

BEFORE THE
OIL CONSERVATION COMMISSION
SANTA FE, NEW MEXICO
AUGUST 9, 1961

EXAMINER HEARING

IN THE MATTER OF:
CASE 2346

TRANSCRIPT OF HEARING

DEARNLEY-MEIER REPORTING SERVICE, Inc.

ALBUQUERQUE, NEW MEXICO

PHONE CH 3-6691



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BEFORE THE
OIL CONSERVATION COMMISSION
SANTA FE, NEW MEXICO
AUGUST 9, 1961

IN THE MATTER OF: -----
:
:
Application of Pan American Petroleum :
Corporation for an order pooling all :
mineral interests in the Basin-Dakota :
Gas Pool in the S/2 of Section 24, : Case 2346
Township 29 North, Range 12 West, San :
Juan County, New Mexico :
:
:

BEFORE:

Daniel S. Nutter, Examiner

EXAMINER HEARING

MR. NUTTER: Case 2346.

MR. MORRIS: Application of Pan American Petroleum Corporation for a force pooling order.

MR. BUELL: For Pan American Petroleum Corporation, Guy Buell. Associated with me, Mr. Charles Malone, of the firm of Atwell and Malone of Roswell.

GEORGE W. EATON, JR.,

called as a witness herein, having been first duly sworn on oath, was examined and testified as follows:

DIRECT EXAMINATION

BY MR. BUELL:

Q Mr. Eaton, would you state your complete name, by whom



you are employed, in what capacity, and at what location, please.

A My name is George W. Eaton, Jr.; and I am employed by Pan American Petroleum Corporation in Farmington, New Mexico; and I am Senior Petroleum Engineer.

Q Mr. Eaton, you have testified at prior Commission Hearings and your qualifications as a Petroleum Engineer are a matter of public record, are they not?

A Yes, sir; they are.

(Whereupon Petitioner's Exhibit 1 marked for identification.)

Q (By Mr. Buell) Mr. Eaton, let me direct your attention, now, to what is marked as Pan American's Exhibit 1. What does that Exhibit reflect?

A Exhibit 1 is a map of a portion of the Basin-Dakota Pool in San Juan County, New Mexico. On Exhibit 1, I have colored the Dakota wells in that particular area involved in red. The specific area covered by Exhibit 1 is the vicinity of Township 29 North, Range 12 West.

Q The specific acreage in question in this Hearing is the south half of Section 24 and the Township and Range you just mentioned?

A Yes, sir: that is true.

Q How have you designated the acreage in question on your Exhibit 1?

A The acreage in the south half of Section 24 of Township

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29 North, Range 12 West is outlined in red.

Q What is the significance, Mr. Eaton, of the various colored portions of the acreage within your red boundary?

A These various colors indicate different interests that exist within that south half section of 24.

Q How many separate tracts, area wise, do we find in the south half?

A Geologically, there are actually 8 separate tracts in the south half Section 24. You will note that there are only six colors. That means that there are really 6 basic leases involved.

Q In other words, I see two blue tracts, the ownership under those two blue tracts, although separate, area wise is the same?

A Yes, sir.

Q Mr. Eaton, has Pan American made a diligent effort to voluntarily farm the standard 320 acre units?

A Yes, sir; they have.

Q Have their efforts in this regard been completely successful?

A No, sir; not 100 per cent successful.

Q At the present time, how many outstanding interests do we have?

A There is one outstanding royalty, and one outstanding working interest at the present time.

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Q Now, with respect to the working interests, who have voluntarily agreed to form this unit, have they all agreed that Pan American should be the operator?

A Yes, sir; they have.

Q Is it your recommendation to this Commission that Pan American be designated as operator in the pooling order that we are requesting to be issued?

A Yes, sir. It is my recommendation that Pan American be named operator in such a pooling order.

Q Mr. Eaton, are you recommending to the Commission here, today, that a penal provision be included in this pooling order?

A Yes, sir; I am.

Q What type of recommendation are you making?

A It's my recommendation that a penalty equal to 50 per cent of the drilling and operating costs be assessed against those working interests who elect to pay their share of such costs out of production rather than in cash at the time they are billed for it --

Q In other words, as I understand your recommendation, even a bond consenting working interest owner, a working interest owner that does not sign the unitization agreement, he could still elect to pay in cash, and there would be no penalty?

A That is true, as long as the working interest is willing to pay his share of costs in cash when billed, and not to pay it out of production from the well, then no penalty would be assessed.

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Q And certainly, you are not including in your recommendation that any penalty apply to any royalty owner?

A No, sir, by no means would it ever apply to a royalty owner.

Q Why do you recommend a penalty for a working interest owner who desires to pay his share instead of in cash, out of production?

A In the drilling of any well, there are certain inherent risks involved that make it highly desirable to have each of the working interest owners who are liable for part of those costs to pay in cash at the time billed.

Q Mr. Eaton, when you mentioned inherent risks, it automatically comes to my mind things like blowouts, lost circulation, trouble that had a lot of additional expense to the drilling of a well. Do you have any other type risks than that, other than the ones we normally think of when we start to drill a well?

