

**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. 15589
ORDER NO. R-14296**

**APPLICATION OF THE NEW MEXICO OIL CONSERVATION DIVISION
COMPLIANCE AND ENFORCEMENT BUREAU FOR A COMPLIANCE ORDER
AGAINST MCKAY OIL CORPORATION, FOR WELLS OPERATED IN CHAVES AND
LEA COUNTIES, NEW MEXICO.**

ORDER OF THE DIVISION

BY THE DIVISION:

This case came on for hearing at 8:30 a.m. on January 5, 2017, at Santa Fe, New Mexico, before Examiner Michael A. McMillan.

NOW, on this 13th day of February, 2017, the Division Director, having considered the testimony, the record, and the recommendations of the Examiner,

FINDS THAT:

(1) The Application of the Oil Conservation Division Compliance and Enforcement Bureau ("Applicant") asserted McKay Oil Corporation, a New Mexico Corporation, OGRID No. 14424 ("McKay" or "Operator") is in violation of Regulations 19.15.5.9 NMAC (non-compliant wells), 19.15.8.9 NMAC (financial assurance for plugging wells), and 19.15.25.8 NMAC (failure to properly plug and abandon wells).

(2) The Application complies with the requirements of 19.15.8.10 NMAC.

(3) Proper and sufficient public notice of the hearing has been provided in accordance with Regulation 19.15.4.9 NMAC.

(4) Proper and sufficient notice was given by certified mail, return receipt requested to McKay, and to Edward L. Mazel, the duly appointed and serving chapter 7 trustee for the Estate of McKay Oil Corporation, Bankruptcy No. 7-11-11678 TR, United States Bankruptcy Court, District of New Mexico.

(5) Applicant appeared through its counsel. Applicant received a return receipt indicating McKay Oil Corporation received the notice provided it, but did not appear. Trustee Mazel made arrangements to appear telephonically, but did not so appear at the appointed time. McKay Petroleum Corporation, McKay Living Trust and Schultz Oil and Gas Properties, each

asserting an interest in the proceedings as working interest owners of one or more of the subject wells, appeared through their counsel, Damon Richards.

(6) The Oil Conservation Division ("Division") has jurisdiction over this case and the subject matter pursuant to NMSA 1978, § 70-2-12.

(7) Applicant is seeking to enforce its police and regulatory powers, and pursuant to 11 U.S.C. §362(b)(4), this case is not subject to the automatic stay imposed by 11 U.S.C. § 362(a).

(8) The wells which are the subject of this case are:

Well Name	Well No.	API No.	County
Antelope Federal	1	30-005-61661	Chaves
Antelope Federal	2	30-005-61766	Chaves
Antelope Federal	3	30-005-61774	Chaves
Bonnie	1	30-005-62551	Chaves
Camp State	1	30-005-61446	Chaves
Five Mile Tank Federal	2	30-005-61403	Chaves
Husky-McKay	1	30-005-61616	Chaves
Inexco Federal	2	30-005-62389	Chaves
Inexco Federal	4	30-005-62382	Chaves
Inexco Federal	5	30-005-63601	Chaves
Inexco Federal	6	30-005-63740	Chaves
Jerry Don Federal	1	30-005-62221	Chaves
McKay B Federal	4	30-005-64082	Chaves
McKay Berrendo	1Y	30-005-62161	Chaves
Pronghorn Federal	1	30-005-62204	Chaves
Rugged Federal	1	30-005-62851	Chaves
West Fork Unit	1	30-005-62625	Chaves
West Fork Unit	2	30-005-62482	Chaves
West Fork Unit	4	30-005-62821	Chaves

West McKay Harvey Federal A	1	30-005-62189	Chaves
Woolworth Ranch Unit	1	30-025-26180	Lea

