

The other thing within that interval and that wellbore, there was a DST across the Atoka interval, but -- it's DST 1 there in the depth column of that log. The DST extended down, actually, into a porosity zone in the upper part of the Morrow line. DST had good recovery of gas, it flowed gas to surface at a million and a half a day with indications of good reservoir pressure.

One thing -- I mean, it's open to interpretation whether or not that gas came from the Townsend -- Atoka-Townsend sand or from the Morrow lime. Another nearby well that was drilled at a similar time, it DST'd the Atoka. The sand by itself was tight, so I'm concerned that -- even though I'm hopeful that, you know, it's of reservoir quality, one of the risks is that -- indeed, that that Atoka interval is tight, and it's tight in both wells. You know, that's a significant risk.

However, I mean on the other side what we're optimistic about is that this interval can be fracture-stimulated to increase production.

Moving down to what we see as our next primary objective, it's shown as the Morrow clastics interval toward the lower part of the cross-section. The HNG well was completed over about four sands within this gross interval. The perforations marked in the depth column that were reported were just top and bottom. I don't believe they perforated that entire section, just probably the gas-effect sands there.

This well was acidized with 5000 gallons. It IP'd for 1.3 million cubic feet a day. It subsequently has made 860 million cubic feet, and it's currently making about 80 MCF a day.

Going over to the Humble Elliott well, they DST'd an interval -- it's DST 3 -- there within that section also. That DST had gas to surface at over 4 million cubic feet a day and also recovered condensate. That's encouraging. The results of the well are discouraging.

The DST Number 2 there within that -- shown on that depth column on the same well, had good shows as well and had gas to surface. This well was subsequently -- Or subsequent to these DSTs, this well was drilled on to the Devonian, and then well was -- a completion attempt was

tried over these porosity zones in the Morrow. The well IP'd for 4.5 million cubic feet a day and 257 million barrels of oil, except it made -- reported production was 82 million cubic feet and no water.

You know, my opinion about this specific area has changed over time. I mean, initially what our thinking was, had been for some time, is the reason we weren't pursuing it harder, is that the Morrow was of limited reservoir extent. I think the more we've looked at this, though, we feel like where the upside to this particular area is, is if that indeed is not the case but what we're dealing with are sands within the Morrow that are water sensitive because of clays.

The other thing, you know, recent technical advancements that also gives us encouragement is that recent fracture-stimulation techniques employed, we feel some optimism that they can enhance the production in both the Atoka and the Morrow.

I would point out again that HNG well only did an acid job -- 5000-gallon acid job. You know, if EOG was drilling that well today, that well would be frac'd fairly extensively, you know, either with CO_2 or methanol.

Q. And those -- the frac techniques and the other enhanced recovery techniques lead you to believe that these wells will be more successful?

A. That's correct.

Q. Or that the proposed well will be more successful.

A. That's correct.

Q. Okay. Were you present during the October 10th, 2002, hearing on Arrington's Case Number 12,942?

A. Yes, I was.

Q. Did you hear Mr. Bill Baker's interpretation of the geology in that case?

A. Yes, I did.

Q. How does your interpretation differ from that of Mr. Baker?

A. I think -- The main difference is that Mr. Baker interprets the two -- pointing to the Humble Elliott Federal well, there's two porosity -- or two zones highlighted in red indicating permeability. Mr. Baker interpreted those zones to be a sand above the Morrow lime. His Morrow lime pick was below where I have it.

I've looked at that -- You know, I had looked at it before and subsequent to the hearing and, you know, looked at sample logs, all the available data. It's not conclusive, but I don't see any reason to change my interpretation that those porosity zones are actually in the Morrow lime sample logs, indicate that they're not real good logs, they're not lag samples, and so there's some --

you know, it's subject to interpretation.

What that does with that lower structural datum, what he, in fact, has is a -- at the proposed location he shows a small structural closure. And you know, that's the difference in my mind. They're not significant differences. For one thing, I don't think -- This is not a structural play for the most part. We've got to have the sand, and I'm looking for -- you know, I'm looking for why would it be deposited here.

Q. When did you start considering the geology in this area?

A. It was earlier this year, late winter or early spring this year. What -- you know, the things that -- Several things that Mr. Heathington had mentioned, you know, request, inquiries by Yates Petroleum as to our interest in the general area. There was also activity and some things going on that we were aware of up south of the Morton area that caused me to start -- you know, to re-look at that.

The other thing that we saw was that the well staked in Section 6 -- it's a Kukui de-gas well, it's in the northeast portion of Section 6 -- those recent developments, you know, the activity was coming to us to the north, you know, we were monitoring that. But they key things was, you know, request and the staking of this Kukui

well in Section 6, that we again started looking at it.

Q. David H. Arrington Oil and Gas, Inc., first proposed this well to you in July, 2002; is that right?

A. That's correct.

Q. Did you do any geologic interpretation of this area for purposes of developing a prospect prior to receiving Arrington's --

A. Yes, we had --

Q. -- proposal?

A. -- we were in the process of working it.

Q. What were you doing?

A. Updating activity, monitoring it. I mean, we had the mapping done based on already -- you know, wells that we had participated in years past. I'd point to the well in the extreme eastern part of the map. That's a well drilled by Nadel and Gussman that we owned a 32-percent working interest in. I mean, we were watching it, we had an interpretation. But I think what -- the kind of renewed interest in the immediate area caused us to reconsider it again.

As I said, my interpretation prior to this, my concern -- and it still is a concern -- is, what is the reservoir quality and as well as, you know, possible clay damage, water damage, preventing economic production. And that's a lot of what caused us to initially have concerns

about pursuing this further.

Q. Now, you said that the renewed interest in the area was spurred by the recent developments there. Was one of those recent developments that spurred your interest in this area Arrington's proposal?

A. No, we were looking at it before the proposal was received.

Q. Okay.

A. He was just a little further ahead of us.

Q. Have you conducted a geologic interpretation independent of that which Mr. Baker presented at the October 10th --

A. Most definitely.

Q. Did you piggyback on Mr. Baker's geology?

A. Not at all.

Q. Did you piggyback on his interpretation?

A. No. I respect Bill Baker's work, but I certainly don't need to copy his work.

Q. Does any part of Exhibits 12, 13 and 14 indicate a copying of Mr. Baker's work?

A. No, they do not.

Q. Okay. Do you believe there's a chance that you could drill a well at the proposed location that would not be a commercial success?

A. Yes, for the reasons outlined before, I do think

that is a definite possibility.

Q. Does Great Western seek a different well location than that proposed by Arrington in Case Number 12,942?

A. No, we do not. We initially looked at a possible location that would more actually twin the Humble Elliott Federal well, but because of surface considerations -- a couple of trailer houses with some other surface structures in that part of the section -- we saw that that was really impossible. And we don't see a significant difference between Arrington's proposed location, you know, and what we would pick first.

Q. Did you, in fact, independently review the area to determine if there was a more feasible surface location?

A. Yes, I did. As I said, our production superintendent looked at other options. I mean, one thing that I considered also geologically was the possibility of drilling this location further to the southeast along this structural re-entrant. I thought geologically they may have more merit, based on not only this subsurface interpretation but also based on the 3-D interpretation that we have.

But there again, we would have had to move significantly further south than I was comfortable with, due to surface problems, or drill the well directionally, and I didn't feel like that was a tradeoff that was

acceptable.

Q. Okay. Does Great Western propose to drill to a different formation or horizon than that proposed by Arrington?

A. No, we do not.

Q. Are you aware that Mr. Baker recommended a 200-percent risk penalty be awarded against the nonconsenting interest owners if Arrington's Application for compulsory pooling is granted?

