Santa Fe Energy Operating Partners, L.P.

Santa Fe Pacific Exploration Company
Managing General Partner

December 8, 1989

Exxon Company, USA
P.O. Box 1600
Midland, Texas 79702-1600

ATTN: Robert C. Olsen
Division Manager
Southwestern Prod. Div.

Re: Forced Pooling Hearings

Dear Mr. Olsen:

During cross-examination of our land witness at the hearing of our competing applications in Case Nos. 9832 and 9797 before the New Mexico Oil Conservation Division on November 29, 1989, your counsel, Mr. Kellahin, commenced inquiry into an area which we feel compelled to call to your attention.

Mr. Kellahin inquired into the legal makeup of Santa Fe Operating Partners, L.P., and Santa Fe Pacific Exploration Company, its managing general partner. The implication of Mr. Kellahin's inquiry was that Santa Fe Operating Partners, L.P. was a less than responsible entity whose apparent interest in drilling the Escalante Fed Com 20 No. 1 Well was motivated by considerations other than sincere efforts to drill an economic producing well.

As Exxon well knows, Santa Fe Operating Partners and its affiliated entities have not attained their status as one of the largest independent oil and gas producers in the United States through inadvertence and happenstance. We have been in business since 1897 and operate in 17 states and the Gulf of Mexico, producing 53,000 barrels of oil per day and 83,000 MCF of gas per day as of 1988. Santa Fe continues to aggressively explore for commercial oil and gas deposits.

Ordinarily we would not raise this issue. However, in a prior hearing before the Oil Conservation Division where Santa Fe Operating Partners, L.P. was involved against Bass Enterprises in Case No. 9528, this very issue was raised by Mr. Kellahin and was subsequently settled by an apology from Bass and instructions from Bass to Mr. Kellahin to also apologize to Santa Fe Operating Partners. We strongly feel that Mr. Kellahin's second attempt to attribute bad faith or illegal activity to Santa Fe Operating Partners transcends legitimate ends. We believe it would be appropriate that you would instruct Mr. Kellahin in a similar manner.

While this type of inquiry may have some relevancy since compulsory pooling hearings do deal with well costs and applicant's financial ability to advance such costs, we strongly protest the implication attributed by Mr.

Permian Basin District
500 W. Illinois
Suite 500
Midland, Texas 79701
915/687-3551

Kellahin to Santa Fe Operating Partners, L.P. and we demand that, should Exxon and Santa Fe Operating Partners be involved in future hearings before the Oil Conservation Division, that this irrelevant accusation not be raised. If it is raised, then you are hereby notified that Santa Fe Operating Partners may take such legal action as is necessary to redress its legal remedies.

Finally, we do hope that we can put this issue behind us, and we look forward to working with Exxon on joint projects which will benefit our mutual interest.

Sincerely yours,

SANTA FE ENERGY OPERATING PARTNERS, L.P.
By: Santa Fe Pacific Exploration Company,
Managing General Partner

By: DB Kilpatrick
D. B. Kilpatrick
Production Manager

EP/efw

cc: L. Bryant Williams, Jr. (Exxon)
Manager Western Expl. Div.

Brockman King (Exxon)
Prod. Land Coordination

W. Thomas Kellahin
Kellahin, Kellahin & Aubrey

William LeMay
Oil Conservation Div.
Chairman & Director

EFW790

EXXON COMPANY, U.S.A.

POST OFFICE BOX 1600 • MIDLAND, TEXAS 79702-1600

PRODUCTION DEPARTMENT
SOUTHWESTERN DIVISION

December 13, 1989

NMOCD Cases 9832 and 9797
Section 20, T-23-S, R-25-E
Eddy County, New Mexico

Mr. Michael E. Stogner
New Mexico Oil Conservation Division
State Land Office Bldg.
310 Old Santa Fe Trail
Santa Fe, New Mexico

Dear Mr. Stogner:

On December 13, 1989, I spoke to Armando Lopez with the Bureau of Land Management (BLM) in Roswell. He indicated that he had been contacted by Santa Fe Operating Partners, L.P. ("Santa Fe") regarding the orientation of a half-section spacing unit in Section 20. I explained to him that Section 20 was comprised of an Amoco south half Federal lease, a Santa Fe quarter section lease (NW/4NE/4) and an Exxon federal lease in the remainder of the north half. I explained that all proposed well locations were in the north half of Section 20 and asked if the BLM had any objection to dedicating the east half of Section 20 to the first well to be drilled on that section. He said that since communitization would be required for any well drilled in the north half, the BLM had no preference for orientation of the half-section unit. He said that when he spoke with Santa Fe he was unaware that communitization would be required for a north half-section unit.

Sincerely,

William T. Duncan Jr.

William T. Duncan Jr.

WTD:bcm

Exxon Post Hearing Exhibit 1

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 EXXON CORPORATION FOR COMPULSORY POOLING AND AN UNORTHODOX WELL LOCATION, EDDY COUNTY, NEW MEXICO	CASE 9832
APPLICATION OF SANTA FE ENERGY OPERATING PARTNERS, L. P., FOR COMPULSORY POOLING AND A NON-STANDARD GAS PRORATION UNIT, EDDY COUNTY, NEW MEXICO	CASE 9797

HEARING MEMORANDUM
EXXON CORPORATION

This matter is currently pending decision before the Hearing Examiner of the New Mexico Oil Conservation Division as a result of a hearing held on November 29, 1989.

The Examiner has directed the parties to submit memorandums on the legal issue of State jurisdiction in oil and gas regulatory matters on federal public domain lands presented at the hearing in this case by December 19, 1989. Exxon Corporation ("Exxon") submits this Hearing Memorandum in response to the Examiner's request.

BACKGROUND

Santa Fe Energy Operating Partners, L.P. ("Santa Fe") owns the fee leasehold in the NW/4NE/4 Section 20, T.23 S., R.25 E., N.M.P.M., Eddy County, New Mexico. Exxon owns a federal lease covering the remainder of the N/2 of Section 20. Amoco Production Company ("Amoco") owns a federal lease covering the S/2 of Section 20. Amoco failed to appear at the hearing in this matter either in support of Exxon or Santa Fe.

Exxon seeks an order pooling all uncommitted mineral interests from the top of the Wolfcamp formation to the base of the Morrow formation underlying the E/2 of Section 20, for a non-standard 301.11 acre gas spacing and proration unit for any and all formations and/or pools spaced on 320-acre spacing and for an exemption from the Special Rules and Regulations governing the Rock Tank Upper and Lower Morrow Gas Pools as promulgated by the Division Order No. R-3452, as amended. This proposed unit is to be dedicated to a well to be drilled at an unorthodox gas well location 1500 feet from the North line and 1100 feet from the East line of Section 20.

Santa Fe seeks an order pooling all mineral interest from the surface to the base of the Morrow formation underlying the N/2 of Section 20 with a well to be drilled at a location 1980 feet from the North line and 1980 feet from the West line within Section 20.

Both Santa Fe and Exxon presented substantial geologic evidence that the NE/4 of Section 20 was the best quarter section in which to locate the initial well. However, during the hearing, Santa Fe contended that Exxon's application must be denied by the Oil Conservation Division ("Division") because the BLM in exercising its federal jurisdiction would not approve the E/2 orientation because of 43 CFR Sec. 3105.2-2 and would not approve the surface location because it was in a draw and exposed to flooding. (See Santa Fe Exhibit No. 2)

Based upon Santa Fe's contentions, the Hearing Examiner perceived that this case represented an example of conflicting federal and state regulatory activity and directed counsel for both parties to prepare a Memorandum to assist the Examiner in resolving this matter.

POST HEARING EVIDENCE

Subsequent to the hearing Exxon has examined the contentions expressed by Santa Fe at the hearing and found them to be wrong.

