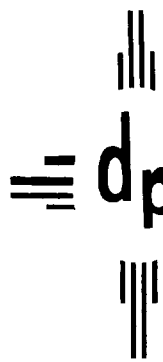


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dugan production corp.

MAY 28 1996

CONSERVATION DIVISION

May 24, 1996

Mr. Bill LeMay, Director
New Mexico Oil Conservation Division
2040 South Pacheco
Santa Fe, NM 87505

**Re: Application for Administrative Approval
Surface Commingling of Produced Liquids
Dugan Production Corp's Davis Federal No. 1
Unit L, Section 24, T-26N, R-11W
Federal Lease SF-078937
San Juan County, NM**

Dear Mr. LeMay,

We are writing to request your administrative approval for the surface commingling of the hydrocarbon liquids produced from the captioned well which is dually completed in the Gallegos Gallup associated oil and the Basin Dakota gas pools. Only the liquids are proposed to be commingled, the gas from each completion will continue to be metered and sold separately. All interest in each zone is common since only one lease is involved. The 40 acre Gallup spacing unit comprises the NW/4 SW/4 and the 320 acre Dakota spacing unit comprises the S/2 of Section 24. Dugan Production's Federal Lease No. SF-078937 covers the entire S/2 of Section 24 and both spacing units. Dugan Production Corp. has 100% working interest in both completions.

The Davis Federal No. 1 was completed as a dual well during August 1962, and as of April 1, 1996 has produced 2,037,887 MCF of gas and 9,585 bbls of oil from the Gallegos Gallup pool plus 970,827 MCF of gas and 6,999 bbls of condensate from the Basin Dakota pool. During the first three months of 1996 production from each zone was as follows:

	<u>Gallegos Gallup</u>	<u>Basin Dakota</u>
	<u>MCF + Bbl - Days On</u>	<u>MCF + Bbl - Days On</u>
January 1996	3529 + 18 - 31	2095 + 15 - 31
February 1996	2928 + 22 - 29	1244 + 2 - 29
March 1996	3073 + 18 - 31	1520 + 7 - 31

The liquids from the Gallup are light brown in color and are slightly paraffinic with gravities ranging from 50.8° to 56.8° API during the last three sales. The liquids from the Dakota are light

straw colored with gravities ranging from 59.2° to 61.6° API during the last three sales. The liquids from each zone are compatible and the commingled stream will actually be less of an operational problem than are the separate streams since the Dakota condensate will help minimize the tendency of the paraffinic Gallup to have a higher BS&W content. As for the liquid values, Dugan Production has a contract with Giant Refining for the sale of this production and we are not penalized for the high liquid gravities, thus the value of the individual streams should be the same as the value of the commingled stream and if the BS&W content of the Gallup oil is actually lowered as a result of this commingling, the commingled production will actually have a higher overall value than the individual streams.

Currently we are using two 210 bbl tanks to store production from the Davis Federal well, one for the Gallup and one for the Dakota. Produced volumes of liquids from each completion have declined over the past 34 years that this well has produced and from the above summary of production, during the first 3 months of 1996 it can be seen that the Gallup completion is currently averaging 19 bbls/month, and the Dakota completion 8 bbls/month. At these rates of production, it takes approximately 11 months for the Gallup and 25 months for the Dakota to accumulate sufficient volumes to haul. Our agreement with Giant Refining requires that we attempt to have a full load (200 bbls) of oil/condensate when we request that they haul our oil to be sold. The Gallup and Dakota together will accumulate a full load in approximately 7 months. The shorter times will benefit all parties in that the oil/condensate will not have to sit in storage so long before being sold which will result in less loss due to evaporation which is a common problem with higher gravity liquids such as exist at this well.

In addition, by producing both completions into one tank, the second tank can be used as a backup tank for use when the full tank is being sold rather than shutting in the well until the tank is emptied and resealed, as is the current practice.

Attachment No. 1 is a copy of the current well site security diagram which presents a schematic diagram of the existing facilities. Our proposal will entail tying together the oil lines from the Gallup and Dakota separators and manifolding the tanks to allow the combined oil line to produce into either tank. Each tank will have a valve which can be used to isolate that tank from the other.

Attachment No. 2 is a portion of our general well location map and, as can be seen, the Davis Federal No. 1 well is the only wellbore located on the S/2 of Section 24, T-26N, R-11W and as previously presented, is dually completed in the Gallegos Gallup and Basin Dakota pools. On Attachment No. 2 we have outlined the boundary of our lease which, in addition to the S/2 of Section 24, also includes the NW/4 of Section 24 and the SW/4 of Section 13. As can

be seen, Dugan Production also is the operator of two other wells located on the subject lease, the Platero Navajo No. 1 well (E-24-26N-11W) and the Platero Navajo No. 2 well (M-13-26N-11), both of which are completed in and produce from the Basin Dakota pool. Both of these wells have their own production facilities and neither well will be affected by the proposed surface commingling on the Davis Federal No. 1 well.

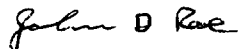
We propose that the commingled liquid hydrocarbon production be allocated between the Gallup and Dakota pools based upon factors determined annually during the required annual GOR test of the Gallup completion (and reported on NMOCD form C-116). Monthly production attributable to each zone will be calculated by applying a percentage factor to the commingled production. The percentage allocation factors will be determined by testing the Gallup to arrive at a percentage of the total volume that is from the Gallup with the remaining percentage being from the Dakota. Once these factors are determined, they will apply until the next annual test is taken and new factors determined.