- (9) McKay is the operator of each of the wells.
- (10) The Application requested issuance of an order from the Division:
- Determining that McKay is in violation of Regulations 19.15.8, 19.15.5.9 and 19.15.25.8 NMAC;
 - Requiring McKay to provide the Oil Conservation Division with acceptable financial assurance within thirty (30) days of issuance of any order;
 - Requiring McKay to return to compliance with Regulations 19.15.5.9(A)(4) and 19.15.25.8 NMAC within sixty (60) days of the issuance of any order by returning the wells to production, plugging the wells in accordance with Regulation 19.15.25 NMAC, or transferring the wells to an operator who is in compliance with the requirements of Regulation 19.15.5.9 NMAC.
 - Determining that in the event McKay does not comply with the actions required within the time permitted, the Division should find that McKay is in violation of a Division Order, that the wells that are not in compliance should be declared abandoned, that the Oil Conservation Division should then plug the abandoned wells in accordance with a Division-approved plugging program and restore and remediate the location, recover its costs from McKay's financial assurance as required by Regulation 19.15.8.13 NMAC, and seek indemnification under NMSA 1978 § 70-2-14(E).
 - requiring Operator to return to compliance with 19.15.5.9 and 19.15.25.8 NMAC within sixty (60) days of the date of the order;
 - in the event of noncompliance, finding the Operator in violation of a Division order for each day after the deadline established in the sought order, declaring the wells abandoned, authorizing the Division to plug the violating wells in accordance with a Division approved plugging procedure and restore and remediate the location, recover costs from the posted financial assurance as permitted by 19.15.8.13 NMAC, and seek indemnification as permitted by NMSA 1978, § 70-2-14 (E).
- (11) Applicant presented as its witness Daniel Sanchez, the Oil Conservation Division's Compliance and Enforcement Manager. After being qualified as a witness, Mr. Sanchez testified:
- That he was knowledgeable of the Oil Conservation Division's records regarding McKay.
 - That the Oil Conservation Division's records regarding McKay were kept in the ordinary course of the Division's business.

- c. That McKay is the operator of record of the twenty (20) wells in Chaves County and one (1) well in Lea County which are the subject of this action.
- d. That the subject wells each have an "active" status;
- e. That monthly production reports on OCD Form C-115 for active wells are required 45 days after each month has ended;
- f. That the last form C-115 supplied to the Division by McKay for any of subject wells was for August 2016;
- g. That the August 2016 report showed only one well, the Woolworth Ranch Unit No. 1 (API No. 30-025-26180), had reported oil and gas production;
- h. That twenty (20) of McKay's twenty-one (21) wells have been inactive with no production for more than one (1) year plus ninety (90) days;
- i. That apart from the Woolworth Ranch Unit Well No. 1, the most recent production from any of the subject wells was in February of 2015;
- j. That the Bonnie No. 1 last produced in January of 1994;
- k. That Regulation 19.15.25.8 NMAC requires all the subject wells be properly plugged and abandoned, returned to production, or placed in approved temporary abandonment status
- l. That the Woolworth Ranch Unit No. 1 is the only well operated by McKay that is not currently in violation of 19.15.25.8 NMAC;
- m. That McKay is in violation of 19.15.5.9(A)(4) NMAC, which requires an operator to have a maximum of two (2) inactive wells if operator has less than one hundred (100) wells;
- n. That three (3) of the Operator's twenty-one (21) wells have inadequate financial assurance in violation of 19.15.8.9 NMAC: the Camp State No. 1 requires Eight Thousand Six Hundred-Fifty Dollars (\$8,650) in single well financial assurance; the McKay Berrendo No. 1Y requires Nine Thousand Ten Dollars (\$9,010) in single well financial assurance; and the West Fork Unit No. 4 requires Eight Thousand Four Hundred Dollars (\$8,400) in single well financial assurance.
- o. That the financial assurance deficiency for the three (3) wells totals twenty six thousand sixty dollars (\$26,060);
- p. That McKay has one (1) Fifty Thousand Dollar (\$50,000) blanket bond and two (2) single well bonds on file with the Division in the amount of Nine Thousand Two Hundred Ninety-Two Dollars (\$9,292) and Nine Thousand Five Hundred Seventy-Eight Dollars (\$9,578);

- q. All financial assurances for McKay are from RLI Insurance Company ("RLI") 2925 Richmond Ave, Suite 1600, Houston, TX 77098.

(12) Trustee Mazel provided no pre-hearing statement, or testimony.

(13) Interested parties McKay Petroleum Corporation, McKay Living Trust, and Schultz Oil and Gas Properties, did not present witnesses, but adduced in cross-examination of Daniel Sanchez:

- a. That McKay Oil Corporation has filed for Chapter 7 Bankruptcy protections;
- b. That authority to operate the properties in the bankruptcy estate lies with Trustee Mazel;

(14) Through their counsel, the interested working interest owners stated they would like to see the Woolworth Ranch Unit Well No. 1 transferred to another operator.

(15) The Division, through its counsel, stated the Division would not oppose a transfer of the Woolworth Ranch Unit Well No. 1 to another operator, registered and in good standing in New Mexico, so long as the transfer was authorized in accordance with applicable statutes and regulations.

THE DIVISION CONCLUDES AS FOLLOWS:

(16) Oil Conservation Commission Order No. R-9210 in Finding Paragraph (5), states that well abandonment rules are in place to prevent migration of fluids, prevent waste, protect correlative rights, and protect fresh waters.

(17) NMSA 1978, Section 70-2-14(B) provides, in relevant part, "If any of the requirements of the Oil and Gas Act [70-2-1 NMSA 1978] or the rules promulgated pursuant to that act have not been complied with, the Oil Conservation Division, after notice and hearing, may order any well plugged and abandoned by the operator or surety or both in accordance with Division rules."