A. Yes, I am.

Q. Do you agree with Mr. Baker that a 200-percent risk penalty be awarded against the nonconsenting interest owners if the lands are pooled?

A. Yes, I do.

Q. Have you reviewed Arrington's recent drilling activities in the area?

A. Yes, I have.

Q. Why don't you review Great Western Exhibit Number 15 for the Examiner?

A. Exhibit 15 is a list of wells based on data provided to me by IHS Energy Services. IHS is a subscription-based data vendor. It's a former Dwight's PI company, and their services provide the oil and gas industry with data that they acquire from, typically, state agencies.

This list covers the period from January, 2001, to the most current data that I had, which is the end of September, I believe. I don't have the exact date of when this -- This data is updated monthly, but it lags in being current.

During that period of time, Arrington Oil and Gas had permitted 23 wells, and they had drilled 13 wells.

This also -- This is for wells drilled in Lea and Eddy County, which is the vast bulk of Arrington Oil and Gas activity during this period of time.

Q. Okay. Let's turn to -- Well, as a part of your review of Arrington's drilling activities, did you also whether Arrington reached voluntary agreement with other interest owners, with respect to Arrington's well proposals?

A. Yes, I did.

Q. Why don't you turn to Exhibit Number 16? Can you review that for the Examiner?

A. Exhibit 16 is a listing which is a summary of information that was acquired from the New Mexico Energy, Minerals and Natural Resources Department, Oil Conservation Division, website that -- under hearing dockets -- all those dockets during that period of time, from January 1 of 2001 through to date, were reviewed.

I was looking to see -- just curious how many

compulsory pooling applications Arrington Oil and Gas had made during this period.

Q. And how many did they make?

A. Twenty.

Q. How many wells did they permit during that same period?

A. Twenty-three.

Q. What does that tell you about Arrington's willingness to reach voluntary agreement?

A. Well, before I answer that, I would point out that I did make an attempt to match up compulsory pooling cases to permitted wells. I could get about half of them to match up. I think, you know, the discrepancy would be that there were permits filed prior to January of 2001 that appear later on the compulsory pooling Application list, or there were wells that were permitted -- or wells that were permitted later that, for whatever reason they have not been drilled or no other application has been made.

But you know, with this comparison the conclusion that I draw is that I feel like that this information points directly to Arrington's inability or his unwillingness to reach voluntary agreement with the interest owners in the projects that they pursue.

Q. Is that consistent with your experience in this case?

A. Most definitely.

Q. Is that consistent with your experience in the case directly to the northeast of Section 34?

A. Yes, it is.

Q. Okay. How many compulsory pooling cases has Great Western been involved in, in the last two years?

A. Two.

Q. Which cases are those?

A. This case before us today, and the one in Section 34.

Q. Has Great Western been involved in other compulsory pooling cases in any other jurisdictions?

A. No, we have not.

Q. Has Great Western drilled and operated wells in other jurisdictions?

A. Yes, we most definitely have.

Q. During that same period of time?

A. Yes, we have.

Q. Has Great Western been successful in reaching voluntary agreement with all the other interest owners in those projects?

A. Yes, we have.

Q. Okay. Does Great Western have any experience drilling and operating Permian Basin wells in the last few years?

A. Most definitely.

Q. Why don't you turn to Exhibit Number 17? Can you please review that for the Examiner?

A. Exhibit 17 is a list of wells also provided from the IHS data set, of wells that were operated by Great Western Drilling Company during the period January 1st to date. There were -- Within this 21-month period, there were 28 wells that were operated by Great Western. This does not include areas outside of southeast New Mexico or the Permian Basin of Texas. During this period of time we did operate six Mesaverde downspacing wells, and additionally we operated a gas well on the Texas Gulf Coast as well.

You'll see the bulk of our activity during this time period has been in Terry County where we had a new field discovery in late 2000 that we have drilled about 20 wells on subsequent to that. This field -- You know, based on the results that we've had there, it's a significant part of our business. We project it to be, you know, a 5-million-barrel reserve field. It's probably about half drilled up. There will be downspacing wells and waterflood operations that will take place here as well.

One thing also of significance that I'd point out about Great Western's operations is that in that specific area we are involved with three other operators that, as a

nonoperating interest owner, when I compare our operations with what they do, we drill the wells consistently lower cost, we have had fewer mechanical and drilling problems. The main issue here is that we're drilling through an area of existing production that's under waterflood, so we have significant issues with lost circulation and water flows there that we've dealt with very well. And also, I would point out that we've made better wells based on production, you know, than the other operators that we're involved in, in that area.

One other kind of significant technical well that Great Western has just recently completed, it's the third well on the list, in Pecos County, this is a 10,000-foot Devonian gas well that we drilled a 3000-foot horizontal lateral in. It was, you know, almost a $2 million operation. It went off well, we've made a good well, you know, it's currently producing a little over a million cubic feet a day.

Q. Are any of these wells depicted on Exhibit 17 deep gas wells in the Permian Basin?

A. Well, that Noelke well in Pecos County is one of the deeper ones that -- the Winkler County McKee well is also -- the depth is not noted there, but it was a deeper well. I don't remember the exact depth.

Q. Does Great Western have the personnel and

experience necessary to prudently drill and operate a deep gas well in the Permian Basin?

A. Yes, we do.

Q. Does Great Western have the personnel and experience necessary to prudently drill and operate the well proposed in this case?

A. Yes, we do.

Q. Mr. Heathington indicated that Great Western had had a prior disagreement with Arrington about some operations and had audited Arrington's operations. Has Great Western ever been audited by other interest owners in their wells?

A. Yes, we have. In March of this year, we were -- an audit was requested by one of our partners in the Terry County wells that we were operating, and this audit was a routine request, due to the amount of activity that we had and the money involved. We recognized that they had the right to do this audit under the operating agreement. The audit involved expenditures related to 15 of these wells at the time, and the associated lease operating expenses. That audit also covered 95 percent of all expenditures during that time period. As I said, the audit was done in March and it was completed in a couple of weeks.

You know, the two significant bottom-line points in the audit was, first, that we expended a total of $10.1

million on behalf of the joint account. When the audit compared AFE estimate to what the actual costs were, specifically related to the drilling of the wells, Great Western's final cost accounting showed that we drilled and completed these wells within 7-percent variation between what we estimated the wells to cost and what the final cost was for the entire project.

The second significant point that came from the audit is that audit exceptions that were identified by our working interest partners were less than one half of one percent of the total dollars expended.

Q. How long have you been in the oil and gas business?

A. Twenty-one years.

Q. How long have you been working in the Permian Basin?

A. Twenty-one years.

Q. Were you involved in the prior projects in which Great Western and Arrington were related?

A. Yes, I was.

Q. Based on your experience and your experience with David H. Arrington Oil and Gas, Inc., do you have an opinion as to whether Arrington can prudently drill and operate the well proposed in this case?

A. Based on our experiences, and comparing that with

the experience that we've had with other operators, I cannot at all be comfortable saying that he would act in a prudent manner. And that's our concern for this whole matter, is that he indeed cannot prudently operate these wells.

Q. Is it your opinion that he cannot prudently operate the well in this case?

A. That's correct.

Q. Do you have an opinion as to whether Great Western can prudently drill and operate the well proposed in this case?

A. Great Western has been in business for over 60 years, all of our staff has been in place. You know, for over ten years this level of activity that I've shown here is typical for what we've done during that period of time, operationally. We have definitely demonstrated that we can consistently operate prudently and efficiently.