A Mr. Buell, I believe that any time that any equipment is run into a well there is risk attached to it. By that, I mean, a bit, drill pipe, drill collars, packers, tubing, anything that might be run into a well involves some degree of risk. I might give an example of some of these unusual things that can happen: At the present time, Pan American has a well with which we had no trouble whatsoever until it reached a depth of about 5,000 feet, at which time, a drive shaft or power shaft on the rig, itself, broke. The well was down at that point with drill pipe in the

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hole for about 36 hours while that rig was being repaired. And since that time, or during that time, the drill pipe and drill collar became stuck at the bottom of the hole, and subsequently the pipe shot off, backed off a few hundred feet above TD; and at the present time, we have still not been able to fish that portion of the tube that is still left in the bottom of the hole out. It looks like to me that we will probably wind up abandoning that hole. That is just an example of what can happen, some of the risks involved.

Q And all of that was really due to a minor, expense wise, break in equipment?

A Yes, sir; it certainly had nothing to do with the geology of the area, of the possibility of lost circulation, blow-out, or even a dry hole.

Q Is a penalty provision of the type you have recommended, is it common and customary in the industry among operators, even when they are voluntarily putting their acreage together?

A Yes, sir; it certainly is. Pan American is a party to a number of unit operating agreements in the San Juan Basin Area, some of which Pan American operates, some of which it is a non-operator. Without failure, each of these voluntary unit operating agreements provide for some penalty to be assessed against those who do not elect to share in cash the cost of the development operation. The normal provision in those operating agreements is for 150 per cent recovery. I am familiar with a few of the more



recent ones which provide for 200 per cent recovery.

Q Actually Mr. Eaton, the operating agreement executed by the consenting working interest owners, with respect to this unit, provides for a penalty of 100 per cent if any of the consenting working interest owners elect to pay out of his share of production rather than in cash; am I correct?

A That is quite true. The penalty is a hundred per cent. That means that those that pay in cash actually recover 200 per cent.

Q Where are you recommending the well be located in the south half of 24, Mr. Eaton, to serve this pooled unit?

A The well will be located in the Northwest Quarter, Southwest Quarter of Section 4, or specifically, it will be located 810 feet from the west line, and 1450 feet from the south line of Section 24.

Q Is that an orthodox location under the Basin-Dakota Gas Pool Rules?

A Yes, sir; it is.

Q In your opinion, Mr. Eaton, in this area of the Basin-Dakota Pool, will one well effectively and efficiently drain in excess of 320 acres?

A Yes, sir; it will.

Q So you would then feel that if this acreage in question in the south half of 24 is not pooled and correlative rights have to be protected by drilling more than one well, it would be



economic waste?

A Yes, sir. Certainly more than one well on that half section would result in economic waste. On the other hand, a well is needed on that particular half section to protect correlative rights.

Q Do you base that statement on the fact of the completed Dakota-Gas Wells, according to your Exhibit No. 1, almost surround the south half?

A Yes, sir; I do.

Q So it is then your opinion, is it not, that the recommendation you are making here today the pooling of all the interests in the south half of Section 24 into a standard 320 acre gas unit will protect correlative rights as well as prevent waste?

A Yes, sir; that is my opinion.

Q Do you have anything else that you would like to add, Mr. Eaton?

A No, sir; I don't believe so.

MR. BUELL: That is all that we have at this time, Mr. Chairman.

MR. NUTTER: Are there any questions?

Q (By Mr. Morris) Mr. Eaton, you testified one royalty interest and one working interest is yet outstanding.

A Yes, sir.

Q What is the extent of each of those interests in the 320 acres?

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A The outstanding royalty interest and the working interest both cover the same acreage. That acreage consists of the Northwest Quarter Southeast Quarter, the Northeast Quarter Southwest Quarter, the Southwest Quarter Southwest Quarter, and the west half Southeast Southwest Quarter of Section 24.

Q Is that the red acreage?

A Yes, sir; that is the red acreage, and the green acreage.

Q And who owns those interests, or is it too diversified to give?

A No, sir. I believe I can break that down for you. In the Northwest Quarter Southeast Quarter, the outstanding working interest amounts to a quarter of a four fifths working interest under lease to National Drilling Company. In the remainder of that acreage, the red acreage on Exhibit 1, National Drilling owns a quarter working interest. The royalty interest is somewhat divided. I might sum it up by saying that it is owned by the Crawfords as a group. In addition, the Turner Securities owns a royalty interest under the Northwest Quarter Southeast Quarter, amounting to one fifth of one eighth.

Q Now, it is my understanding that there is litigation pending that may affect certain interests in the south half of Section 24. Are you familiar with that?

A Not to any detail; no, sir. I am aware that there is litigation involved in this acreage.

Q Do you feel that the outcome of that litigation would in



any way affect it, or anyway should affect the order of the Commission that would be entered in this case today?