Contrary to the position of Santa Fe, Exxon has determined that Mr. Armando Lopez of the BLM will approve the communitization of the E/2 of the section despite the fact that it will consist of portions of two federal leases and a fee lease. (See Exxon Post Hearing Exhibit No. 1 attached)

In addition, Mr. Barry Hunt, the natural resources specialist for the BLM, has approved the surface use of an area within a 400-500 foot diameter circle immediately adjacent to the location proposed by Exxon for the well location despite Santa Fe's contention that any location in the NE/4 would not be approved by the BLM. (See Exxon Post Hearing Exhibit No. 2 attached)

DISCUSSION

Because Santa Fe's assertions at the hearing are not true, the Examiner need not attempt to resolve this case as if it were a conflict between the OCD and BLM. However, to aide the Examiner in understanding the legal framework within which he must decide such matters this Memorandum is provided.

It should be understood that this Memorandum is not intended to address each and every possible area of potential conflict between the OCD and the BLM nor is it an exhaustive analysis of the State v. Federal regulatory activities over oil and gas activities conducted on federal

leases in New Mexico. Finally, this Memorandum is not intended to be a position paper of Exxon Corporation. It is our intent to simply provide a general understanding of the legal background in which the Examiner has discretion to decide this case.

It is well founded in law that the mineral estate is the dominant estate over the surface estate.[1] However, this case cannot be resolved by simply finding that topographical surface constraints cannot be used to defeat the best development of the minerals. The BLM within the context of this case is more than simply the surface owner or a lessor-royalty owner. The federal government has certain jurisdiction over the oil and gas activities conducted on federal lands. That federal jurisdiction does not preclude the State of New Mexico through the OCD from regulating those same activities even if on federal lands.

The property clause of the Constitution authorizes Congress to dispose of and make all necessary rules and regulations in respect to public lands. Congressional power over oil and gas development on federal lands was exercised

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1. J.S. Lowe, Oil and Gas Law at 33 (1983); Williams and Meyers, Oil and Gas Law Sec. 2-18-9

with the adoption of the Mineral Leasing Act of 1920 and several other laws governing environmental protection and special leasing procedures.[2]

While not disputing the power of Congress to regulate oil and gas activities on public lands in this manner, most western states including New Mexico have conservation laws which assume the existence of concurrent jurisdiction over public lands. New Mexico makes no distinction between public and private lands in its conservation statutes.[3]

The supremacy clause of the U.S. Constitution requires that state law give way to superior federal law only where the state law is in actual direct conflict with a properly adopted federal law or where the state law is in conflict with the objectives of the federal law.[4]

The subject case does not present such a direct conflict. Rather, as is true of most conflicts between state and federal law the potential conflict is much more subtle because of the common concerns shared by both federal

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2. Ebner, State and Local Regulation of Activities on Federal Oil and Gas Leases, in Law of Federal Oil and Gas Leases at 24-10 (1989) (hereinafter cited as "Law of Federal Oil and Gas Leases").

3. N.M. Stat. Ann. Sec. 70-2-6 (1978); Law of Federal Oil and Gas Leases at 24-11.

4. Law of Federal Oil and Gas Leases at 21-13.

and state governments in respect to conservation and the protection of public health and safety. We must, therefore, look to see how both the state and federal government attempt to exercise their respective authority towards the same goal.

The long history of cooperation between the OCD and the BLM with respect to oil and gas operations on federal cases in New Mexico has averted many potential regulatory conflicts. For example, the BLM has acquiesced in the OCD's exercise of jurisdiction over matters relating to the location of wells, well spacing, the establishment of drilling units, and limiting the rate of development and production. The BLM also recognizes the OCD compulsory pooling orders in lieu of communitization of tracts within a spacing unit which includes federal leases.

In addition, BLM officials continue to appear at OCD hearings in order that the BLM's views might be considered in the formulation of State OCD orders, rules and decisions. The joint efforts of the agencies in developing the Oil-Potash Rules is characteristic of the cooperation between them.

Further, the Mineral Leasing Act clearly expresses a congressional intention to allow state regulation of certain specific aspects of a federal oil and gas lessee's operations. Section 30 of the Mineral Leasing Act requires

that each lease contain provisions relating to diligence, employment practices and the prevention of undue waste, but also requires that "NONE OF SUCH PROVISIONS SHALL BE IN CONFLICT WITH THE LAWS OF THE STATE IN WHICH THE LEASED PROPERTY IS SITUATED."[5] Section 32 of the Mineral Leasing Act further requires that "Nothing in this Act shall be construed or held to affect the rights of the States or other local authority to exercise any rights which they may have, including the right to levy and impose taxes upon improvements, output of mines, or rights, property or assets of any lessee of the United States."[6]

Finally, the Federal Land Policy and Management Act of 1976 ("FLPMA") similarly provides no decisive rule as to the permissible extent of state and local control over federal oil and gas operations. Through FLPMA, the BLM directly entered the area of land use planning, long the exclusive preserve of state and local governments. However, while the active presence of the BLM and OCD in land use matters raises the possibility of sharp conflicts, the Congress in anticipating such conflicts directed that the federal land use plans "be consistent with State and local

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5. 30 U.S.C. Sec. 187 (1982); Law of Federal Oil and Gas Leases at 24-15 (emphasis added).

6. 30 U.S.C. Sec. 189 (1982); Law of Federal Oil and Gas Leases at 24-16.

plans to the maximum extent (the Secretary of Interior) finds consistent with Federal law and the purposes of this Act."[7]

There are two cases which acknowledge the right of the State to exercise control over certain oil and gas activities on federal lands, one decided by the federal Tenth Circuit Court which includes New Mexico and one decided by the Wyoming Supreme Court.

In Texas Oil & Gas Corp. v. Phillips Petroleum Company, 277 F.Supp. 366 (W.D.Okla. 1967), aff'd per curiam, 406 F.2d 1303 (10th Cir.), cert. denied, 396 U.S. 829 (1969), plaintiffs, owners of working interests in certain federal oil and gas leases, sought to avoid the effect of an order of the Oklahoma Corporation Commission force pooling their working interests after they had elected not to participate in the permitted drilling activity. Plaintiffs argued that by virtue of the Mineral Leasing Act and the regulations promulgated thereunder, the federal government had effectively pre-empted state law by asserting its jurisdiction to regulate the exploration, development and

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7. 43 U.S.C, Sec 1712(a) (development of land use plans, 1732(a) management in accordance with land use plans) (1982); Law of Federal Oil and Gas Leases at 24-21.

conservation of federal lands leased for oil and gas exploitation. In rejecting this argument, the Court cited Sections 30 and 32 of the Mineral Leasing Act and stated:

> This language is not aimed at putting the lands under the exclusive control of the Federal Government to the exclusion of the States. Contrary to the position of plaintiffs, the Federal Mineral Leasing Act of 1920, as amended, seems to leave to the States the power to exercise State police power over Federal oil and gas leases.[8]

The Court pointed out that Congress had, however, imposed two limitations upon the reserved state jurisdiction which had to be considered before state action would be permitted: first, that no assignment of a federal oil and gas lease may be effective without the consent of the federal government and, second, that all pooling or communitization agreements involving federal and non-federal lands must be approved by the federal government. In this case, as in the subject case, the Department of the Interior had approved the state's pooling arrangement. Accordingly, the condition precedent to state action, namely federal concurrence, had been satisfied.

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8. Id., at 369.

In Gulf Oil Corp. v. Wyoming Oil and Gas Conservation Commission, 693 P.2d 227 (1985), the Wyoming Supreme Court held that the state's approval of a drilling permit on a federal lease could be conditioned on the operator's securing a means of drill site access other than that originally proposed by the operator. The court rejected contentions that the federal government "occupied the field" by its extensive environmental regulation on federal lands, noting that Sections 30 and 32 of the Mineral Leasing Act expressly preserved that traditional regulatory role of the states.

CONCLUSION

Santa Fe's anticipated conflict over the use of the surface of the NE/4 of Section 20 has not materialized. In fact, the OCD and the BLM are in agreement as to the manner of development of the minerals and the use of the surface.

The BLM has indicated it would approve the use of the surface in the NE/4 of Section 20 within a circular area of some 400 to 500 feet in diameter immediately adjacent to and just south of the Exxon proposed location "E-1." It is obvious that Santa Fe failed to diligently pursue a surface location with the BLM in the NE/4 of Section 20. Exxon has done that and found that the BLM will approve a surface

location which fits both Santa Fe and Exxon's interpretation of the best geologic location for the first well in the section.