Q. Are you aware that Arrington's term assignments expire -- at least one of them expires the beginning of March, 2003?

A. Yes, I am.

Q. Is Great Western willing to have a requirement written into any order resulting from this hearing that a well be spudded before March 1st, 2003?

A. Yes, we would.

Q. Okay.

A. We respect that right to preserve his working interests, and certainly we would not want to jeopardize that.

Q. Were Great Western's Exhibits 12 through 17 prepared by you or compiled under your direction and supervision?

A. Yes, they were.

MR. OWEN: Mr. Examiner, I move the admission into evidence of Exhibits 12 through 17.

EXAMINER BROOKS: Any objection?

MR. FELDEWERT: No, Mr. Examiner.

EXAMINER BROOKS: Twelve through 17 are admitted.

MR. OWEN: That concludes my examination of this witness.

EXAMINER BROOKS: Cross-examination?

CROSS-EXAMINATION

BY MR. FELDEWERT:

Q. Mr. Richards, do you have Exhibits 15 and 17 out in front of you?

A. Yes.

Q. Exhibit 15, this depicts all of the -- this depicts wells that David Arrington has drilled in the last -- or since January of 2001 in Lea and Eddy County; is that right?

A. That's correct.

Q. Okay. And Exhibit 17 depicts wells that were drilled by Great Western in the last two years?

A. That's correct.

Q. It doesn't show any wells in Lea or Eddy County, correct?

A. No, it does not.

Q. Okay. The well that you are proposing here today, that is going to be drilled in Lea County; is that right?

A. That's correct.

Q. Okay. And according to your Exhibit 17, you have not drilled a well in Lea County in the last two years; is that right?

A. Yeah, I believe I stated that to his previous question.

Q. And Arrington has drilled, it looks like, 11 wells in Lea County, right? In the last two years?

A. That would be correct.

Q. Has Great Western drilled any wildcat wells in Lea or Eddy County -- Well, let me back up. Has Great Western drilled any wildcat wells in the last two years?

A. Yes, we have.

Q. Is that one?

A. The EOG TXL was a wildcat well. The Geodyne 1

well was a wildcat well, actually was a -- you know, testing a separate producing trend idea. The Brit Clare 16, even though it's got a high number, that was a wildcat well based on based on distance from production. The ARCO -- Those wells, yes.

Q. Okay, your Exhibit 17 lists one wildcat well, right?

A. Based on -- Yes, that's correct, based on IHS's interpretation of -- yes, that's correct.

Q. Okay, based on their interpretation. And it lists a number of them for David Arrington in and Eddy County on Exhibit 15, right?

A. Yes, it does.

Q. Okay, you've been involved in two compulsory pooling cases --

A. Yes.

Q. -- in New Mexico in the last two years?

A. Yes.

Q. Okay, and how many wells have you proposed in New Mexico over the last two years? Two, right?

A. I believe that's right.

Q. Okay, so in the two wells that you've proposed over the last two years, you've had two compulsory pooling cases, a 100-percent rate, correct?

A. Yeah, if you want to look at it that way, yes.

Q. When did you -- Now, I want to know when you started your examination of the east half of Section 1.

A. We started looking at the area -- to the best of my recollection, it was late winter or early spring of this year.

Q. And you looked at the east half of Section as a prospect?

A. Yes.

Q. In late winter or -- Was it early spring of this year?

A. Yes, that's when we started working the area. I mean, I know where we have acreage, start looking at it all, you know?

Q. Okay. Well, let me ask you this. When did you become serious about developing the east half of Section 1?

A. It was identified as part of the same -- as part of this process, it was this summer.

Q. This summer when?

A. I don't know the exact date, Mr. Feldewert.

Q. And this summer is when Arrington proposed to drill its Triple Teaser well; is that correct?

A. Yes, I don't remember the exact date.

Q. When you received Arrington's well proposal in July of this year, did you talk with Bill Baker about the prospect and location at any time?

A. No.

Q. What did you do in July after receiving Arrington's well proposal?

A. Well, I mean, we had internal discussions about the fact that we would not want to participate with him as an operator.

Q. So you guys drew a firm line with him in July that you were not going to participate with him as an operator?

A. Well, that was the gist of the discussions internally, yes.

Q. Okay. Did you ever call Arrington up and apprise them of that?

A. No.

Q. When did you send a production foreman out to look at a prospect in the east half of Section 1?

A. It was within the last month. I'd say three weeks ago or so.

Q. Three weeks ago?

A. Uh-huh.

Q. So roughly five months after you get Arrington's well proposal?

A. If that's what it is.

MR. FELDEWERT: That's all I have, thank you.

EXAMINER BROOKS: Okay. Redirect, Mr. Owen?

MR. OWEN: Very briefly, Mr. Examiner.

REDIRECT EXAMINATION

BY MR. OWEN:

Q. Mr. Richards, do you have an opinion as to whether there are significant differences in geology between the wells which Great Western has drilled and operated in the Permian Basin and the area around the proposed well, which would affect Great Western's ability to prudently drill and operate this well?

A. The issues are very much similar Basinwide, quite frankly. A lot of it is relative to depth. And at this depth, you know, the basic issues are always going to be deviation, wellbore -- you know, safety containment. In this specific area, the other thing we want to watch for are protection of potential reservoir horizons by preventing and reducing water loss.

Q. Have you been involved in wells in which Great Western was a nonoperator, which were drilled in Lea and Eddy Counties in the last five years?

A. Yes, I have.

Q. Did you review the geology and the engineering associated with the drilling and operating?

A. Yes, we did. We were significantly involved in the decisions on those.

Q. Based on Great Western's experience drilling and

operating wells in the Permian Basin and involvement as a nonoperator in drilling and operating wells in the immediate area around the proposed well, do you have an opinion as to whether Great Western can prudently drill and operate this well?

A. We most definitely can prudently operate this well.

Q. Okay. Now, Mr. Feldewert asked you how many wells Great Western had proposed in New Mexico in the last two years. Do you know how many wells Great Western has proposed anywhere in the last five years?

A. Well, how I would arrive at this number is, this past two years, this represents our typical operated activity. It also represents about half of our overall activity when I include nonoperated activity. You know, if we were the operator, we would be proposing these wells. So in the last five years I'd have to say that we've proposed 50 or 60 wells.

Q. As an operator?

A. As an operator.

Q. How many times have you had to file a compulsory pooling application?

A. Twice.

Q. Why did you file compulsory pooling applications in those cases?

A. To protect our interest.

Q. Against what?

A. Against being forced to participate or be nonconsent with an operator that, based on our past history, could not prudently operate these proposals.

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

EXAMINATION

BY EXAMINER BROOKS:

Q. Okay, I just want to be sure I understand your testimony correctly. You have described some differences between your geologic interpretation and Mr. Baker's geologic interpretation, correct?

A. Some differences. I'm not -- I don't know how significant they are, Mr. Examiner.

Q. That was going to be my next question. I got the sense from your testimony that you did not consider the differences in your interpretations to be particularly significant.

A. I think the main thing that Mr. Baker testified to, that he felt like that this location was significant because there was a small structural closure there, and it was about -- just remembering, his map was about 40 acres in size. I would disagree with his correlation. But you know, we're wanting to drill the same location to the same depth; the outcome is going to be the same, no matter what

the difference between our interpretations are.

Q. Right. Did I understand you to say that you have seismic that covered this area?

A. Yes, we do.

Q. And when did you acquire that, or did you have it done?

A. No, we acquired it. We have what I believe is the same data set that Arrington has, and we acquired that this fall -- August -- I don't remember when it was relative to the well proposals, but it was late summer.