A No, sir. I believe that regardless of the outcome of that litigation that all interest royalties will be protected by the issuance of a force pooling order. As we mentioned previously, we are not asking for a penalty to be assessed against anyone who will elect to pay his portion of the development and operating costs in cash. We are only asking for a penalty to be assessed against those who elect to pay their portion of the costs out of production from the well; and so if, at any time, a working interest is required through this litigation, then the person acquiring that working interest would have an election to pay at that time with regard to whether he desires to pay in cash or whether he wishes to suffer that penalty.

Q If the well had already been drilled successfully, and there was an election not to pay cash ahead of time, would that in any way affect the amount of risk?

A It would be allocated to that particular proportional interest only in this respect. His risk would already have been taken.

Q That is right; but if that person would not have the election until after the well had been drilled, it might pose a nice problem.

A He would have available a lot more facts with which to work than we do at this time prior to the actual drilling of the

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well, it's true. He could certainly put a pencil to the costs involved with a lot more accuracy than we can by guessing what is going to occur. In fact, I'd say he'd be in a better position.

Q If the Commission entered an order, such as you are requesting, granting a 50 per cent penalty provision to non-consenting interests that do not elect to pay their share in advance, do you feel that it would be fair to assess that penalty to a working interest that did not have the option of making their election until after the well had been drilled?

A Yes, sir; I think that is fair. As I had mentioned before, actually he would be in a very good position because he knows what the actual costs involved are. And if they are excessive, and perhaps he would elect to not pay up in cash, take it out of production. If they are normal, he probably would elect to pay in cash, but at least, he would know what they were, exactly.

Q Mr. Eaton, I don't know whether you ever got around to the point of saying whether you felt there was any dry hole risk in a well to be drilled in the south half of Section 24.

A I don't believe I ever stated whether or not I thought so. For the record, I will state I think the risk is very small for getting an actual dry hole.

Q But, there are other inherent risks?

A Other inherent risks other than actual geology that concern whether or not the well is a dry hole; mechanical risks,



rather than geological risks.

MR. MORRIS: Mr. Examiner, I have a communication that I would like to read parts of into the record at a later time bearing upon the portion of certain royalty interests in the south half of Section 24, for consideration, and the subject of my questions to Mr. Eaton.

MR. NUTTER: Very good.

MR. MORRIS: I have no further questions. Thank you.

MR. NUTTER: Mr. Eaton, you said that Pan American had made a diligent effort to handle that acreage on a community basis. Will you outline those efforts that Pan American has made?

THE WITNESS: Yes, sir. Unit, or communitization agreements have been drawn and submitted to all parties of interest. We have received executed copies, or have indicated that we will, from all owners of interest except this royalty interest and this working interest that I just mentioned.

MR. NUTTER: Does the royalty interest have to be pooled, or is there a pooling clause in the lease?

THE WITNESS: No, sir. It has to be pooled.

MR. NUTTER: The ones that you haven't received the communitization from, have you actually received a negative communication from them?

THE WITNESS: We have received a negative communication from the royalty owner. We have received no notice whatsoever from the working interests, although the working interest has been



given ample time to make a reply.

Q Now, this working interest is that quarter interest that you said was owned by National Drilling Company?

A National Drilling Company.

Q And you have not received a reply from them?

A No, sir.

Q Has any effort been made to contact them personally?

A Yes, sir; several times.

Q But they just haven't made up their mind, yet?

A Just move slow.

Q I see. Now, how much of the working interest, here, does Pan American actually own at this time, themselves?

A Pan American owns a working interest under -- Would it be permissible for me to just name the color?

A Yes, because the colors are part of the record, too.

A Pan American owns working interests under all tracts except those colored blue and yellow; and in addition to that, Pan American is designated operator of that Quarter Quarter Section being Northwest Southwest Quarter. Pan American does not actually own the working interests under that particular tract.

Q You said Pan American owns the working interest, however, they don't own 100 per cent of the working interest in the red, do they?

A No, sir; nor in the green.

MR. BUELL: He said, "We own a working interest."



Q (By Mr. Nutter) Now, you own 100 per cent of the working interest in the brown?

A Yes, sir; and Pan American owns 100 per cent of the working interest in the purple, that is it. Would you like for me to go to each one of these tracts. I'll tell you exactly what my records indicate. What Pan American owns, in some cases, is a little bit involved.

A Well, I think we have got the description of what we want here. Now Mr. Eaton, the New Mexico statutes provide that the Commission can on a forced pooling order provide or pay 50 per cent penalty for the risk involved. However, wouldn't you think that that risk that is involved could also include the risk of a dry hole?

A Yes, sir; I certainly do.

Q With this 50 per cent?

A Yes, sir; I certainly do.

Q Now, I have noticed that the weather bureau in some cities has been getting pretty classy in making their predictions of rain or shine; and they will say, "It has a 10 per cent chance, or a 90 per cent chance that it won't rain." What is your estimate in per cent of chances that you will get a producing well here?