Since the subject lease is federal acreage, we have reviewed our proposal with the Farmington District Office of the Bureau of Land Management (BLM) and do plan to provide them with a copy of this application; however, since only one federal lease is involved and all interest (working and royalty) is common, there is no required approval from the BLM.

In summary, we request administrative approval to surface commingle small volumes of liquid hydrocarbon production from the Gallegos Gallup and Basin Dakota pools in Dugan Production's Davis Federal No. 1 well. All interest is common and the commingled stream should have a value equal to or greater than the value of the individual streams. Only liquid production will be commingled, with gas production from each zone continuing to be metered and sold separately.

Should you have questions or need additional information, please let me know.

Sincerely,



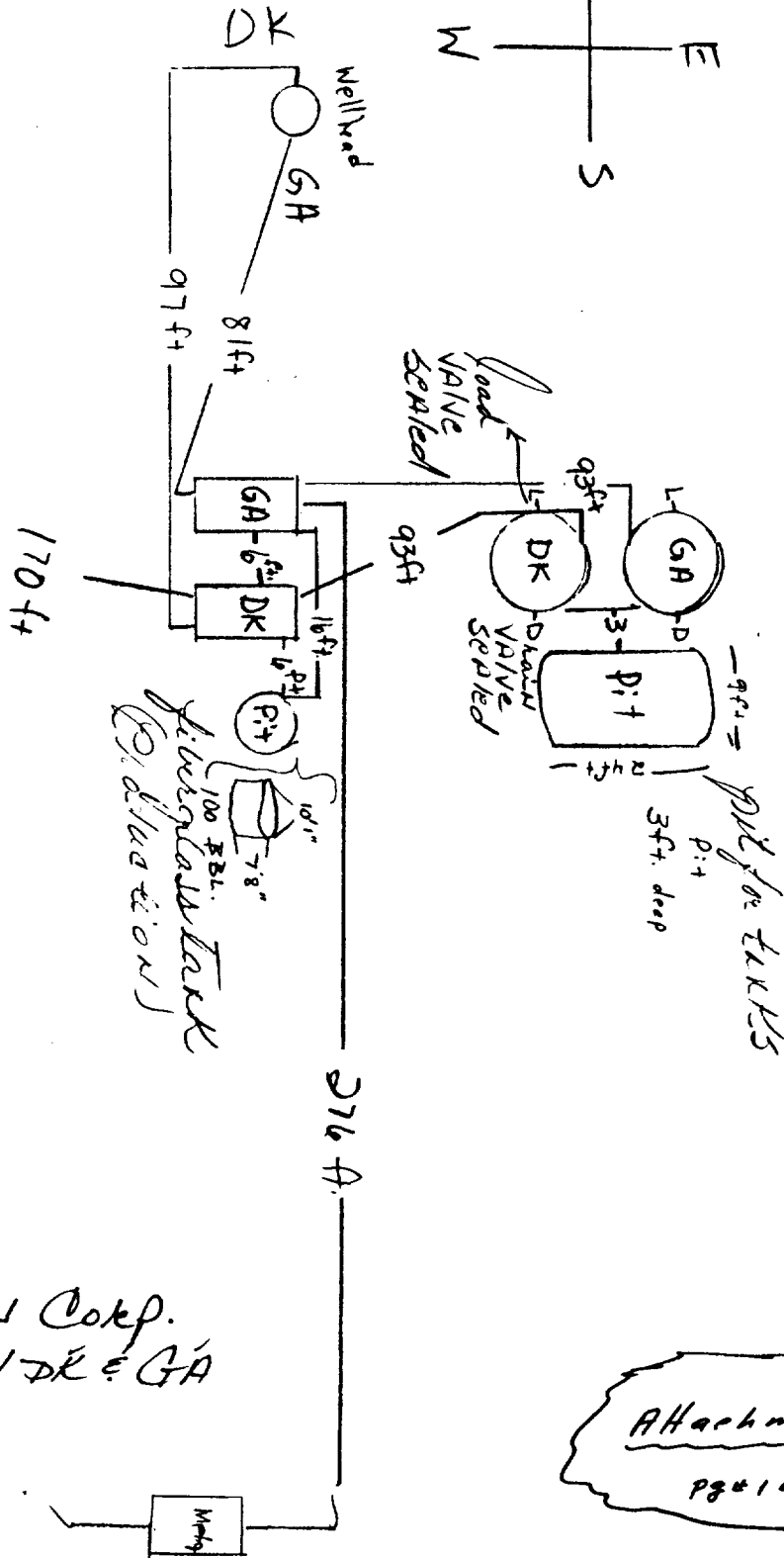
John D. Roe
Manager of Engineering

JDR/cg

attachs.

cc: NMOCD, Aztec
BLM, Farmington District Office

17044



Dugan Production Corp.
Davis Federal #1
NW 1/4, SW 1/4 Sec 24 T46N R11W
15E # SF 078937
San Juan Co N.M.

Dugan Production Corp.
Davis Federal #1 DR & GA
L 24-26N-11W
54-078937
San Juan,
New Mexico

Attachment No. 1

pg 1 of 1