Q. Okay. The well proposal was in July, so that would have been right in the same general area of time, right?

A. Right, we knew from our work and discussing other active operators in the area that the key to this trend is -- for the Morrow, is playing structural lows, either -- you know, kind of isolated lows, which is what is being played up to the northwest by Yates, or being in positions immediately downthrown to faults, which is -- there's a well in Section 22 to the north, it's a significant completion in the Mississippian that was immediately downthrown to a large regional fault.

So having the seismic was, you know, critical to final determination of appropriate locations. I mean, the basic picture that we had based on subsurface has not

changed, but fine-tuning of the locations dictated the need for having the seismic.

Q. Okay. I notice that this Elliott Federal well that's on your cross-section, that this is actually in this unit. You characterize it as inactive. Has this well been plugged and abandoned?

A. Yes, it has.

Q. Okay.

A. We found the dryhole marker there. It's right near a trailer house.

Q. Okay. Now, you mentioned one of these wells in which you drilled through an existing waterflood. That was one of your wells in Texas; is that correct?

A. Most all these in Terry County, they're on -- the shallow producing unit is the Prentice Upper Clear Fork Unit, yes.

Q. Okay. Now, that's not something that's involved in this --

A. No, it's not.

Q. -- this location? Okay. It looks like, from this Exhibit Number 17, that most of your wells have been in Texas; is that correct?

A. That's correct.

Q. And --

A. As I said, I would reiterate that during this

time period we drilled six Mesaverde downspacing wells, and we also drilled a well in the Gulf Coast of Texas.

Q. Now, they don't do a lot of compulsory pooling in Texas.

A. No, sir that's not an option available to us.

Q. Because there are some fairly strict limits on when it's available and because there's some fairly onerous conditions that you have to meet before you can qualify --

A. That's correct.

Q. -- in Texas.

A. So everything that we do in Texas requires that we achieve voluntary joinder, or we're faced with being in a co-tenancy situation where you're carrying that interest with no penalty. So it's very, very mandatory that we achieve voluntary joinder.

EXAMINER BROOKS: I don't have any further questions.

Mr. Catanach?

EXAMINER CATANACH: I don't have any questions.

MR. OWEN: I have a quick --

EXAMINER BROOKS: Go ahead.

EXAMINATION

BY MR. JONES:

Q. Mr. Richards, the rig that you would get if you were awarded this drilling operatorship, would it be a

footage rate or a day rate?

A. They've had discussions with some of the available operators, and those are the two options. I think the first choice would be a footage rate, because we feel like it keeps them, you know, in more of the risk position. But that has not been determined yet.

Q. Okay, I understand you had a real experienced drilling foreman that would sit the well?

A. That's correct.

Q. Okay. Does your foreman sit the wells from the surface to the TD?

A. Yes, typically so, yes. A lot of that's determined by whether not it's footage or day work, you know. The supervision is different, depending on which choice that is.

Q. Right. So they might typically sit for a week and then have a relief sit for a week?

A. Yeah, I think -- That would be correct. This close to Lovington, I think it's going to be pretty much Kenneth Liven there.

Q. Okay, that's his field. Okay, and that person would charge his time out to the well, right?

A. While it's drilling, yes. Otherwise, that is covered under the overhead..

Q. Okay. What geologic risk factor would you assign

this well?

A. Risk penalty factor?

Q. Risk factor.

A. Chance of success of success?

Q. Chance of success of success. Or chance of -- yeah, success.

A. Well, to answer that, what my main concern is, I think we're going to make a well that's productive of gas. I think where I see the risk is whether or not it achieves volumes that are in quantities to pay out and return an investment to us. So the chance of completion, I would say, is fairly high. One in, you know, 70 percent or whatever. The chance of commercial success I would have to categorize as much lower than that.

Q. Okay. Who owns the northeast of Section 34 in the next township? On your Exhibit 13, you show over 30 feet of thickness, and...

A. The east half of 34 is the acreage that's involved in the other compulsory pooling case that's before the Commission now. We own interest there in the south half of the northeast and the north half of the southeast, and a well has been proposed to be drilled there in the northwest of the southeast.

MR. JONES: Okay, that's all of my questions. Thank you.

EXAMINER BROOKS: Gentlemen, anything further?

MR. OWEN: Nothing further for this witness. As you might expect, I do have a few remarks.

EXAMINER BROOKS: Okay. Well, Mr. Feldewert, do you have anything to present?

MR. FELDEWERT: I have no evidence to present, no, Mr. Examiner. We presented our case at the October 10th hearing.

EXAMINER BROOKS: Very good. I assume you also want to make some remarks?

MR. FELDEWERT: Yes --

EXAMINER BROOKS: Okay, well --

MR. FELDEWERT: -- please.

EXAMINER BROOKS: -- as the Applicant you may proceed first, Mr. Owen.

MR. OWEN: Thank you, Mr. Examiner.

Mr. Examiner, Mr. Feldewert is going to hand you a three-ring binder with a number of cases from the Division. I appreciate the opportunity to address those. I think that those cases are going to be cases which I've presented to you in another case, and which -- They are cases in which the Division recently considered competing force pooling applications.

Those cases were decided on a number of different factors. One of them was decided on geology, one of them

was decided on the majority interest. One or two of them were decided on who proposed the well first, because the other factors were equal. Those factors are split among all those orders.

The only place that we have -- Much to Mr. Catanach's discomfort, the only place that we have those factors compiled is in the April 5th, 1995, memo from Mr. Catanach to Mr. LeMay. And Mr. Catanach did an exemplary job of categorizing those factors which this Division should consider in deciding competing force pooling applications.

I'm sure that Mr. Feldewert is going to go into great detail with regard to those orders, and I'll wait to address those until after he puts them before you. Suffice it to say that they strongly favor Great Western's Application in this case.

But turning to the April 5th, 1995, memo, because that's the only one that has a comprehensive set of factors, I'd like to go through that.

The main thing that you need to consider is relevant and pertinent evidence in a number of different factors numbered a) through i). The first one is "Any information related to pre-hearing negotiations conducted between the parties."

There's only been one party that has proposed any

negotiations. That's Great Western. Arrington has not negotiated, and has declined to negotiate when Great Western has proposed it. Without giving you the details of those negotiations, which Mr. Heathington did not do, the salient fact is that Arrington has declined to negotiate; Great Western has offered negotiations.

The second factor is the willingness of the operator to reach a voluntary agreement. Great Western has reached voluntary agreement with the other interest owner in this well, the third party. Arrington has reached voluntary agreement with nobody. Great Western contacted Arrington last week to gauge interest in a compromise, in a voluntary agreement. Arrington was unwilling to consider a voluntary agreement.

Arrington has failed to reach voluntary agreement in 20 out of 23 recent projects in which Arrington was involved in just the last two years. Arrington's practice of invoking this Division's power to take another party's interest should not be endorsed or encouraged by this Division.

Arrington doesn't just pool first and negotiate later, Mr. Examiner. If we look at the evidence in this case, Arrington pools first and acquires its interests later. At the time that it filed its Application, Arrington held no interest, zero interest, in this acreage.

One of Arrington's contract landmen -- and that's exactly how Mr. Baker's [*sic*] capacity is characterized in the transcript from the October 10th hearing, on page 6, lines 17 through 25:

QUESTION: Mr. Douglas, would you please state your full name and address for the record?

ANSWER: My name is Dale Douglas, I reside in Midland, Texas.

QUESTION: And by whom are you employed and in what capacity?