A I am not the weather bureau, but I will say this: The chances are very good that we will get a producing well. As you can see from Exhibit 1, the Dakota Well is in practically all

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directions from that location. In fact, there is one on the north half of Section 4. In addition, a well that is drilling, and data on which will be available prior to the time that this well is drilled, I am sure, is Pan American Gallegos Canyon Unit No. 93, which is in the Southwest Quarter Northwest Quarter of Section 36, right in Township 29 North, Range 12 West; so by the time we get ready to drill this well in the south half of Section 24, we'll have total wells, practically all the way around it and adjacent to Section 24.

Q So, you would say the weather outlook here is favorable?

A Yes, sir; I would say that.

Q You cited this one incident where the shaft on the drilling rig broke, or something, and the pipe got stuck in the hole.

A Yes.

Q Do things like this happen actually very often, Mr. Eaton?

A No, not too frequently. It's just one of those things that can happen. I cited it as an example of what risks are involved when material or equipment of any kind is run into a hole, but it doesn't necessarily have to be the risk of a geologic dry hole, but there are mechanical aspects of the actual drilling and completion operations that are also risky. All things don't occur often.

Q Well, do you think that if the risk of a dry hole is



eliminated that the risk of these mechanical failures is such that a 50 per cent penalty is appropriate?

A Yes, sir; for the reason: We are not asking that a penalty be assessed against any one working interest unless he elects to ride the well down and take his, or pay his part out of production from the well. If he's willing to pay up in cash at the time drilled, regardless of whether the well has been drilled or is in the prospective stage of drilling, and pays in cash, then no penalty would be assessed against that person. Only in the case that he intends to ride the well down and pay his part of production from the well do I think that a penalty is justified.

Q And this 50 per cent penalty you feel is justified for mechanical risk.

A Yes, sir.

Q And eliminates the possibility of a dry hole?

A Yes, sir. It is a common industry use, too. It certainly is not an unusual thing that we are recommending here. It's a portion of almost every unit operating agreement, whether it be for a proproation unit or a federal unit covering many sections such as, for example, the Gallegos Canyon Unit. The operating agreement for Gallegos Canyon Unit provides for a 150 per cent recovery for those who don't consent and elect to pay this cash at the time billed.

Q Well, at the time the Gallegos Canyon Unit was written,



there was probably some geological risk, wasn't there?

A Yes, sir; but the provision regarding the penalty still prevails even today, when geological risk is no greater than in the case of the well in the south half of Section 24.

MR. NUTTER: Are there any further questions?

MR. MORRIS: One more question.

Q (By Mr. Morris) Mr. Eaton, do you have a location in mind for the well that will be drilled in this Unit?

A Yes, sir. It will be 810 feet from the west line and 1450 feet from the south line.

Q 810 from the west line and --

A 1450 --

Q -- from the --

A -- line.

Q Thank you, sir.

MR. NUTTER: If there are no further questions --

MR. BUELL: I have two.

MR. NUTTER: Mr. Buell.

Q (By Mr. Buell) Mr. Eaton, I want the record to be crystal clear in this regard: With respect to any party who requires, subsequent to the drilling of this well, a working interest, either throughout or in any way, any factors that have occurred, or any contingencies that have become a reality, all of those factors will inure to the benefit of this after acquiring working interest ownership.



A Yes, sir.

Q And I feel this way: Unfortunately, in my opinion, that is the case.

A Yes, sir.

Q Mr. Eaton, we talked a lot about a risk and penalty for a dry hole. In the event there is a dry hole, is there any penalty?

A No, sir.

MR. BUELL: That is all.

Q (By Mr. Nutter) Mr. Eaton, what is your estimated cost for drilling this well?

A About \$70,000.00 drilling equipment.

Q Has a AFE already been prepared on this well?

A Yes, sir.

Q And the total is approximately \$70,000.00?

A Yes, sir. Actually, I believe the drilling costs estimated about \$65,000.00, but there will be a five to \$6,000.00 lease equipment involved.

MR. NUTTER: Are there any further questions of Mr. Eaton? You may be excused.

Mr. Morris, do you have something?

MR. MORRIS: Yes, sir; I do. I have a letter from Mr. William J. Cooley, attorney for the Crawford Interest that has been mentioned today, and I would like to offer his letter as part of the record in this case.

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To paraphrase, summarize Mr. Cooley's letter: He refers to a lawsuit presently pending against Cause No. 4687 Civil, in the United States District Court for the District of New Mexico, concerning the acreage colored red and green on Pan American's Exhibit. The Crawford Interests apparently are contesting the Pan American ownership of the lease on that acreage, and to read a paragraph of Mr. Cooley's letter:

"As attorney for James E. Crawford, et al, I am authorized to state that my clients have no objection to a force pooling order on the south half of Section 24, provided said order is conditioned upon the outcome of said United States District Court Case No. 4687, and provided further that your order does not contain any risk penalty provision."

I will offer the letter as part of the record.

MR. NUTTER: Does anyone have anything further they wish to offer in Case 2346?