The BLM has indicated it would approve the communitization of the E/2 of Section 20 for the test well proposed by Exxon.[9] Any transfer of working interest effected by New Mexico's forced pooling order would follow from approval of the communitization of the E/2. The asserted limited federal controls having thus been satisfied, the Division's orders for the compulsory pooling of the E/2 of Section 20 would be controlling.

The Federal government and the State of New Mexico have concurrent jurisdiction over public domain lands. There are only two federal requirements which must be met before New Mexico may order the compulsory pooling of a federal lessee's interest. Exxon has satisfied these requirements. The Division has jurisdiction to compel the pooling of any federal leasehold in the E/2 of Section 20 as requested by Exxon.

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9. See letter dated December 13, 1989, from Mr. William T. Duncan, Jr. of Exxon to Mr. Michael E. Stogner of the Division attached hereto as Exhibit "1."

The fact that an applicant before the OCD has certain federal regulatory hurdles to overcome cannot and should not be used as a justification for not abiding by what the OCD determines to be in the best interest of prevention of waste and protection of correlative rights.

Enclosed as Exhibit 3 is a proposed order for entry by the Division approving the Exxon application.

SUBMITTED BY:

KELLAHIN, KELLAHIN & AUBREY
P.O. Box 2265
Santa Fe, New Mexico 87504
(505) 982-4285

W. Thomas Kellahin

Candace Hamann Callahan

EXXON COMPANY, U.S.A.

POST OFFICE BOX 1600 • MIDLAND, TEXAS 79702-1600

PRODUCTION DEPARTMENT
SOUTHWESTERN DIVISION

December 12, 1989

W. T. Duncan
Exxon Company, U.S.A.
P. O. Box 1600
Midland, TX 79702

Dear Mr. Duncan:

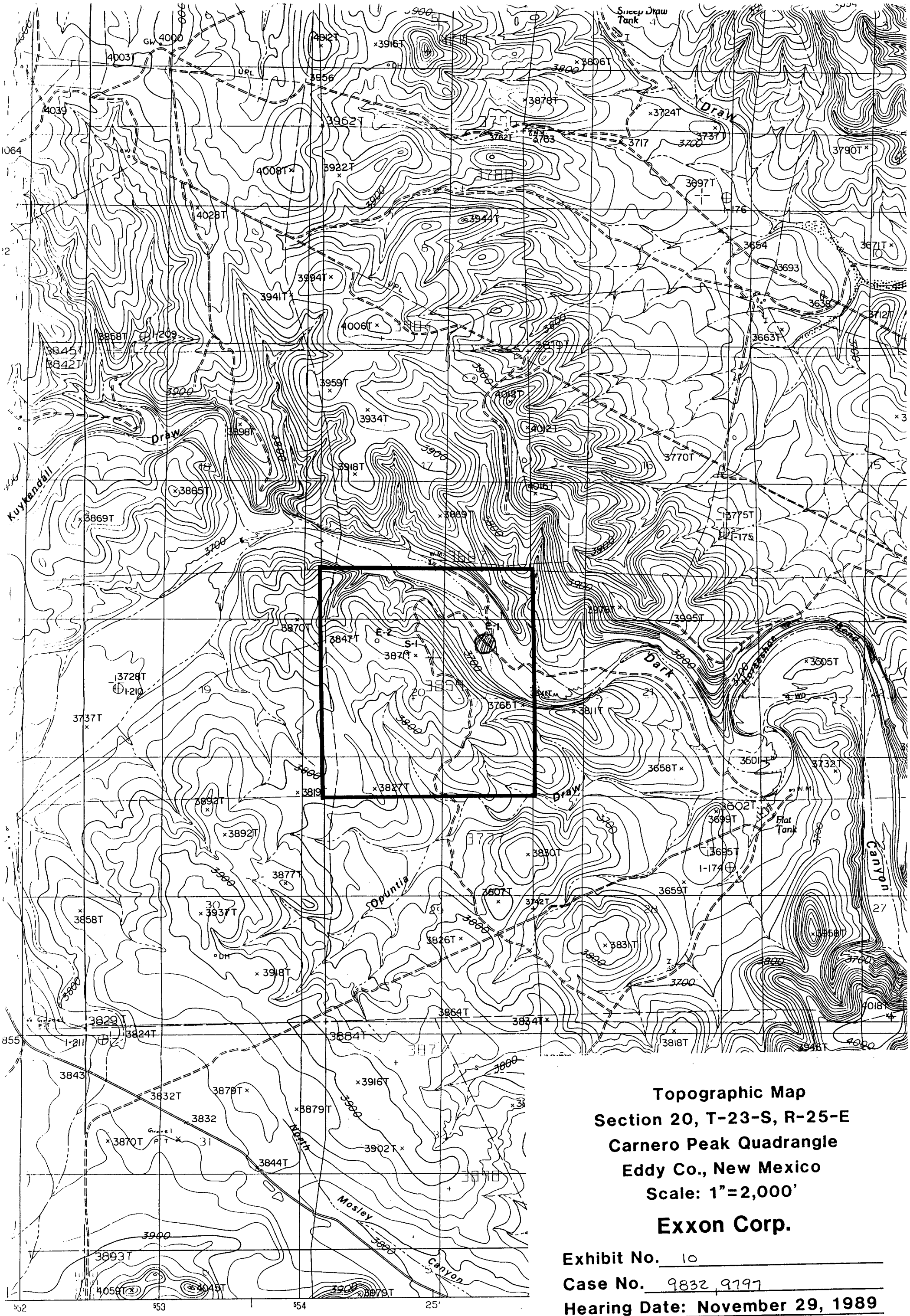
On Friday, December 8, 1989 Bill Tate and I met with Barry Hunt, natural resource specialist for the BLM, on site at the above mentioned location (SE/NE/Sec. 20, 23S, 25E). Mr. Hunt inspected our proposed site which was approximately 1/2 way between Santa Fe's site #2 and #4 as shown on their Exhibit #9. He indicated that he could see no problem with the proposed site and willingly signed a copy of our Exhibit #10.

Also at that meeting, I investigated the proposed access road that Santa Fe seemed so concerned about at the hearing. In my opinion, construction of the road would not require unusual measures and its relative short length would not add significantly to the total site preparation cost. This would be the only difference in cost in our proposed site and Santa Fe's site #1.

If I can be of further assistance, please call me at (915)-688-7682.

J. W. Hill

JWH:shd.H2



Topographic Map
Section 20, T-23-S, R-25-E
Carnero Peak Quadrangle
Eddy Co., New Mexico
Scale: 1"=2,000'

Exxon Corp.

Exhibit No. 10
Case No. 9832, 9797
Hearing Date: November 29, 1989

CROSS HATCHED AREA ADJACENT TO E-1 APPEARS TO BE ACCEPTABLE SURFACE LOCATION. TO BLM AS WITNESSED BY BARRY HUNT 12/8/89.
Barry W. Hunt

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 EXXON CORPORATION FOR COMPULSORY POOLING AND AN UNORTHODOX WELL LOCATION, LEA COUNTY, NEW MEXICO — CASE 9832

APPLICATION OF SANTA FE ENERGY OPERATING PARTNERS, L. P., FOR COMPULSORY POOLING AND A NON-STANDARD GAS PRORATION UNIT, EDDY COUNTY, NEW MEXICO — CASE 9797

EXXON'S PROPOSAL
ORDER OF THE DIVISION

BY THE DIVISION:

This cause came on for hearing at 8:15 a.m. on November 29, 1989, at Santa Fe, New Mexico, before Examiner Michael E. Stogner.

NOW, on this ____ day of December, 1989, the Division Director, having considered the testimony, the record, and the recommendations of the Examiner, and being fully advised in the premises,

FINDS THAT:

(1) Due public notice having been given as required by law, the Division has jurisdiction of this cause and the subject matter thereof.

