



January 11, 2012

**VIA HAND DELIVERY**

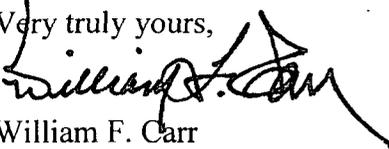
Ms. Florene Davidson  
Commission Clerk  
Oil Conservation Commission  
New Mexico Department of Energy,  
Minerals and Natural Resources  
1220 South Saint Francis Drive  
Santa Fe, New Mexico 87505

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Re: **PROPOSED ORDER WITH PROPOSED FINDINGS AND CONCLUSIONS**  
Oil Conservation Commission Case Nos. 14497 and 14538: Application Of David H. Arrington Oil & Gas, Inc. For Compulsory Pooling, Lea County, New Mexico, *And* Application Of Marshall & Winston, Inc. To Cancel Operator's Authority, Terminate A Spacing Unit, And Approve A Change Of Operator, Lea County, New Mexico

Dear Ms. Davidson:

Pursuant to the directions of the Oil Conservation Commission at the December 8, 2011 hearing in the above-referenced consolidated cases in which it granted my client's application, enclosed please find David H. Arrington Oil & Gas, Inc.'s *Proposed Order Of The Oil Conservation Commission*. The *Proposed Order* contains my client's proposed findings, conclusions, and orders. By copy of this letter, I am providing this Proposed Order to all parties of record in this case.

Very truly yours,  
  
William F. Carr  
Larry J. Montañño  
Attorneys for David H. Arrington Oil & Gas, Inc.

Enclosure

cc: Parties of record  
David K. Brooks, Esq.  
Oil Conservation Division

James Bruce  
Marshall & Winston, Inc.

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**STATE OF NEW MEXICO  
ENERGY, MINERALS AND NATURAL RESOURCES DEPARTMENT  
OIL CONSERVATION COMMISSION**

**IN THE MATTER OF THE HEARING  
CALLED BY THE OIL CONSERVATION  
COMMISSION FOR THE PURPOSE OF  
CONSIDERING:**

**APPLICATION OF MARSHALL & WINSTON, INC.,  
TO CANCEL AN OPERATOR'S AUTHORITY AND  
TERMINATE A SPACING UNIT AND APPROVE  
A CHANGE OF OPERATOR, LEA COUNTY, NEW MEXICO.**

**CASE NO. 14538**

**IN THE MATTER OF THE APPLICATION OF DAVID H.  
ARRINGTON OIL & GAS, INC., FOR COMPULSORY  
POOLING, LEA COUNTY, NEW MEXICO.**

**CASE NO. 14497  
ORDER NO. R-13372  
(DE NOVO)**

**DAVID H. ARRINGTON OIL & GAS, INC.'S  
PROPOSED ORDER OF THE OIL CONSERVATION COMMISSION**

**BY THE COMMISSION:**

**THIS MATTER** came before the Oil Conservation Commission ("Commission") for consideration on December 8, 2011, and the Commission, having considered the evidence in support and opposition to these applications, on this 23rd day of January, 2012,

**FINDS THAT:**

- (1) Due notice of the hearing on these applications has been given, and the Commission has jurisdiction of the parties to these cases and the subject matter thereof.
- (2) By its application in Case No. 14538, Marshall & Winston, Inc. ("Marshall & Winston"), seeks an order canceling the authority of David H. Arrington Oil & Gas, Inc., to operate the Green Eyed Squealy Worm Well No. 1 (API No. 30-025-36013), located 1974 feet from the South line and 1129 feet from the East line in the NE/4 SE/4 of Section 26, Township 15 South, Range 34 East, NMPM, Lea County, New Mexico. Marshall & Winston requests that it be designated operator of the well for a proposed reentry of the well to test an oil zone on 40-acre spacing in the Cisco Canyon formation.
- (3) By its application in Case No. 14497, David H. Arrington Oil & Gas, Inc. ("Arrington") seeks an order pooling all mineral interests from the surface to the base of the Upper Morrow formation in the S/2 of Section 26, Township 15 South, Range 34 East, NMPM, Lea County, New Mexico, to form a 320- acre gas spacing and proration unit for all formations and pools developed on 320- acre spacing

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within this vertical extent, including the North Edison-Morrow Gas Pool (76360), the Undesignated North Hume-Morrow Gas Pool (78850) and a 160-acre spacing and proration unit comprising the SE/4 of said Section 26 for all formations and pools developed on 160-acre spacing. Arrington proposes to dedicate these spacing and proration units to the Green Eyed Squealy Worm Well No. 1 (API No. 30-025-36013) located 1974 feet from the South line and 1129 feet from the East line in the NE/4 SE/4 of said Section 26. Arrington requests that it be designated operator of the well.