MR. BUELL: Mr. Examiner, I might just state in closing that I don't see anything inconsistent in Mr. Cooley's letter with regard to his clients, the Crawfords, and our recommendation. In the event they would prevail in this litigation and become a working interest owner, if they elect to pay in cash, there will be no penalty. They will have the same option that all the current working interest owners have either to elect to pay in cash or assume a penalty and pay out of production. They will have the benefit in all probability. I do not know how long it

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will be before the suit is settled, but they will have the benefit of any after-acquired billing to the drilling of the well. They will be in a better position to evaluate their working position than any of us are now. So, there is no way, in my opinion, that they can be adversely affected by the order we are asking here today.

MR. NUTTER: When is Pan American planning to drill the well?

MR. BUELL: Mr. Eaton, do you have any information on that?

MR. EATON: No, sir; I sure don't.

MR. BUELL: I think we will drill it immediately, Mr. Examiner. Other than offering our Exhibit 1 formally, that is all I have.

MR. NUTTER: Pan American's Exhibit 1 will be entered into evidence.

(Whereupon Pan American's Exhibit 1 received in evidence.)

MR. NUTTER: Does anyone have anything further in this case? We will take the case under advisement.

(Whereupon the Hearing of Case No. 2346 was concluded.)

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was examined and testified as follows:

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BY MR. BUELL:

Q Mr. Eaton, would you state your complete name, by whom

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you are employed, in what capacity, and at what location, please.

A My name is George W. Eaton, Jr.; and I am employed by Pan American Petroleum Corporation in Farmington, New Mexico; and I am Senior Petroleum Engineer.

Q Mr. Eaton, you have testified at prior Commission Hearings and your qualifications as a Petroleum Engineer are a matter of public record, are they not?

A Yes, sir; they are.

(Whereupon Petitioner's Exhibit 1 marked for identification.)

Q (By Mr. Buell) Mr. Eaton, let me direct your attention, now, to what is marked as Pan American's Exhibit 1. What does that Exhibit reflect?

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A Yes, sir: that is true.

Q How have you designated the acreage in question on your Exhibit 1?

A The acreage in the south half of Section 24 of Township



29 North, Range 12 West is outlined in red.

Q What is the significance, Mr. Eaton, of the various colored portions of the acreage within your red boundary?

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Q In other words, I see two blue tracts, the ownership under those two blue tracts, although separate, area wise is the same?

A Yes, sir.

Q Mr. Eaton, has Pan American made a diligent effort to voluntarily farm the standard 320 acre units?

A Yes, sir; they have.

Q Have their efforts in this regard been completely successful?

A No, sir; not 100 per cent successful.

Q At the present time, how many outstanding interests do we have?

A There is one outstanding royalty, and one outstanding working interest at the present time.



Q Now, with respect to the working interests, who have voluntarily agreed to form this unit, have they all agreed that Pan American should be the operator?

A Yes, sir; they have.

Q Is it your recommendation to this Commission that Pan American be designated as operator in the pooling order that we are requesting to be issued?

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Q In other words, as I understand your recommendation, even a bond consenting working interest owner, a working interest owner that does not sign the unitization agreement, he could still elect to pay in cash, and there would be no penalty?

A That is true, as long as the working interest is willing to pay his share of costs in cash when billed, and not to pay it out of production from the well, then no penalty would be assessed.

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Q And certainly, you are not including in your recommendation that any penalty apply to any royalty owner?

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Q Mr. Eaton, when you mentioned inherent risks, it automatically comes to my mind things like blowouts, lost circulation, trouble that had a lot of additional expense to the drilling of a well. Do you have any other type risks than that, other than the ones we normally think of when we start to drill a well?

A Mr. Buell, I believe that any time that any equipment is run into a well there is risk attached to it. By that, I mean, a bit, drill pipe, drill collars, packers, tubing, anything that might be run into a well involves some degree of risk. I might give an example of some of these unusual things that can happen: At the present time, Pan American has a well with which we had no trouble whatsoever until it reached a depth of about 5,000 feet, at which time, a drive shaft or power shaft on the rig, itself, broke. The well was down at that point with drill pipe in the



hole for about 36 hours while that rig was being repaired. And since that time, or during that time, the drill pipe and drill collar became stuck at the bottom of the hole, and subsequently the pipe shot off, backed off a few hundred feet above TD; and at the present time, we have still not been able to fish that portion of the tube that is still left in the bottom of the hole out. It looks like to me that we will probably wind up abandoning that hole. That is just an example of what can happen, some of the risks involved.

Q And all of that was really due to a minor, expense wise, break in equipment?

A Yes, sir; it certainly had nothing to do with the geology of the area, of the possibility of lost circulation, blow-out, or even a dry hole.

Q Is a penalty provision of the type you have recommended, is it common and customary in the industry among operators, even when they are voluntarily putting their acreage together?

A Yes, sir; it certainly is. Pan American is a party to a number of unit operating agreements in the San Juan Basin Area, some of which Pan American operates, some of which it is a non-operator. Without failure, each of these voluntary unit operating agreements provide for some penalty to be assessed against those who do not elect to share in cash the cost of the development operation. The normal provision in those operating agreements is for 150 per cent recovery. I am familiar with a few of the more



recent ones which provide for 200 per cent recovery.