(2) The Applicant, Exxon Corporation ("Exxon") seeks an order pooling all uncommitted mineral interests from the top of the Wolfcamp formation to the base of the Morrow formation underlying the E/2 of Section 20, T23S, R25E, Eddy County, New Mexico, for a non-standard 301.11 acre gas spacing and proration unit for any and all formations and/or pools spaced on 320-acre spacing and for an exemption from the Special Rules and Regulations governing the Rock Tank Upper and Lower Morrow Gas Pools as promulgated by Division Order No R-3452, as amended. Said unit to be dedicated to a well to be drilled at an unorthodox gas well location 1500 feet from the North line and 1100 feet from the East line of Section 20.

(3) Santa Fe Energy Operating Partners, L. P. ("Santa Fe") seeks an order pooling all mineral interest from the surface to the base of the Morrow formation underlying the N/2 of Section 20 with a well to be drilled at a location 1980 feet from the North line and 1980 feet from the West line within said Section 20.

(4) The dispute between Exxon and Santa Fe is over the orientation of the spacing unit and the well location.

(5) Exxon and Santa Fe are in agreement that:

(a) Section 20 should be developed on 320 acre gas spacing and separated from both the Rock Tank Upper and Lower Gas Pools which are spaced on 640 acre spacing;

(b) Santa Fe should be designated the operator;

(c) Santa Fe's proposed AFE is appropriate;

(d) a 200% risk factor penalty is justified regardless of where the well is drilled in the section; and

(e) Exxon's proposed overhead rates of $5,885.00 per month while drilling and $614.00 per month while producing are fair and reasonable.

(6) On the issue of well spacing, Exxon provided substantial geologic and engineering evidence that Section 20 was separated from the Rock Tank Upper and Lower Gas Pools based upon the following:

(a) Structural cross sections and structure map which demonstrate that the eastern extent of Rock Tank is found at an original gas/water contact which is between -6647 feet and 6356 feet. (Exxon Exhibits 4, 5 & 6)

(b) that the highest structural position of the Morrow in Section 20 is -6775 feet. This structural position is 419 feet downdip of the lowest productive well in the Rock Tank Pools, and 128 feet downdip of a Rock Tank well which was below the original Rock Tank gas/water contact. (Exxon Exhibit 4)

(c) petroleum engineering calculations which show that while Rock Tank Upper and Lower Gas Pools are spaced on 640 acre spacing, both pools were nearing depletion with the Rock Tank Upper Morrow Pool wells averaging approximately 297 acres drained per well and the Lower Morrow Pool wells averaging approximately 491 acres drained per well.

(7) Santa Fe provided a geologic expert witness who agreed with Exxon's geologic conclusions concerning the separation of Section 20 from the Rock Tank Morrow Pools.

(8) Santa Fe did not present any petroleum engineering witness.

(9) Both Exxon and Santa Fe testified that Santa Fe originally planned to participate in a Morrow test well in Section 16 in which Santa Fe had a 33% working interest, identified in Exxon Exhibit 12, but abandoned that well to

pursue the subject well in Section 20 in which Santa Fe has a 6% working interest despite the fact that the Section 16 well is lower risk with more favorable geology. (Santa Fe Exhibit 6 and 7)

(10) On the issue of the well location, Santa Fe first proposed the well be located 660 feet from the North line and 1980 feet from the East line (NW/4NE/4) of Section 20 based upon its interpretation of the geology, but because the BLM would not approve that location and because they presumed the well spacing to be 640 acres, they moved the well to a proposed location on Exxon's lease, 1980 feet from the North and West lines (SE/4NW/4) of the Section.

(11) Exxon provided geologic evidence concerning the thickness of the Lower Morrow Sandstone (identified by Santa Fe as Sequence L-1 on Santa Fe Exhibit 8) and on the thickness of the Upper Morrow Sandstone (identified by Santa Fe as Sequence 4) and concluded that the optimum location for the well was 1500 feet from the North line and 1100 feet from the East line of Section 20.

(12) Santa Fe contended that Sequence 2 (see Exhibit 8) was the primary objective for development of Section 20 while Exxon demonstrated that Sequence 2 in the Morrow upon

which Santa Fe relied has been tested in each of the wells on Santa Fe's cross section and found to be wet and/or non-productive in commercial quantities.

(13) Santa Fe agreed with Exxon that the best well location in Section 20 is in the NE/4, but stated that the BLM would not approve the location because of topographical constraints.

(14 Exxon well location construction expert testified that the Exxon location was an approvable surface location on Exxon acreage and would meet the BLM requirements.

(15) The NE/4 of the Section is the optimum location for the initial well and Exxon's proposed location should be approved as the location for the first well in the section.

(16) On the issue of the orientation of the spacing unit, Exxon provided substantial geologic evidence that two stand up units (E/2 and W/2) with the first well located in the NE/4 and the second well in the NW/4 would provide the maximum opportunity for full development of the section with two wells.

(17) Although Santa Fe testified that a lay down orientation of the spacing units with wells in the NE/4 and SE/4 was the best, they in fact staked their well location in the NW/4, which is inconsistent with Santa Fe's geologic testimony.

(18) Santa Fe has a 37 acre interest in the Section 20 being the NW/4 NE/4, while Exxon has the balance of the N/2 of Section 20 with Amoco having the S/2 of Section 20.

(19) Amoco has failed to appear in support of either applicant.

(20) Exxon presented engineering evidence which justifies two wells in the section. Santa Fe provided no engineering evidence.

(21) Exxon's proposed orientation of the spacing unit with E/2 dedicated to the initial well is the orientation which will more practically result in the full development of the section.

(22) While Santa Fe contended that the BLM would not approve the drilling of a well at the Exxon proposed location, Exxon has provided written confirmation from the BLM showing approval of an area immediately south of the Exxon location 1500 feet from the North line and 1100 feet from the East line of Section 20.

(23) Exxon and Santa Fe both presented structural interpretations (Exhibit SF #6 and Exxon #4) which are in general agreement about the orientation of the structure, however both testified that sand thickness is more important than structure as a criterion for the location of the initial well.

(24) Exxon was the only party to present geologic isoliths on the Morrow intervals proven productive in the immediate area.

(25) Although the NW/4 has better structural position than the NE/4, the NE/4 of Section 20 has significantly greater reservoir thickness than the NW/4 (Exxon Exhibit 9) and maximizing thickness is more important than structure for the initial well.

(26) Santa Fe testified that they would drill the well regardless of which orientation was determined best.

(27) Santa Fe's 6% interest in Section 20 and interest in the spacing unit does not change regardless of whether or not the orientation of the spacing unit is E/2 or N/2.

(28) To avoid the drilling of unnecessary wells, to protect correlative rights, to avoid waste, and to afford to the owner of each interest in said unit the opportunity to recover or receive without unnecessary expense his just and fair share of the production in any pool completion resulting from this order, the subject application as amended should be approved by pooling all mineral interests whatever they may be, within said amended unit.

(29) Santa Fe should be designated the operator of the subject well and unit.

(30) Any non-consenting working interest owner should be afforded the opportunity to pay his share of estimated well costs to the operator in lieu of paying his share of reasonable well costs out of production.

(31) Both Exxon and Santa Fe proposed a 200% risk penalty to be assessed against those interest owners subject to the force-pooling provisions of this order, and in support thereof presented evidence and testimony at the hearing.

(32) While the Division is precluded by statute from awarding a risk factor penalty of more than 200%, it is common in the industry for working interest owners to acknowledge that the geologic risk of certain wells will far exceed that maximum.

(33) Although the proposed unorthodox well location allows the operator and working interest owners to reduce the geologic risk involved in drilling and completing the subject well that does not diminish the risk to less than the maximum 200% risk factor penalty.

(34) Any non-consenting working interest owner who does not pay his share of estimated well costs should have withheld from production his share of the reasonable well costs plus an additional 200% thereof as a reasonable charge for the risk involved in the drilling of the well.

(35) Any non-consenting interest owner should be afforded the opportunity to object to the actual well costs, but actual well costs should be adopted as the reasonable well costs in the absence of such objection.

(36) Following determination of reasonable well costs, any non-consenting working interest owner who has paid his share of estimated costs should pay to the operator any amount that reasonable well costs exceed estimated well costs and should receive from the operator any amount that paid estimated well costs exceed reasonable well costs.