(4) These applications raise related issues and have been consolidated for the purposes of hearing.

(5) The Green Eyed Squealy Worm Well No. 1 was drilled in early 2004 by Arrington, as Operator and as the largest interest owner therein. The well produced gas from the Morrow formation until late 2007, when it was shut in. *See* Arrington Exhibit 2, Testimony of Kastner at 14. Arrington, Marshall & Winston and others paid their respective shares of the well costs. *See* Testimony of Kastner at p. 7; Testimony of Hammit at p. 61.

(6) Thereafter, Arrington proposed to Marshall & Winston a re-entry attempt under the JOA covering this acreage in the Cisco formation which Marshall & Winston declined. *See* Testimony of Kastner at Transcript p. 14; Testimony of Hammit at p. 65.

(7) Arrington's lease in the South half of Section 26 expired due to lack of production and the JOA covering this acreage expired by its own terms. Thereafter, Arrington acquired a new oil and gas lease covering this acreage and an easement from the surface owner to assure access to the well. *See* Arrington Exhibit Nos. 2 and 3; Testimony of Kastner at Transcript at pp. 15-16; Testimony of Hammit at p. 66. Marshall and Winston also have entered a surface use agreement with the surface owner. *See* Testimony of Hammit at p 73.

(8) Arrington owns 75% of the working interest in the South half of said Section 26 and Marshall & Winston own 25% of the working interest in the South half of the Section. Marshall & Winston owns 100% of the working interest in the NE/4 SE/4 of said Section which it proposes to dedicate to the Green Eyed Squealy Worm No. 1 if it successfully completes the well in the Cisco formation. *See* Testimony of Kastner at Transcript p.8; Testimony of Hammit at p. 68.

(9) With the assistance of new engineering employees who have experience in re-entering Morrow wells and re-establishing commercial production in this formation, Arrington re-evaluated the Morrow and determined that it was a good candidate for a re-entry attempt. *See* Testimony of Bucy at pp. 50-51.

(10) In March of 2010, Arrington sent a workover proposal to Marshall & Winston for a joint development effort in the Morrow formation, but they were unable to reach an agreement. *See* Testimony of Kastner at Transcript p. 15.

(11) The parties have been unable to reach an agreement for the development of the S/2 of this Section with a re-entry attempt in the Morrow formation of this acreage and, following Arrington's notice that it would seek a pooling order, each filed their respective applications in these consolidated cases. *See* Testimony of Hammit at pp. 70-71.

(12) The cases were heard by a Division Examiner on September 2, 2010 and, on March 16, 2011, the Division entered Order No. R-13372 granting the application of Marshall & Winston. *See* Order No. R-13372.

**The Evidence:**

(13) In support of its application in Case No. 14497, and in opposition to the application of Marshall & Winston in Case No. 14538, Arrington presented the following testimony:

- (A) Prior to being shut in, the Green Eyed Squealy Worm Well No. 1 produced more than 397 million cubic feet of natural gas, more than 11,000 barrels of oil and 17,000 barrels of water. *See* Testimony of Ball at p 26.
- (B) The Morrow zones in which Arrington proposes to attempt a re-entry are good quality sections of this formation and geologically correlate with other wells that have produced from offsetting Morrow wells. *See* Testimony of Ball at pp. 26 and 28.
- (C) In 2007, the well was not producing and it looked like a good candidate to attempt to clean up the well and bring it back onto production; however, Arrington could not get the swab down the well due to an obstruction in the tubing. After fracture stimulating the well, it still made too much water to produce on its own. *See* Testimony of Carrasco at p. 33.
- (D) When it was apparent that no agreement could be reached on completing the well in the Cisco formation, Arrington decided to take one more look at returning the well to production in the Morrow formation before abandoning that zone. *See* Testimony of Carrasco at p. 34.
- (E) Arrington's production engineer analyzed the well in April 2010 and based on Arrington's experience in its Bills Hopper Well and the recent results obtained by another operator of deep gas wells, he concluded that Arrington should add artificial lift to this well to lift the water off the Morrow formation, thereby permitting the well to produce. *See* Testimony of Carrasco at pp. 35-38, 41; Testimony of Bucy at pp. 50-52.
- (F) If this re-entry in the Morrow is not attempted before using the well to try to complete in the Cisco formation, it will be extremely difficult or impossible to later test the Morrow in this well and recover the remaining Morrow reserves under this acreage. *See* Testimony of Carrasco at 38.
- (G) Arrington presented an economic projection for the well using a commercial program called PHD Win that showed the well would be very economical with a return possible of as much as 1,000 percent and evidence that showed production from the well to be in excess of a BCF of gas and 48,000 bbls of oil. *See* Arrington Exhibit Nos. 8 and 9; Testimony of Bucy at 53.
- (H) Arrington believes that the reentry attempt can be completed within 90 days depending on the current condition of the wellbore. *See* Testimony of Carrasco at 39.

(I) Marshall & Winston recently conducted some work on this wellbore, and Arrington is therefore unaware of its current condition. If the condition of the well is such that it requires more than 90 days to complete this reentry, Arrington may need additional time to complete the reentry attempt. *See* Testimony of Carrasco at p. 39

(14) In support of its application in Case No. 14538, and in opposition to the application of Arrington in Case No. 14497, Marshall & Winston presented the following testimony:

(A) Marshall & Winston presented reserve and economic estimates showing Arrington's proposed reentry to be a marginal prospect. *See* Testimony of Savage at pp. 81-84.

(B) The Maxwell 26 Well No. 1 (the "Maxwell well") is located in the northwest quarter of Section 26 and dedicated to acreage in which neither Arrington or Marshall & Winston owns an interest. It is the only well that produces from the Morrow reservoir in Section 26. *See* Testimony of Savage at p. 88.

(C) The Maxwell well has produced for more than 10 years, and continues to produce from this Morrow reservoir. *See* Testimony of Savage at p. 97.

(D) Marshall & Winston estimates there remain approximately 1.8 BCF to be recovered out of this Morrow reservoir. *See* Testimony of Savage at pp. 86-89.

(E) The Morrow sand that is the subject of Arrington's application extends across all of Section 26. *See* Testimony of Savage at p. 87.

(F) Although some Morrow wells in Lea County, New Mexico that have been shut in and then returned to production come back on at their original producing rates (Savage at 100), their average producing rates after being shut in is 53 percent of their original producing rates. *See* Testimony of Savage at p. 93.

(G) Marshall & Winston has commenced re-completion operations on the Green Eyed Squealy Worm Well No. 1 and Arrington will have to squeeze the new perforations before it can attempt its reentry. *See* Savage at p. 94-96. Arrington has also dropped a fish in the well that can result in problems when an operator attempts to reenter a well. *See* Testimony of Savage at p. 96.

**ARRINGTON'S APPLICATION:**

(15) Division Order No. R-13372 also denied the application of Arrington concluding:

Section 70-2-17.C NMSA 1978, as amended provides that the Division shall issue compulsory pooling orders "to avoid the drilling of unnecessary wells or to protect correlative rights, or prevent waste. Thus David H. Arrington Oil & Gas, Inc. as applicant for compulsory pooling, bears the burden of proving, by appropriate geological and engineering evidence, that pooling should be granted for one or more of those reasons, *See Simms v. Mechem*, 72 N.M. 186, 382 P.2d 183 (N.M. 1962). Surprisingly they had not calculated the expected economics and reserves of the recompletion procedure." Order No. R-13372, Conclusions Regarding Legal Issues, Paragraph E, p. 5.

(16) As observed by the Division's Order No. R-13372 in these cases, to obtain a compulsory order the Applicant must establish that granting its application avoids the drilling of unnecessary wells, or protects correlative rights, or prevents waste. *See* Order No. R-13372, Conclusions Regarding Legal Issues, Paragraph E, p. 5.