Q Actually Mr. Eaton, the operating agreement executed by the consenting working interest owners, with respect to this unit, provides for a penalty of 100 per cent if any of the consenting working interest owners elect to pay out of his share of production rather than in cash; am I correct?

A That is quite true. The penalty is a hundred per cent. That means that those that pay in cash actually recover 200 per cent.

Q Where are you recommending the well be located in the south half of 24, Mr. Eaton, to serve this pooled unit?

A The well will be located in the Northwest Quarter, Southwest Quarter of Section 4, or specifically, it will be located 810 feet from the west line, and 1450 feet from the south line of Section 24.

Q Is that an orthodox location under the Basin-Dakota Gas Pool Rules?

A Yes, sir; it is.

Q In your opinion, Mr. Eaton, in this area of the Basin-Dakota Pool, will one well effectively and efficiently drain in excess of 320 acres?

A Yes, sir; it will.

Q So you would then feel that if this acreage in question in the south half of 24 is not pooled and correlative rights have to be protected by drilling more than one well, it would be



economic waste?

A Yes, sir. Certainly more than one well on that half section would result in economic waste. On the other hand, a well is needed on that particular half section to protect correlative rights.

Q Do you base that statement on the fact of the completed Dakota-Gas Wells, according to your Exhibit No. 1, almost surround the south half?

A Yes, sir; I do.

Q So it is then your opinion, is it not, that the recommendation you are making here today the pooling of all the interests in the south half of Section 24 into a standard 320 acre gas unit will protect correlative rights as well as prevent waste?

A Yes, sir; that is my opinion.

Q Do you have anything else that you would like to add, Mr. Eaton?

A No, sir; I don't believe so.

MR. BUELL: That is all that we have at this time, Mr. Chairman.

MR. NUTTER: Are there any questions?

Q (By Mr. Morris) Mr. Eaton, you testified one royalty interest and one working interest is yet outstanding.

A Yes, sir.

Q What is the extent of each of those interests in the 320 acres?



A The outstanding royalty interest and the working interest both cover the same acreage. That acreage consists of the Northwest Quarter Southeast Quarter, the Northeast Quarter Southwest Quarter, the Southwest Quarter Southwest Quarter, and the west half Southeast Southwest Quarter of Section 24.

Q Is that the red acreage?

A Yes, sir; that is the red acreage, and the green acreage.

Q And who owns those interests, or is it too diversified to give?

A No, sir. I believe I can break that down for you. In the Northwest Quarter Southeast Quarter, the outstanding working interest amounts to a quarter of a four fifths working interest under lease to National Drilling Company. In the remainder of that acreage, the red acreage on Exhibit 1, National Drilling owns a quarter working interest. The royalty interest is somewhat divided. I might sum it up by saying that it is owned by the Crawfords as a group. In addition, the Turner Securities owns a royalty interest under the Northwest Quarter Southeast Quarter, amounting to one fifth of one eighth.

Q Now, it is my understanding that there is litigation pending that may affect certain interests in the south half of Section 24. Are you familiar with that?

A Not to any detail; no, sir. I am aware that there is litigation involved in this acreage.

Q Do you feel that the outcome of that litigation would in

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any way affect it, or anyway should affect the order of the Commission that would be entered in this case today?

A No, sir. I believe that regardless of the outcome of that litigation that all interest royalties will be protected by the issuance of a force pooling order. As we mentioned previously, we are not asking for a penalty to be assessed against anyone who will elect to pay his portion of the development and operating costs in cash. We are only asking for a penalty to be assessed against those who elect to pay their portion of the costs out of production from the well; and so if, at any time, a working interest is required through this litigation, then the person acquiring that working interest would have an election to pay at that time with regard to whether he desires to pay in cash or whether he wishes to suffer that penalty.

Q If the well had already been drilled successfully, and there was an election not to pay cash ahead of time, would that in any way affect the amount of risk?

A It would be allocated to that particular proportional interest only in this respect. His risk would already have been taken.

Q That is right; but if that person would not have the election until after the well had been drilled, it might pose a nice problem.

A He would have available a lot more facts with which to work than we do at this time prior to the actual drilling of the

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well, it's true. He could certainly put a pencil to the costs involved with a lot more accuracy than we can by guessing what is going to occur. In fact, I'd say he'd be in a better position.

Q If the Commission entered an order, such as you are requesting, granting a 50 per cent penalty provision to non-consenting interests that do not elect to pay their share in advance, do you feel that it would be fair to assess that penalty to a working interest that did not have the option of making their election until after the well had been drilled?

A Yes, sir; I think that is fair. As I had mentioned before, actually he would be in a very good position because he knows what the actual costs involved are. And if they are excessive, and perhaps he would elect to not pay up in cash, take it out of production. If they are normal, he probably would elect to pay in cash, but at least, he would know what they were, exactly.

Q Mr. Eaton, I don't know whether you ever got around to the point of saying whether you felt there was any dry hole risk in a well to be drilled in the south half of Section 24.

A I don't believe I ever stated whether or not I thought so. For the record, I will state I think the risk is very small for getting an actual dry hole.

Q But, there are other inherent risks?