(37) $5885.00 per month while drilling and $614.00 per month while producing should be fixed as reasonable charges for supervision (combined fixed rates); the operator should be authorized to withhold from production the proportionate share of such supervision charges attributable to each non-consenting working interest, and in addition thereto, the operator should be authorized to withhold from production the proportionate share of actual expenditures required for operating the subject well not in excess of what are reasonable, attributable to each non-consenting working interest.

(38) All proceeds from production from the subject well which are not disbursed for any reason should be placed in escrow to be paid to the true owner thereof upon demand and proof of ownership.

(39) Upon the failure of the operator of said pooled unit to commence the drilling of the well to which said unit is dedicated on or before March 1, 1990, the order pooling said unit should become null and void and of no effect whatsoever.

(40) Should all parties to this forced pooling reach voluntary agreement subsequent to entry of this order, this order shall thereafter be of no further effect.

(41) The operator of the well and unit shall notify the Director of the Division in writing of the subsequent voluntary agreement of all parties subject to the forced pooling provisions of this order.

IT IS THEREFORE ORDERED THAT:

(1) All mineral interest, whatever they may be, from the top of the Wolfcamp formation the base of the Morrow formation, underlying the E/2 of Section 20, T23S, R25E, NMPM, Eddy County, New Mexico, are hereby pooled to be dedicated to a well to be drilled at an unorthodox well location approximately 1500 feet from the North line and 1100 feet from the East line of said Section 20.

(2) The application of Exxon is hereby granted.

(3) The application of Santa Fe is hereby DENIED.

(4) That Santa Fe Energy Operating Partners, L. P. is hereby designated as operator.

PROVIDED HOWEVER THAT, the operator of said unit shall commence the drilling of said well on or before the 1st day of March, 1990, and shall thereafter continue the drilling of said well with due diligence to a depth sufficient to test the Morrow formation.

PROVIDED FURTHER THAT, in the event said operator does not commence the drilling of said well on or before the 1st day of March, 1990, Ordering Paragraph No. (1) of this order shall be null and void and of no effect whatsoever, unless said operator obtains a time extension from the Division for good cause shown.

PROVIDED FURTHER THAT, should said well not be drilled to completion, or abandonment, within 120 days after commencement thereof, said operator shall appear before the Division Director and show cause why Ordering Paragraph No. (1) of this order should not be rescinded.

(5) After the effective date of this order and within 90 days prior to commencing said well, the operator shall furnish the Division and each known working interest owner in the subject unit an itemized schedule of estimated well costs.

(6) Within 30 days from the date the schedule of estimated well costs is furnished to him any non-consenting working interest owner shall have the right to pay his share of estimated well costs to the operator in lieu of paying his share of reasonable well costs out of production and any such owner who pays his share of estimated well costs as provided above shall remain liable for operating costs but shall not be liable for risk charges.

(7) The operator shall furnish the Division and each known working interest owner an itemized schedule of actual well costs within 90 days following completion of the well; if no objection to the actual well costs is received by the Division and the Division has not objected within 45 days following receipt of said schedule, the actual well costs shall be the reasonable well costs; provided however, if there is objection to actual well costs within said 45-day period the Division will determine reasonable well costs after public notice and hearing.

(8) Within 60 days following determination of reasonable well costs, any non-consenting working interest owner who has paid his share of estimated well costs in advance as provided above shall pay to the operator his pro rata share of the amount that reasonable well costs exceed estimated well costs and shall receive from the operator his pro rata share of the amount that estimated well costs exceed reasonable well costs.

(9) The operator is hereby authorized to withhold the following costs and charges from production:

(a) The pro rata share of reasonable well costs attributable to each non-consenting working interest owner who has not paid his share of estimated well costs within 30 days from the date the schedule of estimated well costs is furnished to him, and

(b) As a charge for the risk involved in the drilling of the well, 200% of the pro rata share of reasonable well costs attributable to each non-consenting working interest owner who has not paid his share of estimated well costs within 30 days from the date the schedule of estimated well costs is furnished to him.

(10) The operator shall distribute said costs and charges withheld from production to the parties who advanced the well costs.

(11) $5885.00 per month while drilling and $614.00 per month while producing are hereby fixed as reasonable charges for supervision (combined fixed rates); the operator is hereby authorized to withhold from production the proportionate share of such supervision charges attributable to each non-consenting working interest, and in addition thereto, the operator is hereby authorized to withhold from production the proportionate share of actual expenditures required for operating such well, not in excess of what are reasonable, attributable to each non-consenting working interest.

(12) Any unleased mineral interest shall be considered a seven-eighths (7/8) working interest and a one-eighth (1/8) royalty interest for the purpose of allocating costs and charges under the terms of this order.

(13) Any well costs or charges which are to be paid out of production shall be withheld only from the working interest's share of production, and no costs or charges shall be withheld from production attributable to royalty interests.

(14) All proceeds from production from the subject well which are not disbursed for any reason shall immediately be placed in escrow in Eddy County, New Mexico, to be paid to the true owner thereof upon demand and proof of ownership; the operator shall notify the Division of the name and address of said escrow agent within 30 days from the date of first deposit with said escrow agent.

(15) Should all parties to this forced pooling order reach voluntary agreement subsequent to entry of this order, this order shall thereafter be of no further effect.

(16) The operator of the well and unit shall notify the Director of the Division in writing of the subsequent voluntary agreement of all parties subject to the forced pooling provisions of this order.

(17) Jurisdiction of this cause is retained for the entry of such further orders as the Division may deem necessary.

DONE at Santa Fe, New Mexico on the day and year hereinabove designated.

STATE OF NEW MEXICO
OIL CONSERVATION DIVISION

WILLIAM J. LEMAY
Director

SEAL

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January 10, 1990

HAND DELIVERED

Michael Stogner
Hearing Examiner
Oil Conservation Division
310 Old Santa Fe Trail
Santa Fe, New Mexico 87501

Re: Santa Fe Energy Operating Partners, L.P., Case No. ~~9795~~ 9797
Exxon Company, U.S.A., Case No. 9832

Dear Mr. Stogner:

Enclosed is our Proposed Order in the above-referenced cases, together with the supporting Memorandum Brief that you requested.

Thank you for your indulgence and patience due to our delay in submitting these materials to you.

Very truly yours,

Ernest L. Padilla

ELP:pmc
Enclosures as stated

cc: Santa Fe Operating Partners, L.P.
W. Kellahin, Esq., (w/encl.)

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:

CASE NO. 9797 and 9832
ORDER NO. R-_____

APPLICATION OF SANTA FE ENERGY
OPERATING PARTNERS, L. P. FOR
COMPULSORY POOLING AND NON-STANDARD
GAS PRORATION UNIT, EDDY COUNTY,
NEW MEXICO

APPLICATION OF EXXON COMPANY, U.S.A.
FOR COMPULSORY POOLING, UNORTHODOX
GAS WELL LOCATION AND NON-STANDARD
GAS PRORATION UNIT, EDDY COUNTY,
NEW MEXICO

SANTA FE ENERGY OPERATING PARTNERS, L.P.

PROPOSED ORDER OF THE DIVISION

BY THE DIVISION:

This cause came on for hearing at 8:15 a.m. on November 29, 1989, at Santa Fe, New Mexico, before Examiner Michael E. Stogner.

NOW, on this ___ day of _____, 1990, the Division Director, having considered the testimony, the record and the recommendations of the Examiner, and being fully advised in the premises,

FINDS THAT:

1. Due public notice having been given as required by law, the Division has jurisdiction of this cause and the subject matter thereof.

2. The applicant in Case 9797, Santa Fe Energy Operating Partners, L.P. (Santa Fe), seeks an order pooling all mineral interests from the surface to the base of the Morrow formation underlying the following described acreage in Irregular Section 20, Township 23 South, Range 25 East, and in the following manner: all of said Section 20 to form a non-standard 599.41-acre, more or less, gas spacing and proration unit for the Undesignated Rock Tank-Lower Morrow Gas Pool and Undesignted Rock Tank-Upper Morrow Gas Pool; and, Lots 1 through 7 and the NW/4NE/4 (N/2 equivalent) of said Section 20, forming a non-standard 301.37-acre gas spacing and proration unit for any and all formations and/or pools developed on 320-acre spacing within said vertical extent. Both units are to be dedicated to a single well to be drilled at a standard gas well location 1980 feet from the North and West lines (Unit F) of said Section 20.