ANSWER: I'm an independent petroleum landman doing contract land services for David Arrington Oil and Gas, Inc.

Dale Douglas owned interest in this property since March of 2001. Arrington first acquired its interest September 27th, 2002. That is the first time that Arrington owned any interest in this property, and that was a small interest, a 14-percent interest, from Tom Brown, Inc. Arrington acquired the balance of its interests, with which it sits before you today, on October 4th, 2002, through an assignment from Mr. Douglas.

Arrington doesn't just pool first and negotiate later, it pools first and acquires its interests later.

Moreover, Arrington proposed a well at a location 1335 feet from the east line on July 25th. It filed its Application on September 17th. It didn't acquire any interest, September 27th. It didn't acquire its majority interest until October 4th, and it never proposed a well at the 1665 location. The only way Great Western knew about it is, we came to the hearing on October 10th.

One of the factors that some of these orders consider is, when was the first well proposal made? Arrington has never proposed a well at the 1665 location. It's proposed a well at a 1335 location. Great Western has proposed a well at both locations and is properly before the Examiner on that Application.

The third factor is the interest ownership with the particular spacing unit being sought.

Arrington sits here today representing 50 percent of the interest. Again, I'm not going to go into great detail on that; I've done it *ad nauseum*. But Arrington has only very recently acquired that interest. Arrington had no right, to the extent that any negotiations were considered, to the extent that any activity was undertaken by David H. Arrington Oil and Gas, prior September 27th, 2002. All of that activity was taken before Arrington owned any interest in this tract at all.

Great Western represents 50 percent of the

interest before you. That interest is committed to this project through a joint operating agreement, which treats not just who's committed to this well and what the risk penalty for nonconsenting interest owners is, but a great deal of other factors, including joint accounting, including subsequent operations. All the factors are listed in the joint operating agreement, and I invite you to consider them. They're far more comprehensive than any order that could be issued by this Division. That voluntary agreement should be recognized and should be endorsed by this Division.

The next factor is the geologic evidence and testimony as it relates to the proposed well locations, especially if the locations are different. That's not at issue.

There's a slight difference between the geology, but the reason that was presented is to show you that Great Western wasn't sitting around. Great Western was developing this project. It was developing this project independently of Arrington. It acquired its 3-D seismic in August, I believe Mr. Richards testified. But it had been considered and actively working the geology on this prospect since the beginning of this year. The geology is not an issue. But what is at issue is that Great Western has been actively developing this project.

And that is the next factor, the information regarding the date the prospect was developed, proposed, et cetera. I want to stress again that Arrington has never proposed a well at the location which is before you. Arrington files its Application, then acquires its interests, and never proposes the well. It proposed the well with those costs at the 1335 location. But it's not an insignificant fact that Arrington has not proposed this well.

Great Western has considered this prospect since early 2002. It proposed the well on September 30th, 2002. It submitted its AFE on October 21st -- well its amended AFE, pardon me. Its initial AFE was submitted on September 30th, 2002, with the proposed JOA, and its amended AFE was submitted on October 21st, 2002. Its Application, in fact, was filed not the day after the Great Western AFE was submitted but sometime thereafter, in October.

Regarding Arrington's negotiations, it's also not an insignificant fact that Great Western has proposed a JOA, has proposed monthly rates for operation and supervision. Arrington has not. All Arrington has proposed is a well at a location that's not before the Division, with no detailed proposal, such as has been submitted by Great Western.

The next factor is the overhead rates for

supervision. Great Western's rates are slightly lower, but as Mr. Heathington testified, that's not significant, we're not making an issue of that in this case.

What we are making an issue of is the reasonableness of Arrington's estimate. Great Western comes in right around its AFEs on the wells it drills, Arrington doesn't.

Great Western testified -- and the only testimony before this Division is that Arrington consistently overshoots its AFEs by a large margin, including in one case 180 percent. We're not presenting that to you to testify about the prior dispute between the parties, we're presenting that to you so that you can assess the reasonableness of Arrington's proposed overhead rates. We submit that the rates proposed by Arrington are reasonable, but we submit that Arrington's estimate itself is probably not where Arrington is going to come out. Those costs are suspect.

The next factor is the proposed risk penalty. That's simply not at issue. Both parties are proposing a 200-percent risk penalty.

Next factor is the significant difference in AFEs. Is there any significant difference in AFEs? I've already covered that. They're very close. We're not making an issue of the actual AFEs themselves, we're making

an issue about Arrington's actual estimates. I think it highly likely, and based on these witnesses' expertise, experience, it's their opinion that Arrington will not come in close to those AFEs, or close to his AFE.

Final factor is other information deemed pertinent by the Division Examiner. And with all due respect to Mr. Catanach, there is one factor that's outlined in Order Number R-10,731-B that falls within this, it doesn't fall within the other factors listed. And on page 9 of that order, one of the factors is -- listed on that order, is that both parties are capable of operating the property prudently, so it's not a factor in that case, in Order Number R-10,731-B.

In this case, though, it is an issue. Arrington is not capable of operating this property prudently. Great Western and Davoil have formally and voluntarily committed to the well through execution of the JOA naming Great Western as the operator.

This Division's statutory duties are to prevent waste and protect correlative rights. By joining Great Western's proposal and executing Great Western's JOA, Davoil has indicated its agreement that Great Western is a party better suited to preventing waste, protecting correlative rights and operating this property prudently. This Division should recognize that endorsement.

Moreover, Arrington has specifically shown its deficiencies as an operator in previous dealings with Great Western in four different ways.

First, Arrington doesn't have the necessary personnel on staff to oversee the drilling and completion of wells. Mr. Heathington testified extensively regarding that fact.

Second, Arrington failed to comply with its JOA provisions, it failed to act as a prudent operator by withholding access to joint accounting records, by denying interview access to Great Western's personnel for the preparation of joint interest billings and the operation of wells, by denying access to Arrington's offices for purposes of conducting an audit.

As a result, the nonoperators, including Great Western, when they're involved with Arrington, are consistently damaged by increased costs, as well as the opportunity to make informed consent and nonconsent decisions.

The third reason that Arrington is not a prudent operator is, in its previous dealings with Great Western, it failed to have any procedures for the control of lease and well equipment. That shows a failure by Arrington to conduct all well operations in a good and workmanlike manner.

And finally the fourth reason Arrington is not a prudent operator, as Mr. Heathington indicated, is, it failed to provide notice to Great Western and other interest owners when it undertook subsequent operations, including plugging, abandoning wells, sidetracking wells, undertaking other subsequent operations.

In short, Mr. Examiner, what we have in this case is essentially equal interests, essentially equal geology, essentially equal estimated costs.

What we also have in this case is evidence supporting the conclusion that Arrington is not capable of operating this well prudently.

What we also have in this case is evidence that Arrington didn't even own any interest in this well when it filed its Application.

What we have in this case is evidence that the statement made by Arrington in its Application that it owned an interest, working interest, in the property and had the right to drill, was false at the time it was made.

What we have in this case is extensive testimony that Great Western is an extremely experienced operator with the personnel and experience necessary to drill and operate this well in a prudent manner. We request that you dismiss Arrington's Application and enter an order pooling the lands and naming Great Western as operator.

Thank you.

EXAMINER BROOKS: Mr. Feldewert?

MR. FELDEWERT: If I may approach --

EXAMINER BROOKS: You may.

MR. FELDEWERT: It's been a long day, we've had a lot of Arrington-bashing. I'm going to try to focus the case on what I understand to be the relevant factors before this Division, and the first -- Under Tab 1 I have Mr. Catanach's April, 1995, memorandum.