A Other inherent risks other than actual geology that concern whether or not the well is a dry hole; mechanical risks,



rather than geological risks.

MR. MORRIS: Mr. Examiner, I have a communication that I would like to read parts of into the record at a later time bearing upon the portion of certain royalty interests in the south half of Section 24, for consideration, and the subject of my questions to Mr. Eaton.

MR. NUTTER: Very good.

MR. MORRIS: I have no further questions. Thank you.

MR. NUTTER: Mr. Eaton, you said that Pan American had made a diligent effort to handle that acreage on a community basis. Will you outline those efforts that Pan American has made?

THE WITNESS: Yes, sir. Unit, or communitization agreements have been drawn and submitted to all parties of interest. We have received executed copies, or have indicated that we will, from all owners of interest except this royalty interest and this working interest that I just mentioned.

MR. NUTTER: Does the royalty interest have to be pooled, or is there a pooling clause in the lease?

THE WITNESS: No, sir. It has to be pooled.

MR. NUTTER: The ones that you haven't received the communitization from, have you actually received a negative communication from them?

THE WITNESS: We have received a negative communication from the royalty owner. We have received no notice whatsoever from the working interests, although the working interest has been



given ample time to make a reply.

Q Now, this working interest is that quarter interest that you said was owned by National Drilling Company?

A National Drilling Company.

Q And you have not received a reply from them?

A No, sir.

Q Has any effort been made to contact them personally?

A Yes, sir; several times.

Q But they just haven't made up their mind, yet?

A Just move slow.

Q I see. Now, how much of the working interest, here, does Pan American actually own at this time, themselves?

A Pan American owns a working interest under -- Would it be permissible for me to just name the color?

A Yes, because the colors are part of the record, too.

A Pan American owns working interests under all tracts except those colored blue and yellow; and in addition to that, Pan American is designated operator of that Quarter Quarter Section being Northwest Southwest Quarter. Pan American does not actually own the working interests under that particular tract.

Q You said Pan American ownsthe working interest, however, they don't own 100 per cent of the working interest in the red, do they?

A No, sir; nor in the green.

MR. BUELL: He said, "We own a working interest."

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Q (By Mr. Nutter) Now, you own 100 per cent of the working interest in the brown?

A Yes, sir; and Pan American owns 100 per cent of the working interest in the purple, that is it. Would you like for me to go to each one of these tracts. I'll tell you exactly what my records indicate. What Pan American owns, in some cases, is a little bit involved.

A Well, I think we have got the description of what we want here. Now Mr. Eaton, the New Mexico statutes provide that the Commission can on a forced pooling order provide or pay 50 per cent penalty for the risk involved. However, wouldn't you think that that risk that is involved could also include the risk of a dry hole?

A Yes, sir; I certainly do.

Q With this 50 per cent?

A Yes, sir; I certainly do.

Q Now, I have noticed that the weather bureau in some cities has been getting pretty classy in making their predictions of rain or shine; and they will say, "It has a 10 per cent chance, or a 90 per cent chance that it won't rain." What is your estimate in per cent of chances that you will get a producing well here?

A I am not the weather bureau, but I will say this: The chances are very good that we will get a producing well. As you can see from Exhibit 1, the Dakota Well is in practically all

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directions from that location. In fact, there is one on the north half of Section 4. In addition, a well that is drilling, and data on which will be available prior to the time that this well is drilled, I am sure, is Pan American Gallegos Canyon Unit No. 93, which is in the Southwest Quarter Northwest Quarter of Section 36, right in Township 29 North, Range 12 West; so by the time we get ready to drill this well in the south half of Section 24, we'll have total wells, practically all the way around it and adjacent to Section 24.

Q So, you would say the weather outlook here is favorable?

A Yes, sir; I would say that.

Q You cited this one incident where the shaft on the drilling rig broke, or something, and the pipe got stuck in the hole.

A Yes.

Q Do things like this happen actually very often, Mr. Eaton?

A No, not too frequently. It's just one of those things that can happen. I cited it as an example of what risks are involved when material or equipment of any kind is run into a hole, but it doesn't necessarily have to be the risk of a geologic dry hole, but there are mechanical aspects of the actual drilling and completion operations that are also risky. All things don't occur often.

Q Well, do you think that if the risk of a dry hole is



eliminated that the risk of these mechanical failures is such that a 50 per cent penalty is appropriate?

A Yes, sir; for the reason: We are not asking that a penalty be assessed against any one working interest unless he elects to ride the well down and take his, or pay his part out of production from the well. If he's willing to pay up in cash at the time drilled, regardless of whether the well has been drilled or is in the prospective stage of drilling, and pays in cash, then no penalty would be assessed against that person. Only in the case that he intends to ride the well down and pay his part of production from the well do I think that a penalty is justified.

Q And this 50 per cent penalty you feel is justified for mechanical risk.

A Yes, sir.

Q And eliminates the possibility of a dry hole?