(18) Regulation 19.15.5.10(B) NMAC authorizes the Division to commence compliance proceedings for violation of a provision of the Oil and Gas Act, NMSA 1978, Sections 70-2-1 through 70-2-38, or a provision of a rule or order issued pursuant to the act.

(19) McKay is the operator of record for the subject wells and is responsible for compliance with the Oil and Gas Act and Oil Conservation Rules.

(20) Chapter 7 Trustee for McKay is the person authorized by the Bankruptcy Code to Control McKay's acts.

(21) The testimony provided by Applicant and the representations of counsel at the hearing clearly established that McKay is in violation of Regulations 19.15.5.9, 19.15.8.9, and 19.15.25 NMAC.

(22) The Application should be approved.

IT IS THEREFORE ORDERED THAT:

(1) The Application of Oil Conservation Division Compliance and Enforcement Bureau for a compliance order against McKay finding same in violation of Regulations 19.15.5.9, 19.15.8.9, and 19.15.25.8 NMAC, for the twenty (20) subject wells, all located in Chaves County, New Mexico, is hereby approved.

(2) McKay shall post adequate financial assurance as required by Regulation 19.15.8.9 NMAC and the Division for all wells for which the Division has determined bonding is insufficient within thirty (30) days of the issuance of this Order. At this time the wells are: the Camp State Well No. 1 for which the amount of single well financial assurance is Eight Thousand Six Hundred Fifty dollars (\$8,650); the McKay Berrendo Well No. 1Y, for which the single well financial assurance in the amount of Nine Thousand Ten dollars (\$9,010); and the West Fork Unit Well No. 4, for which the single well financial assurance is Eight Thousand Four Hundred dollars (\$8,400).

(3) The following twenty (20) wells are in violation of 19.15.25.8 NMAC. 19.15.5.9 NMAC which requires an operator of fewer than one hundred (100) wells to have no more than two (2) wells out of compliance with 19.15.25.8: NMAC:

Well Name	Well No.	API No.	County
Antelope Federal	1	30-005-61661	Chaves
Antelope Federal	2	30-005-61766	Chaves
Antelope Federal	3	30-005-61774	Chaves
Bonnie	1	30-005-62551	Chaves
Camp State	1	30-005-61446	Chaves
Five Mile Tank Federal	2	30-005-61403	Chaves
Husky-McKay	1	30-005-61616	Chaves
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Inexco Federal	4	30-005-62382	Chaves
Inexco Federal	5	30-005-63601	Chaves
Inexco Federal	6	30-005-63740	Chaves
Jerry Don Federal	1	30-005-62221	Chaves
McKay B Federal	4	30-005-64082	Chaves
McKay Berrendo	1Y	30-005-62161	Chaves
Pronghorn Federal	1	30-005-62204	Chaves
Rugged Federal	1	30-005-62851	Chaves
West Fork Unit	1	30-005-62625	Chaves
West Fork Unit	2	30-005-62482	Chaves
West Fork Unit	4	30-005-62821	Chaves
West McKay Harvey Federal A	1	30-005-62189	Chaves

(4) The Operator shall bring the twenty (20) wells out of compliance with 19.15.25.8 NMAC into compliance with 19.15.25.8 NMAC within sixty (60) days of the issuance date of this order by accomplishing one of the following with respect to each well:

- a. causing the well to be plugged and abandoned in accordance with 19.15.25.8 NMAC and in accordance with a Division approved plugging program;
- b. restoring the well to production if the well is an oil and gas well; or
- c. causing the well to be temporarily abandoned with Division approval in accordance with 19.15.25.13 NMAC.

(5) If the Operator has not completed the ordering requirements within the prescribed period, the Operator shall be in violation of this order, and the Division shall be authorized:

- a. Subject to the applicable provisions of Title 11, United States Code, to plug and abandon the subject wells that are out of compliance with Division rules; and
- b. to recover costs from either the Operator or the United States Bureau of Land Management in accordance with 19.15.8.13 NMAC; and NMSA 1978, Section 70-2-14 (E) if funds available from applicable financial assurance are not sufficient to cover all costs which the Division incurs in plugging and abandoning the wells.

(6) If McKay cannot reasonably complete the work described above within the specified time, McKay may file, prior to the expiration of the deadlines set forth above, an application for hearing to request an extension. At hearing, McKay shall provide evidence of its good faith efforts at complying with this Order, the work completed to date, and why good cause exists for the extension. McKay shall also propose a revised schedule for completion of the required work.

(7) Jurisdiction of this case 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.



SEAL

STATE OF NEW MEXICO
OIL CONSERVATION DIVISION

DAVID R. CATANACH
Director