And Mr. Owen went through the relevant and pertinent evidence that's described in the memo. I find that rather surprising because we spent most of the day on irrelevant and unnecessary evidence under this memorandum. And I'm talking specifically at the bottom of that page we've had subjective judgment calls on Mr. Arrington's ability to drill a well, we've had subjective judgment calls on Mr. Arrington's ability to produce and operate the well, and we've had extensive discussion on incidents and description of previous disagreements between the parties over there in Texas.

Now, we do not have a witness, and I have not prepared a case to have a little mini-trial on every disagreement that these entities have had in the past, because I've always understood that those are irrelevant. And it's my understanding that that has been the Division's

policy since 1995. And we'll walk through the orders. I have yet to see any order where there's any decision based on previous disagreements between the parties or subjective judgment calls on the ability of the operator to drill or operate a well.

And keep in mind that this is coming from an operator who has drilled absolutely no wells in Lea or Eddy County in the last two years and therefore, I submit, has absolutely no experience in this area.

The relevant factors are evidence concerning the prehearing negotiations and willingness of operators to negotiate a voluntary agreement.

Arrington Exhibit Number 3, which we submitted, they sent out their well proposal in July of this past summer. They didn't file a pooling Application until September.

Mr. Heathington on the stand said, We will never participate in a well with Mr. Arrington.

Mr. Richards got on the stand and said, Well, we made a firm decision in July that we're not going to participate in any well with Mr. Arrington.

They do nothing till October. The Monday before the pooling hearing is when we receive their competing well proposal. The day before the pooling hearing is when they file their competing pooling Application. It didn't even

have a case number yet by the time we got to the hearing. That's how last-minute it was.

Clearly the entity that has demonstrated an unwillingness to negotiate any kind of a voluntary agreement with Arrington which would allow him to operate any well is Great Western.

The second factor, interest ownership within a particular spacing unit, favors Arrington. He owns 50 percent, he's going to pay half of the costs of this well. Great Western owns 32 percent, roughly. They're going to pay roughly a third of the costs of this well.

The next two, geologic evidence, information regarding the dates -- I'm sorry, geologic evidence, et cetera, that's a wash in this case. There's no disagreement on that.

The factor in e), information regarding dates the prospect was developed, proposed, et cetera. That is Arrington's Exhibit Number 3.

Now, given the fact that they sat around since July and did absolutely nothing, they've tried to come up with some reason why Arrington never proposed a well in July. They try to put some blinders on and say, oh, we never got a well proposal in July at 1665, it was at 1335.

Well, Mr. Examiner, Great Western -- I mean, we could play that game, but Great Western has not proposed

any well at 1335. There's no well advertised at 1335, they never proposed a well -- I'm sorry, there's no well advertised at 1665, which is where everybody agrees that it should be located, and they never proposed a well to the interest owners at 1665.

Arrington advertised the 1665 location, Arrington's compulsory pooling Application filed in September talked about a 1665 location, everybody knows that 1665 is where the well is going to have to be drilled. That little technical argument, to me, gets them nowhere.

They also tried to make an issue about when Mr. Dale Douglas, who works on behalf of Arrington, has worked on behalf of Arrington for a long time, holds property on behalf of Arrington -- they tried to make an issue as to when Mr. Douglas assigned the interest over to Arrington that he acquired under the term assignment. That interest assignment was effective March 1st, 2002. So for all intents and purposes when Mr. Arrington files his Application, he owns the interest.

But if we want to play that game, Great Western comes in here, and you can't find one letter from Great Western to Mr. Dale Douglas, the guy they say owned the property, the guy they say held the working interest.

Great Western, from day one, which of course was late in October -- they sent all the information, they send

their well proposal, they send their competing pooling Application to Arrington, not Dale Douglas. So for them to come in here and say that Arrington did not own the interest, did not have a right to drill a well, was not a working interest property, is ridiculous. And to the extent they want to maintain that position, that means they failed to propose a well to the proper interest owner at the time that it was sent.

But we shouldn't be playing that game, because there is no issue here that the parties have proposed wells. The issue here is, who went first and who did the work and who has shown the diligence?

Now, before we leave the Catanach memo, there's only one other point here that has any distinction and that is other information deemed pertinent by the Division Examiner. I would submit to you that the fact that Mr. Arrington has a term assignment expiring in March of 2003 is a significant factor that the Division ought to take into account in naming an operator, because it seems to me that Mr. Arrington ought to have the opportunity, and I think he has earned the right, to control his own destiny with respect to that term assignment.

Now, I want to quickly go through the orders because it has been a long day, but Mr. -- and I apologize, but in the packet, in the front packet of the notebook

there is an order. It's inserted in the front. I didn't get it into the notebook. It's Order Number 10,731. This is an order that Mr. Owen apprised the Division of in connection with another case.

And you'll see if you go through that order, which was entered by Mr. Catanach in January of 1997, they had competing well proposals between InterCoast -- you have to be careful how you say that name, but InterCoast -- and Yates, in which they were proposing an east-half location. If you look at page 3 of that order, you'll see that the AFEs were substantially the same, the overhead rates there was no debate, there was no debate over the risk penalty. And so what the Division did is, they went through the chronology of events.

And what Mr. Owen quotes -- and his letter to the Division is found on page 7 of the -- I'm sorry, page 8 of the opinion, and it's Paragraph (24). And it says, "In the absence of other" competing "factors, the operatorship of the E/2" which was in dispute "should be awarded to the operator who originally developed the prospect, developed the" geology "data necessary to determine the optimum well location, and initially sought to obtain farmout or voluntary agreement to drill its well."

EXAMINER BROOKS: For the record, I believe it says "other compelling factors". It sounded like you might

have said "competing", and I --

MR. FELDEWERT: Thank you.

EXAMINER BROOKS: -- want to make sure the record is correct. Go ahead.

MR. FELDEWERT: So that is what the Division told the operators in 1997, and you'll see there that they then awarded the operatorship to InterCoast. And this was in a situation, Mr. Examiner, where Yates testified, as Great Western has done today, that they will commence drilling of a well by the drilling deadline to preserve a farmout agreement that InterCoast was concerned about losing. They left the destiny of that farmout agreement in InterCoast's hands, the looked at the chronology of events, and InterCoast was the party that first presented the well, they're the ones that worked towards getting the well permitted. Therefore, they were first in line. And according to the Division, they were entitled to a pooling order.

Now, that was back in 1997 that the Division articulated that first in time, first in line position.

And if you look at the next order under Tab 1 [*sic*], which is Order Number 11,566, this was an order that was dated April 17th, 2001, after a hearing before Examiner Stogner. And what you'll find in this order, Mr. Examiner, is that the parties agreed on everything that's laid out in

Mr. Catanach's memo.

And Ocean was the entity that first proposed a deep gas well in the subject area. They did that in October. Yates didn't file a competing pooling application with the Division or propose a well until December.

And what the Division said in 2001, in Paragraph (21) on page 7 was the following: "Having proposed a deep gas well to the Morrow formation within the subject 355.80-acre lay-down...spacing and proration unit first, Ocean's proposal set forth..." and they lay out the case numbers "...should be approved, and the application...of Yates...should be denied."

So what the Division has told the operators in 1997 and again in 2001, and I submit in all periods since that time, is that when we have a situation like this, when the parties agree on the geology, when there is no debate over the costs, that what the Division will look to is who filed first, who did the work.

And that strongly favors Mr. Arrington here. He was out there in January staking a well, when Great Western was just dusting off their geology and reacting to a farmout from Yates. Mr. Arrington was out there proposing a well in July when Great Western still had not acquired enough information to where they thought they could do anything and really didn't express the desire to develop

this property. So I would submit that when you look at these orders, Mr. Arrington should prevail in this matter.