A Yes, sir. It is a common industry use, too. It certainly is not an unusual thing that we are recommending here. It's a portion of almost every unit operating agreement, whether it be for a propration unit or a federal unit covering many sections such as, for example, the Gallegos Canyon Unit. The operating agreement for Gallegos Canyon Unit provides for a 150 per cent recovery for those who don't consent and elect to pay this cash at the time billed.

Q Well, at the time the Gallegos Canyon Unit was written,



there was probably some geological risk, wasn't there?

A Yes, sir; but the provision regarding the penalty still prevails even today, when geological risk is no greater than in the case of the well in the south half of Section 24.

MR. NUTTER: Are there any further questions?

MR. MORRIS: One more question.

Q (By Mr. Morris) Mr. Eaton, do you have a location in mind for the well that will be drilled in this Unit?

A Yes, sir. It will be 810 feet from the west line and 1450 feet from the south line.

Q 810 from the west line and --

A 1450 --

Q -- from the --

A -- line.

Q Thank you, sir.

MR. NUTTER: If there are no further questions --

MR. BUELL: I have two.

MR. NUTTER: Mr. Buell.

Q (By Mr. Buell) Mr. Eaton, I want the record to be crystal clear in this regard: With respect to any party who requires, subsequent to the drilling of this well, a working interest, either throughout or in any way, any factors that have occurred, or any contingencies that have become a reality, all of those factors will inure to the benefit of this after acquiring working interest ownership.



A Yes, sir.

Q And I feel this way: Unfortunately, in my opinion, that is the case.

A Yes, sir.

Q Mr. Eaton, we talked a lot about a risk and penalty for a dry hole. In the event there is a dry hole, is there any penalty?

A No, sir.

MR. BUELL: That is all.

Q (By Mr. Nutter) Mr. Eaton, what is your estimated cost for drilling this well?

A About \$70,000.00 drilling equipment.

Q Has a AFE already been prepared on this well?

A Yes, sir.

Q And the total is approximately \$70,000.00?

A Yes, sir. Actually, I believe the drilling costs estimated about \$65,000.00, but there will be a five to \$6,000.00 lease equipment involved.

MR. NUTTER: Are there any further questions of Mr. Eaton? You may be excused.

Mr. Morris, do you have something?

MR. MORRIS: Yes, sir; I do. I have a letter from Mr. William J. Cooley, attorney for the Crawford Interest that has been mentioned today, and I would like to offer his letter as part of the record in this case.



To paraphrase, summarize Mr. Cooley's letter: He refers to a lawsuit presently pending against Cause No. 4687 Civil, in the United States District Court for the District of New Mexico, concerning the acreage colored red and green on Pan American's Exhibit. The Crawford Interests apparently are contesting the Pan American ownership of the lease on that acreage, and to read a paragraph of Mr. Cooley's letter:

"As attorney for James E. Crawford, et al, I am authorized to state that my clients have no objection to a force pooling order on the south half of Section 24, provided said order is conditioned upon the outcome of said United States District Court Case No. 4687, and provided further that your order does not contain any risk penalty provision."

I will offer the letter as part of the record.

MR. NUTTER: Does anyone have anything further they wish to offer in Case 2346?

MR. BUELL: Mr. Examiner, I might just state in closing that I don't see anything inconsistent in Mr. Cooley's letter with regard to his clients, the Crawfords, and our recommendation. In the event they would prevail in this litigation and become a working interest owner, if they elect to pay in cash, there will be no penalty. They will have the same option that all the current working interest owners have either to elect to pay in cash or assume a penalty and pay out of production. They will have the benefit in all probability. I do not know how long it

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will be before the suit is settled, but they will have the benefit of any after-acquired billing to the drilling of the well. They will be in a better position to evaluate their working position than any of us are now. So, there is no way, in my opinion, that they can be adversely affected by the order we are asking here today.

MR. NUTTER: When is Pan American planning to drill the well?

MR. BUELL: Mr. Eaton, do you have any information on that?

MR. EATON: No, sir; I sure don't.

MR. BUELL: I think we will drill it immediately, Mr. Examiner. Other than offering our Exhibit 1 formally, that is all I have.

MR. NUTTER: Pan American's Exhibit 1 will be entered into evidence.

(Whereupon Pan American's Exhibit 1 received in evidence.)

MR. NUTTER: Does anyone have anything further in this case? We will take the case under advisement.

(Whereupon the Hearing of Case No. 2346 was concluded.)

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STATE OF NEW MEXICO)
) ss.
COUNTY OF BERNALILLO)

I, MICHAEL P. HALL, Court Reporter, do hereby certify that the foregoing and attached transcript of proceedings before the New Mexico Oil Conservation Commission at Santa Fe, New Mexico, is a true and correct record to the best of my knowledge, skill and ability.

IN WITNESS WHEREOF, I have affixed my hand and notary seal this 9th day of August, 1961.

Michael P. Hall

Court Reporter - Notary Public

My Commission expires:
June 20, 1965.

I do hereby certify that the foregoing is a complete record of the proceedings in the Examiner hearing of Case No. 2346 heard by me on 8/9, 1961.
[Signature], Examiner
New Mexico Oil Conservation Commission

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