3. The applicant in Case 9832, Exxon Company, U.S.A. (Exxon), seeks an order pooling all mineral interests from the top of the Wolfcamp formation to the base of the Morrow Formation, underlying the NW/4NE/4 and Lots 1, 6, 7, 8, 9, 14 and 15 (E/2 equivalent) of Section 20, Township 23 South, Range 25 East, forming a non-standard 301.11-acre gas

spacing and proration unit for any and all formations and or pools developed on 320-acre spacing within said vertical extent. Applicant further seeks to be exempt from the Special Rules and Regulations governing the Rock Tank-Upper and Lower Morrow Gas Pools as promulgated by Division Order No. R-3452, as amended. Said unit is to be dedicated to a well to be drilled at an unorthodox gas well location 1500 feet from the North line and 1100 feet from the East line (Unit A) of said Section 20.

4. Each applicant, Santa Fe and Exxon, seeks to name Santa Fe the operator of the unit each seeks to have pooled. Also, each applicant has the right to drill and both propose to drill a well upon their respective units, as described above, to a depth sufficient to test the Morrow formation.

5. Case Nos. 9797 and 9832 were consolidated for purpose of hearing and should be consolidated for purpose of issuing an order inasmuch as the cases involve certain common acreage and the granting of one application would necessarily require the concomitant denial of the other.

6. There are interest owners in both proposed proration units who have not agreed to pool their interests.

7. Section 18, Township 23 South, Range 25 East, Eddy County, New Mexico, directly diagonally offsets Section 20 and therefore are within one mile of each other. Section 18 has been developed under the Rock Tank-Upper and Lower

Morrow Gas Pool special rules providing for 640-acre well spacing.

8. Prior to its application herein, Santa Fe was adivsed by the Division's Artesia District Office that development of Section 20 in the Morrow formation would be governed by the Rock Tank-Upper and Lower Morrow Gas Pool special rules.

9. Exxon presented geological evidence showing a fault which segregated Sections 18 and 20; Santa Fe acknowledged that a geologic anamoly could exist between Sections 18 and 20, but disputes that a fault exists between both sections.

10. Based on applicability of statewide 320-acre spacing rules of the Division, Santa Fe and Exxon presented testimony and evidence on the configuration of proration units for the development of Section 20; Santa Fe advocated development for lay-down units and Exxon advocated development on stand-up units.

11. A proration and spacing unit comprised of the E/2 of Section 20 would require splitting a federal oil and gas lease comprised entirely of the S/2 of Section 20, the effect of which could contravene federal oil and gas regulations, and thereby prohibiting approval of a communitization agreement by the Bureau of Land Management of the Department of the Interior.

12. The geological evidence presented at the hearing by both applicants was not in conflict as to the desireability of drilling the initial well in Section 20 in the NE/4 of said Section 20. The NE/4 of Section 20 has no viable surface drillsite due to topography or safety hazard.

13. Santa Fe's proposed location for a N/2 proration unit and spacing unit allows for better development of Section 20 in the Morrow formation becuase it offers the best geologic compromise to a NE/4 location and still allows a second well location in the SE/4 of Section 20 which would encounter better sand thickness.

14. Section 20 should be developed on 320-acre spacing pursuant to the Division's statewide general rules and regulations.

15. The application of Exxon, to the extent that it requests an E/2 of Section 20 proration and spacing unit, is not in the best interests of the prevention of waste or the protection of correlative rights and will impair orderly development of the hydrocarbon reserves underlying Section 20.

16. As stated in Finding (15) above, the application of Exxon in Case No. 9638 should therefore be denied.

17. To avoid the drilling of unnecessary wells, to protect correlative rights, to prevent waste and to afford to the owner of each interest in said unit the opportunity to recover or receive without unnecessary expense his just

and fair share of the gas in said pools, the application of Santa Fe in Case No. 9797 should be approved by pooling all mineral interests, whatever they may be, in the Atoka and Morrow formations underlying Lots 1 through 7, inclusive, and the NW/4NE/4 (N/2 equivalent) of Section 20 forming a non-standard 301.37-acre spacing and proration units. Said unit should be dedicated to a well to be drilled at a standard gas well location 1980 feet from the North and West lines (Unit F) of said Section 20.

18. Santa Fe should be designated the operator of the subject well and unit as described above.

19. Any non-consenting working interest owner should be afforded the opportunity to pay his share of estimated well costs to the operator in lieu of paying his share of reasonable well costs out of production.

20. Any non-consenting working interest owner who does not pay his share of estimated well costs should have withheld from producing his share of the reasonable well costs plus an additional 200 percent thereof as a reasonable charge for the risk involved in the drilling of the well.

21. Any non-consenting interest owner should be afforded the opportunity to object to the actual well costs but actual well costs should be adopted as the reasonable well costs in the absence of such objection.

22. Following determination of reasonable well costs, any non-consenting working interest owner who has paid his

share of estimated costs should pay to the operator any amount that reasonable well costs exceed estimated well costs and should receive from the operator any amount that paid estimated well costs exceed reasonable well costs.

23. $5,500.00 per month while drilling and $550.00 per month while producing should be fixed as reasonable charges for supervisions (combined fixed rates); the operator should be authorized to withhold from production the proportionate share of such supervision charges attributable to each non-consenting working interest, and in addition thereto, the operator should be authorized to withhold from production the proportionate share of actual expenditures required for operating the subject well, not in excess of what are reasonable, attributable to each non-consenting working interest.

24. All proceeds from production from the subject well which are not disbursed for any reason should be placed in escrow to be paid to the true owner thereof upon demand and proof of ownership.

25. Upon the failure of the operator of said pooled unit to commence the drilling of the well to which said unit is dedicated on or before _____, 1990, the Order pooling said unit should become null and void and of no effect whatsoever.

26. Should all the parties to this forced pooling reach voluntary agreement subsequent to entry of this order, this order shall thereafter be of no further effect.

27. The operator of the well and unit shall notify the Director of the Division in writing of the subsequent voluntary agreement of all parties subject to the forced pooling provision of this order.

IT IS THEREFORE ORDERED THAT:

1. The application of Exxon in Case No. 9832 for an order pooling all mineral interests from the base of the Wolfcamp to the base of the Morrow Formation underlying the E/2 of Section 20, Township 24 South, Range 34 East, NMPM, Lea County, New Mexico, forming a non-standard 301.11-acre gas spacing and proration unit for said formation to be dedicated to a single well to be drilled at a location which is non-standard for the proposed Morrow unit 1500 feet from the North line and 1100 feet from the East line (Unit H) of said Section 20 is hereby denied.

2. All mineral interests, whatever they may be, in all formations and/or pools developed on 320-acre spacing underlying the N/2 equivalent of Section 20, Township 23 South, Range 25 East, NMPM, Eddy County, New Mexico, are hereby pooled to form a non-standard 301.37-acre gas spacing and proration unit for all such formations and/or pools, to be dedicated to a well to be drilled at a standard gas well

location 1980 feet from the North and West lines (Unit F) of Section 20.

PROVIDED HOWEVER THAT, the operator of said unit shall commence the drilling of said well on or before _____, 1990, and shall thereafter continue the drilling of said well with due diligence to a depth sufficient to test the Morrow formation.

PROVIDED FURTHER THAT, in the event said operator does not commence the drilling of said well on or before _____ 1990, Ordering Paragraph No. 2 of this order shall be null and void and of no effect whatsoever, unless said operator obtains a time extension from the Division for good cause shown.

PROVIDED FURTHER THAT, should said well not be drilled to completion or abandonment, within 120 days after commencement thereof said operator shall appear before the Division Director and show cause by ordering Paragraph No. 2 of this Order should not be rescinded.

3. Santa Fe is hereby designated the operator of the subject well and unit.

4. After the effective date of this Order and within 90 days prior to commencing said well, the operator shall furnish the Division and each known working interest owner in the subject unit an itemized schedule of estimated well costs.