Now, we've also talked about ownership in this spacing unit. If you look at the next order that I have in the book, it's Order Number R-10,731-B. It was a debate between Yates and Medallion.

And if you look at Paragraph (24) of that particular order, Mr. Examiner, which is on page 10, it says, "In the absence of compelling factors such as geologic and prospect differences, ability to operate prudently, or any reason why one operator would economically recover more oil or gas by virtue of being awarded operations than the other, 'working interest control,' as defined and modified by findings 23 (d) and (e) should be the controlling factor in awarding operations."

The working interest ownership here favors Arrington. The working interest ownership control in this case is 50-50.

The next order, Division Order Number R-10,742, this was an order entered in a hearing with Examiner Catanach. It was entered in 1996. If you look at Paragraph (21) on page 6, it was a dispute between Penwell and Santa Fe Energy. In Paragraph (21) a) it points out that "Penwell initially developed the prospect in the N/2

of Section 28 by first proposing..." a well.

Then in Paragraph (22), this is what the Division told operators: "In the absence of other compelling factors, the operatorship of the E/2 of Section 29 should be awarded to the operator who initially developed the prospect, who initially undertook the risk involved in drilling..." that well that they were talking about, "...and whose geologic interpretation appears to more accurately depict the Strawn reservoir underlying the subject acreage."

There's no difference in geology here, but what is of importance here is that they were looking at the operator who initially went out and tried to develop this prospect. Who did the work, who got out there in the field, who tried to get this project on line first? That was Penwell, and that's why Penwell was designated the operator.

Finally, the last -- Well, I have in here a Commission order now, 11,663. That was entered in November of 2001. It was a dispute over the orientation of a spacing unit, Mr. Examiner.

What's important here is, if you look at page 5, Paragraph 24, here's what the Commission told operators in 2001, in Paragraph 24 on page 5: "It has long been the practice of the Commission to require parties to show good

faith and diligence in proposing a well to other interest owners in the unit as a prerequisite of a compulsory pooling order." And they cite the Oil and Gas Act. That's what the Commission said.

Now the last order that I have in this booklet is Order Number R-10,977, and the reason that I have that in there is because this was an order entered by the Division after a hearing with Mr. Catanach. It was dated 1998 but consistent with what the Commission said as its long-standing practice. You will see on page 3 [*sic*] at Paragraph (3) that the Division dismissed an application that was filed by Redstone because the pooling application and the well proposal was filed within a week of one another.

So Mr. Examiner, I submit to you that under the Commission precedent, under the precedent set by this Division, Great Western has to come in and show diligence as a prerequisite to a consideration of its pooling Application. And that's because you have to have diligence not only to develop the property but also to negotiate in good faith.

And I would submit that their actions in this case fall well below that requirement. They've held their property since 1973. They did nothing, they let Arrington do all the work this year. They complain about Arrington's

operations, but they do absolutely nothing to develop the property themselves. and upon receiving Arrington's well proposal in July, they do nothing for three months. They sit around and do absolutely nothing.

And they wait till the Monday of the pooling hearing in which to propose a well, and the day before the pooling hearing in which to file a competing pooling Application.

I don't think that that shows diligence, I don't think that shows good faith. But that's up for the Division to decide.

Arrington's Exhibit Number 3 lays out all it has done this past year to get this case in line. And it represents that Arrington is the party that is first in line, a fact that the Commission and the Division has indicated is important in cases like this.

Arrington owns a majority of the working interest, another important consideration in cases like this. Arrington is the party that has demonstrated the diligence to move this case forward, to move this prospect forward, another important consideration.

And finally, Arrington is the working interest owner who's facing the expiration of a term assignment. They can promise all they want, but we don't know what's going to happen. And I submit to you that Arrington has

the right, and it has earned the right, to control its destiny with respect to that term assignment. It has done everything it has been required to do under the Oil and Gas Act and under the Division's orders and the Commission orders and the precedence of this body to be entitled to a pooling application and be entitled to the pooling application -- or order that it has requested in this case.

We ask that you grant Mr. Arrington's pooling Application so that it can continue in a timely fashion with the development of this property that it initiated way back in January of this year.

Thank you.

EXAMINER BROOKS: Rebuttal, Mr. Owen?

MR. OWEN: Yes, thank you, Mr. Examiner.

First case from the Division to which Mr. Feldewert refers, Order Number R-10,731, was a Division case. In that case the Division did find that the operation should go to InterCoast because InterCoast proposed the well first.

That case was taken *de novo*, the Commission considered that argument. Turn to Tab Number 3 that Mr. Feldewert provided you. That is Order Number R-10,731-B. On page 7 the Commission recognizes the fact that Medallion -- which, due to an unfortunate slip of the tongue from Mr. Carr was re-named -- was the new name of InterCoast --

Medallion made the same argument to the Commission. That argument was rejected.

Medallion contends that it is an experienced operator, and due to the fact that it took the initiative in developing the prospect and was a moving force in getting the well drilled, it should be allowed to operate its State of New Mexico 20 Well Number 1 and operate the east half of Section 20. That's Mr. Feldewert's first-in-line argument. It's not the basis on which this case was denied.

This case was denied -- Or this case was decided on another basis entirely, working interest control. It's indicated on page 10 in Findings Number (24) and (25). And Mr. Feldewert makes much of the working interest control, he states that Arrington controls 50 percent and Great Western controls a very small percentage.

In fact, Mr. Examiner, to figure out what we mean by working interest control I want to refer you a few pages back to page 6. On that page 6 under Finding (16) it indicates that Yates Petroleum Company, Yates Drilling Company, Abo Petroleum Company and Myco Industries collectively own 37 percent, and by virtue of a unit agreement Yates controlled an additional 14.765 percent.

Working interest control means how much of the working interest do you control? In this case, Arrington

controls 50 percent now. They didn't at the time the Application was filed. Great Western controls 50 percent by virtue of the joint operating agreement which has been executed. That's not an issue in this case.

I would also like to point out that in Finding Number (24) on page 10 of Order Number R-10,731-B, the Commission in rejecting Medallion, formerly InterCoast's, argument about the first-in-line argument, said that in the absence of other compelling factors -- and it described these other compelling factors -- geologic and prospect differences, ability to operate prudently and then other things which are not at issue in this case -- the geologic and prospect differences are not at issue in this case; the ability to operate prudently is.

Mr. Feldewert went through Mr. Catanach's 1995 memo. He said that all the testimony that we presented about Arrington's inability to operate prudently is irrelevant because it has to do with subjective calls and it has to do with prior disagreements between the parties.

Mr. Examiner, I submit that pursuant to Order Number R-10,731-B, one of the compelling factors before you are the parties' ability to operate this property prudently. Great Western presented significant testimony, unrebutted testimony, that Arrington is unable to operate this property prudently. We didn't present that to throw

mud on Arrington and show about these previous disagreements that we've had. We did it to show you that Arrington is unable to operate this well prudently.

I'd like to move briefly through the other orders which Mr. Feldewert presented to you.

Under Tab 2, Order Number R-11,566, operations were granted to Ocean. And in that case, Mr. Examiner, on page -- Well, what I want to do with that case, Mr. Examiner, is refer back to the transcript from the hearing held on October 10th.

In that hearing, Mr. Feldewert represented, on page 46, lines 18 through 25, that "Our office has always advised clients that if you receive a well proposal, you must take action. You can't do anything for over two months, and then the week of the pooling hearing suddenly file -- or submit to the working interest owners an alternative plan, come over to the Division two days before the pooling hearing or the day before the pooling hearing and file a competing pooling application."