5. Within 30 days from the date the schedule of estimated well costs is furnished to him, any non-consenting working interest owner shall have the right to pay his share of estimated well costs to the operator in lieu of paying his share of reasonable well costs out of production, and any such owner who pays his share of estimated well costs as provided above shall remain liable for operating costs but shall not be liable for risk charges.

6. The operator shall furnish the Division and each known working interest owner an itemized schedule of actual well costs within 90 days following completion of the well; if no objection to the actual well costs is received by the Division and the Division has not objected within 45 days following receipt of said schedule, the actual well costs shall be the reasonable well costs; provided however, if there is objection to actual well costs within said 45-day period the Division will determine reasonable well costs after public notice and hearing.

7. Within 60 days following determination of reasonable well costs, any non-consenting working interest owner who has paid his share of estimated well costs in advance as provided above shall pay to the operator his pro rata share of the amount that reasonable well costs exceed estimated well costs and shall receive from the operator his pro rata share of the amount that estimated well costs exceed reasonable well costs.

8. The operator is hereby authorized to withhold the following costs and charges from production:

(A) The pro rata share of reasonable well costs attributable to each non-consenting working interest owner who has not paid his share of estimated well costs within 30 days from the date the schedule of estimated well costs is furnished to him.

(B) As a charge for the risk involved in the drilling of the well, 200 percent of the pro rata share of reasonable well costs attributable to each non-consenting working interest owner who has not paid his share of estimated well costs within 30 days from the date the schedule of estimated well costs is furnished to him.

9. The operator shall distribute said costs and charges withheld from production to the parties who advanced the well costs.

10. $5,500.00 per month while drilling and $550.00 per month while producing are hereby fixed as reasonable charges for supervision (combined fixed rates); the operator is hereby authorized to withhold from production the proportionate share of such supervision charges attributable to each non-consenting working interest, and in addition thereto, the operator is hereby authorized to withhold from production the proportionate share of actual expenditures

required for operating such well, not in excess of what are reasonable, attributable to each non-consenting working interest.

11. Any unleased mineral interest shall be considered a seven-eighths (7/8) working interest and a one-eighth (1/8) royalty interest for the purpose of allocating costs and charges under the terms of this order.

12. Any well costs or charges which are to be paid out of production shall be withheld only from the working interest's share of production, and no costs or charges shall be withheld from production attributable to royalty interest.

13. All proceeds from production from the subject well which are not disbursed for any reasons shall immediately be places in escrow in Lea County, New Mexico, to be paid to the true owner thereof upon demand and proof of ownership; the operator shall notify the Division of the name and address of said escrow agent within 30 days from the date of first deposit with said escrow agent.

14. Should all parties to this forced pooling order reach voluntary agreement subsequent to entry of this order, this order shall thereafter be of no further effect.

15. The operator of the well and unit shall notify the Director of the Director in writing of the subsequent voluntary agreement of all parties subject to the forced pooling provisions of this order.

16. Jurisdiction of this cause is retained for the entry of such further orders as the Division may deem necessary.

DONE at Santa Fe, New Mexico, on the day and year hereinabove designated.

STATE OF NEW MEXICO
OIL CONSERVATION DIVISION

WILLIAM J. LEMAY
Director

S E A L

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:

CASE NOS. 9797 and 9832
ORDER NO.

APPLICATION OF SANTA FE ENERGY OPERATING
PARTNERS, L.P. FOR COMPULSORY POOLING
AND NON-STANDARD GAS PRORATION UNIT,
EDDY COUNTY, NEW MEXICO

APPLICATION OF EXXON COMPANY, U.S.A.
FOR COMPULSORY POOLING, UNORTHODOX
GAS WELL LOCATION AND NON-STANDARD
GAS PRORATION UNIT, EDDY COUNTY,
NEW MEXICO

MEMORANDUM BRIEF

INTRODUCTION

The issues raised during the course of the hearing involve federal/state conflict issues. On one hand, The Bureau of Land Management of The Department of Interior (BLM) manages and regulates activities conducted on federal lands. On the other hand, The Oil Conservation Division (Division) pursuant to state statutory scheme, regulates oil and gas activities for conservation purposes. In this case land management policies of the BLM could directly conflict

with the Division's order should the Division grant the Exxon application.

Initially, federal preemption of the Division's authority is one of the issues which must necessarily be discussed in this Memorandum Brief. Secondly, it is no surprise to anyone that, in recent years, federal legislation has increasingly created considerations which the BLM and the state, itself, must address in what once were routine matters that would not create federal/state conflicts. No attempt will be made in this Brief to address all potential aspects of the current law relative to federal/state conflicts since such an exhaustive analysis would constitute quite an immense undertaking. Instead, we will limit our discussion to the actual issues raised in the hearing and, in that vein, present to the Division potential impacts of a ruling which would conflict with federal authority.

DISCUSSION

A. Federal Preemption

The realm of the federal preemption doctrine, in this instance, is probably best illustrated by an opinion rendered by the Ninth Circuit Court of Appeals in Ventura County v. Gulf Oil Corp., 601 F.2d 1080 (9th Cir 1979), aff'd 445 U.S. 947 (1980). Relying on Kleppe v. New Mexico,

426 U.S. 529 (1976) the Ninth Circuit invalidated county regulations holding:

> The federal government has authorized a specific use of federal lands, and Ventura cannot prohibit that use, either temporarily or permanently, in an attempt to substitute its judgment for that of Congress... [T]he states and their subdivisions have no right to apply local regulations impermissibly conflicting with achievement of a congressionally approved use of federal lands and the provision of [30 USC] Section 189 does not alter this principle.

601 F.2d at 1084.

The proviso referred to by the Court provided "that nothing in this Act shall be construed or held to affect the rights of the States or other local authority to exercise any rights which they may have..." 30 U.S.C. Section 189. This provision was part of the original enactment of the Mineral Leasing Act of 1920 under which the lands under consideration are managed by the BLM.

Section 30, another pertinent section of the Mineral Leasing Act of 1920, codified as 30 U.S.C. Section 187, seemingly is stronger in terms of state power in that it provides that no lease provision "shall be in conflict with any laws of the state in which the leased property is situated." Yet the Ventura court said that Section 30 of the Act applied only to "employment practices, prevention of

undue waste and monopoly, and diligence requirements." 601 F.2d at 1085. Regarding Section 32 (30 USC Section 189) the court said that Section 32 "cannot give authority to the state which it does not already possess." Id. at 1086.

Kleppe v. New Mexico, supra, holds that states do enjoy general legislative jurisdiction on federal lands, but that Congress concurrently also has general "legislative" jurisdiction over such lands, and that therefore state or local regulations may be preempted under the supremacy clause of the United States Constitution.

Kirkpatrick Oil & Gas Co. v. United States 675 F.2d 1122 (1982) contains an excellent discussion of issues almost identical to the issues raised in the instant case. We believe that this case fairly sets forth the standards that are applicable to the potential conflict in federal/state jurisdiction raised by the issues of this case. Kirkpatrick held that a state communitization may not bind federally owned land without the consent of the Secretary of the Interior. We quote liberally from the court opinion which said:

> Although the Constitution empowers Congress to regulate federal lands, U.S. Const. art. IV, Section 3, cl. 2, Congress determines whether or not to exercise this power. Texas Oil & Gas Corp. v. Phillips Petroleum Co., 277 F.Supp. 366, 368 (W.D. Okla. 1967), aff'd per curiam, 406 F.2d 1303 (10th Cir.), cert. denied, 396 U. S. 829, 90 S.Ct. 80, 24 L.Ed.2d 80 (1969). Through the Mineral Lands Leasing Act of 1920, codified at 30 U.S.C. Sub-section 181-263, Congress has prescribed limited, but not exclusive, controls over

the leasing of federal lands for oil and gas production. Wallis v. Pan American Petroleum Corp., 384 U.S. 63, 86 S.Ct. 1301, 16 L.Ed.2d 369 (1966); Texas Oil & Gas, 277 F.Supp. at 369.

Kirkpatrick relies upon 30 U.S.C. Section 187 and 189 as indicating that Congress intended to submit federal oil and gas lands to state-forced communitization. Section 187 lists certain provisions that must appear in federal mineral leases and declares, "None of such provisions shall be in conflict with the laws of the State in which the leased property is situated." But this section primarily focuses on various safeguards for workers on federal oil and gas lands and does not relate to land use controls. See Ventura County v. Gulf Oil Corp., 601 F.2d 1080, 1085 (9th Cir. 1979), aff'd mem., 445 U.S. 947, 100 S.Ct. 1593, 63 L.Ed.2d 782 (1980). Section 189 states, in pertinent part, "Nothing in this chapter shall be construed or held to affect the rights of the States or other local authority to exercise any rights which they may have, including the right to levy and collect taxes upon improvements, output of mines, or other rights, property, or assets of any lessee of the United States." This proviso gives the states no power they do not already possess Ventura County, 601 F.2d at 1086. It does not answer the question whether the states can communitize federal lands without federal consent. This Court relied upon sections 187 and 189 in affirming enforcement of an Oklahoma communitization order entered over the objection of lessees of federal lands. Texas Oil & Gas, 406 F.2d 1303. But, as both the trial and circuit court opinions stressed, there the Secretary had approved the state order. The decision does not control the instant case, in which the federal lessee approved the state order but the Secretary did not.

Section 226(j) specifically treats communitization of federal leases. In its most pertinent paragraph it provides:

> "When separate tracts cannot be independently developed and operated in conformity with an established well-spacing or development program, any lease, or a portion thereof, may be pooled with other lands, whether or not owned by the United States, under a communitization or drilling agreement providing for an apportionment of

> production or royalties among the separate tracts of land comprising the drilling or spacing unit when determined by the Secretary of the Interior to be in the public interest, and operations or production pursuant to such an agreement shall be deemed to be operations or production as to each such lease committed thereto."

30 U.S.C. Section 226(j) (emphasis added).

Kirkpatrick emphasizes the word "agreement" and argues that the Secretary's consent is required only for voluntary agreements, not for state-ordered communitization. The government argues for a broader construction. We agree with the government.

In a number of paragraphs section 226(j) delegates to the Secretary's discretion the power to approve, in order to promote conservation, modifications to federal mineral leases, unit or cooperative plans, and operating, drilling, or development contracts. To be consistent with the rest of section 226(j), Congress must have intended that the Secretary have approval authority over any communitization of federal lands, and that no state-ordered forced pooling would bind the government without the Secretary's consent.

A fairly recent decision of the Interior Board of Land Appeals has held that Congress has preempted state regulation of communitization or drilling agreements affecting federal oil and gas leases. Kennedy & Mitchell, Inc., 68 IBLA 80, GFS (O&G) 269 (1982) citing Texas Oil & Gas Corp. v. Phillips Petroleum Co., 406 F.2d 1303 (10th Cir.) cert. denied, 396 U.S. 829 (1969). Other IBLA decisions uphold the proposition that the Secretary of the Interior's consent is a separate decision and that a state order is but a factor for the Secretary's consideration.

See, 2 Law of Federal Oil and Gas Leases, Section 18.13 (1989).

As a consequence, the caution expressed by Santa Fe Energy Operating Partners, L.P. (Santa Fe), with regard to splitting federal leases is viewed by Santa Fe as a very serious matter because the federal government, as lessor, requires compliance with its regulations. Until final approval by the Bureau of Land Management of a communitization agreement involving an E/2 spacing and proration unit, an order of the Division pooling such E/2 spacing and proration unit is literally subject to invalidation since it would impermissibly usurp the Secretary of the Interior's authority.

B. Well Location Issues

In a state court decision issued by the Wyoming Supreme Court, Gulf Oil Corp. v. Wyoming Oil and Gas Commission, 693 P.2d 227 (1985) the court rejected preemption contentions, but conceded, based on Kleppe, supra, that Wyoming's Conservation Commission could be preempted. In that case a federal lessee sought a drilling permit for its proposed drilling activity on national forest lands. The Conservation Commission granted the application but conditioned its approval on the federal lessee not using its

preferred access route because it would "unreasonably damage...other lands."

In disposing of the preemption contentions, the Wyoming Court credited the National Environmental Policy Act of 1970 (NEPA) and the Environmental Quality Improvement Act of 1970 (EQIA) as stating a federal policy which "governs the interpretation and administration of all laws of the United States including the Mineral Leasing Act..." 693 P.2d at 236.

By relying on the NEPA and EQIA, the Wyoming Court placed some of the obligation of enforcing environmental mandates on the state. The effect of the Wyoming case rationale is that it placed the state in a "Catch-22" position - by ducking one issue it acquired a potentially more burdensome one.

In enacting NEPA, Congress declared federal policy as such:

> the continuing policy of the Federal Government, in cooperation with State and local governments, . . . to use all practicable means and measures . . . in a manner calculated to foster and promote the general welfare, to create and maintain conditions under which man and nature can exist in productive harmony, and fulfill the social, economic, and other requirements of present and future generations of Americans.

42 U.S.C., Section 4331.

Pursuant to that policy, NEPA declared a determination to "assure for all Americans safe, healthful, productive and

esthetically and culturally pleasing surroundings . . ." and to "attain the widest range of beneficial uses of the environment without degradation, risk to health or safety, or other undesirable and unintended consequences. . . ." Id. (emphasis ours) Later Congress enacted the EQIA, declaring "that there is a national policy for the environment which provides for the enhancement of environmental quality," and declaring that "the primary responsibility for implementing this policy rests with State and local government." 42 U.S.C. Section 4371.

During the hearing, Santa Fe's witnesses testified about Santa Fe's safety concerns with placing its location at the bottom of the canyon. In addition, Santa Fe cited concerns of the danger of building a road and thereafter traversing the grade of the road to a well location at the bottom of the canyon, which itself is potentially subject to flooding. Furthermore, the Bureau of Land Management had recommended that the well be placed at the rim of the canyon.

Safety and environmental degration are immediate factors which, under the Wyoming ruling and the above-cited federal environmental legislation, the OCD must consider. These are factors which are not entirely within the federal government's province, and which rest squarely on the Division for its determination.

CONCLUSION

Federal public land management policies are unquestionably burdening oil and gas producers. See e.g., Brooks, Multiple Use Versus Dominant Use: Can Federal Land Use Planning Fulfill the Principles of Multiple Use for Mineral Development 33 Rocky Mountain Mineral Law Institute (1987). The encroachment of federal policy into what may have once been considered exclusive state concerns continues on an ever-increasing basis.

In this case it simply seems senseless to tempt further federal encroachment, either through preemption or enforcement of environmental mandates, when the proposed Santa Fe location will avoid the temptation. The Santa Fe location offers a suitable geological location and allows further development of Section 20 with minimal environmental damage or creation of a safety hazard which would pose a safety threat into an indeterminate future period.

Respectfully submitted,

PADILLA & SNYDER

By: _____

Ernest L. Padilla
Post Office Box 2523
Santa Fe, New Mexico 87504-2523
(505) 988-7577

CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing Memorandum Brief was mailed, postage prepaid, to W. Thomas Kellahin, Esq., Kellahin, Kellahin & Aubrey, P. O. Box 2265, Santa Fe, New Mexico 87504-2265, this 10th day of January, 1990.

Ernest L. Padilla

STATE OF NEW MEXICO

ENERGY, MINERALS AND NATURAL RESOURCES DEPARTMENT

OIL CONSERVATION DIVISION

GARREY CARRUTHERS
GOVERNOR

March 29, 1990

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Mr. Thomas Kellahin
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Attorneys at Law
Post Office Box 2265
Santa Fe, New Mexico

Re: CASE NO. 9797 and 9832
ORDER NO. R-9135

Applicant:
Santa Fe Energy Operating Partne
and ~~Exxon Company, U.S.A.~~ L.P

Dear Sir:

Enclosed herewith are two copies of the above-referenced Division order recently entered in the subject case.

Sincerely,

Florene Davidson

FLORENE DAVIDSON
OC Staff Specialist

Copy of order also sent to:

Hobbs OCD x
Artesia OCD x
Aztec OCD

Other Ernest L. Padilla