He goes on to say that -- on page 48, lines 13 through 17, he goes on to say that one of the factors is "...properly proposed the well in writing to the working interest owners, sought concurrence from them and timely filed a pooling application after the necessary, what I've always understood to be, six-week period of time to allow

the parties to attempt to reach an agreement."

Mr. Feldewert represented to the Division that it is his office's policy to advise a six-week period of time before you can file a pooling application, you must propose the well six weeks before you file a pooling application.

In Order Number R-11,566 Mr. Carr, from Mr. Feldewert's office, represented Yates. Yates filed its application on December 20th, 2000. Yates first submitted its proposal on December 27th, 2000. It's not the policy of Holland and Hart to recommend a six-week period of time. This 30-day rule or six-week rule or whatever the rule, however the rule is characterized, does not exist. There is no prerequisite period of time which a party must observe between proposing a well and filing an application.

I'd like to turn to the third case again. That is Order Number R-10,731-B. We've already talked about that case, Mr. Examiner. I want you to concentrate very carefully on the fact that there are other compelling factors in this case. That other compelling factor, as specifically enumerated by the Commission in rejecting the Division, includes the ability of the operator to operate this well prudently. We've presented evidence that Great Western can and Arrington cannot.

I'd like for you to turn to the fourth tab. Mr. Feldewert, several times, said that it is this Division's

policy, long-standing policy, to give operations to the party that filed first, the party that did the work.

Mr. Examiner, you've seen the geologic testimony. You've seen that both parties have done a lot of work, a lot of geologic work, a lot of work getting this prospect developed. Both parties have done the work. Is it this Division's policy to give operations to the party that files first? It's not.

Look at Number R-10,742 under the fourth tab provided by Mr. Feldewert. Mr. Feldewert turns you to page 6 of that order. In Finding Number (21) a) it says that "Penwell initially developed the prospect...by first proposing to drill the F.H. '28' State Com Well No. 1".

In this case Penwell was not the first to file, Penwell was not the first to propose this well at issue in this case. I want you to turn to page number 4.

The first full paragraph says that "By letter dated September 25, 1996..." Santa Fe proposed the well.

The next paragraph says that "By letter dated October 1, 1996..." Penwell proposed the well.

Santa Fe proposed the well first, Mr. Examiner.

The next full paragraph says that two weeks later, not six weeks or 30 days, Penwell filed a compulsory pooling application.

The next full paragraph says that on October

24th, 1996, Santa Fe filed its compulsory pooling application. Penwell, who proposed the well second and filed its compulsory pooling application second -- Actually, it did file its compulsory pooling application first. Penwell proposed the well second. It's not whoever happens to get in line here who's going to prevail in every case. The question is, are there other compelling factors?

And in fact the Division recognizes that in Finding Number 22 on page 7. "In the absence of other compelling factors..." it says that because Penwell first developed the prospect Penwell should be designated the operator.

Mr. Examiner, other compelling factors are at issue in this case, including the specific other compelling factor of Arrington's inability to prudently operate this property.

The next case is Order Number R-11,663-C, and that was entered on December 5th, 2001. I'm not sure quite why Mr. Feldewert brought this before you, because this case was decided on geologic factors. It had nothing to do with who proposed the well first, it had nothing to do with who held a majority interest. It had to do with geologic factors. That's indicated in Finding Number 19 on page 4.

But what I would point you to, Mr. Examiner, is Finding Number 25 on page 5. The Commission has not set

out specific standards for establishing what still constitutes good faith and diligence, preferring to address these issues on a case-by-case basis. There's no first-in-line rule. You need to decide these cases on a case-by-case basis.

The final application before you, Mr. Examiner, or the final order, is Order Number R-10,977, entered in 1998. In that case, Redstone's application was dismissed because Redstone filed its application before they proposed the drilling of the well.

We've talked about whether it is this Division's policy to require the filing of an -- the submitting of a proposal before the filing of an application. It's not. But even if it is, Great Western submitted its proposal before it filed its application in this case. It's not an issue. This order is not at issue in this case.

What is at issue is a party's good-faith negotiations. What is at issue is a party's willingness to reach a voluntary agreement. What is at issue is Arrington's ability to operate prudently.

Great Western has submitted the only proposals to reach voluntary agreement. Yes, Great Western is unwilling to participate in a well in which Arrington is the operator. That doesn't mean that's the only option for voluntary agreement. There are farmout options, there are

options where Great Western would operate, there are options where Arrington would drill and Great Western would operate. There are all kinds of options. And Great Western has proposed those options to Arrington. Arrington has refused to negotiate.

Arrington didn't even own an interest when it filed its Application. We're talking about good faith and diligence. Arrington was not diligent in acquiring its interest before it files an Application. Instead, it comes before the Division and makes a false statement, that it does own a working interest, when it files its Application. It's not good faith, it's not diligent.

And finally, Mr. Examiner, don't discount the testimony that's before you about the parties' relative abilities to diligently and prudently drill and operate this well. Great Western is a very experienced operator with significant experience in the Permian Basin, has the experience and the personnel on hand to drill and operate this well in a prudent manner. Arrington does not.

We request that you dismiss Arrington's Application and enter an order naming Great Western operator of this well.

Thank you.

MR. FELDEWERT: Mr. Examiner, if I may, two things.

One, I think we have some -- a decision that has to be made by the Division here, and that is, are we going to turn these compulsory pooling cases into operator-bashing? Are we supposed to come in here and start bashing the other operators over the head, over their subjective judgment calls and their ability to operate a well? That seems to me that what they are proposing, because that is the only compelling factor that they have put forth, in contrast to what the Division has always recognized as the appropriate factors.

Secondly, I'm not sure what Mr. Owen is representing to the Division, because in his November 6th letter to the Division he referenced Order R-10,731, and he said that in other words, the Division --

(Building alarm began to sound.)

MR. FELDEWERT: -- endorsed the first-in-line factor as the only determining factor when it viewed all the other factors as equal.

So I don't -- You know, I'm not saying that is the only factor. What I'm saying is that good faith and diligence have to be considered, and I think we're trying to go down the path here of turning these cases into operator-bashing rather than the factors that the Division introduced from the Examiner.

EXAMINER BROOKS: Okay.

MR. OWEN: Just for the record, I don't think the alarm has anything to do with the veracity of Mr. Feldewert's statements.

EXAMINER BROOKS: I agree with that. I think we're going to have to probably respect the alarm.

If there's nothing further, Cases Number 12,942 and 12,956 will be taken under advisement.

(Thereupon, these proceedings were concluded at 2:05 p.m.)

* * *

I do hereby certify that the foregoing is a complete record of the proceedings in the Examiner hearing of Case No. _____, heard by me on _____, 20__.

_____, Examiner
Oil Conservation Division

CERTIFICATE OF REPORTER

STATE OF NEW MEXICO)
) ss.
COUNTY OF SANTA FE)

I, Steven T. Brenner, Certified Court Reporter and Notary Public, HEREBY CERTIFY that the foregoing transcript of proceedings before the Oil Conservation Division was reported by me; that I transcribed my notes; and that the foregoing is a true and accurate record of the proceedings.

I FURTHER CERTIFY that I am not a relative or employee of any of the parties or attorneys involved in this matter and that I have no personal interest in the final disposition of this matter.

WITNESS MY HAND AND SEAL November 24th, 2002.

STEVEN T. BRENNER
CCR No. 7

My commission expires: October 16th, 2006