**UNNECESSARY WELLS:**

(17) Marshall & Winston testified that Morrow reserves are present throughout Section 26 (Savage at 105) and under the South half of Section 26 there are 1.8 BCF of Morrow gas reserves to be recovered. *See* Testimony of Savage at p. 89.

(18) Unless another well is completed in the South half of Section 26, there will be no opportunity for the owners of the Morrow reserves to produce their share of these reserves. *See* Testimony of Savage at p. 106.

(19) The Green Eyed Squealy Worm Well No. 1 is connected to the common Morrow reservoir under Section 26 and, if capable, could produce the reserves under the south half of this Section. *See* Testimony of Savage at p. 108.

(20) To determine if the Green Eyed Squealy Worm Well No. 1 is capable of producing these Morrow reserves under the south half of Section 26, the owners of these reserves must to test the formation. *See* Testimony of Savage at p. 111.

(21) If this re-entry is not approved, the only way to test and produce Morrow reserves under the South half of Section 26 is to drill another well which, if unsuccessful, would have to be plugged and abandoned.

(22) The drilling of an additional well to test the Morrow formation under the South half of Section 26 would be an unnecessary well.

**FINDING:** Approval of Arrington's application will avoid the drilling of an unnecessary well and should be **GRANTED**.

**PROTECTS CORRELATIVE RIGHTS:**

(23) The Oil and Gas Act (the "Act") imposes on the Commission the duty to protect correlative rights. *See* Section 70-2-33.H NMSA 1978.

(24) The Act defines "Correlative Rights" as:

"the opportunity afforded, so far as it is practicable to do so, to the owner of each property in a pool to produce without waste his just and equitable share of the oil or gas or both in the pool, being an amount, so far as can be practically determined, and so far as can be practically obtained without waste, substantially in the proportion that the quantity of recoverable oil or gas or both under the property bears to the total recoverable oil or gas or both in the pool, and for such purpose to use his just and equitable share of the reservoir energy.

(25) For an operator to obtain its just and reasonable share of the reserves under a tract, a well is required. *See* Testimony of Savage at p. 106

(26) Arrington seeks an opportunity to produce its just and equitable share of the remaining Morrow reserves under the South half of Section 26 and to do so desires to use the Green Eyed Squealy Worm Well No. 1.

(27) Marshall & Winston testified that, while every situation is different (Savage at 124), you do not know what you can produce from the Morrow until you drill a well. *See* Testimony of Savage at p. 103.

(28) Marshall and Winston acknowledged that it would not have to participate in the Arrington reentry attempt (Testimony of Savage at p. 109) and that, if Arrington's reentry attempt was successful, all owners in the south Half of Section 26 would share in the production from the well. *See* Testimony of Savage at pp.110 -111

**FINDING:** To deny Arrington the opportunity to attempt to return the Green Eyed Squealy Worm Well No. 1 to production in the Morrow formation would impair the correlative rights of Arrington. Arrington's application should be **GRANTED.**

**PREVENTION OF WASTE:**

(29) The Oil and Gas Act charges the Division with the duty to prevent of waste of oil and gas. Section 70-2-11.A NMSA 1978.

(30) The Act defines "Underground Waste" as follows:

"Underground Waste" as ... the locating, spacing, drilling, equipping, **operating or producing, of any well or wells in a manner to reduce or tend to reduce the total quantity of crude petroleum oil or natural gas ultimately recovered from any pool,** ..." Section 70-2-3.A NMSA 1978. Emphasis added.

(31) Arrington's undisputed geological evidence shows there is a potentially productive zone in the Morrow formation under the South half of Section 26. *See* Testimony of Ball at p. 26.

(32) Arrington presented engineering testimony that showed, based on its experience with another Morrow well and on the experience of other Morrow operators, that by pumping water off the Morrow formation, the well could be returned to production and the total recovery of crude oil or natural gas can be increased from the well. *See* Arrington Exhibit 9; Testimony of Carrasco at pp. 36-38; Testimony of Bucy at pp. 50-53.

(33) Marshall & Winston admitted that if the owners of the reserves under the South half of Section 26 could not test the Morrow formation and attempt to re-establish production from this formation, reserves could be left in the ground. *See* Testimony of Savage at p. 111.

**FINDING:** The denial of Arrington's application could tend to reduce the total quantity of crude petroleum oil or natural gas recovered from this pool and, therefore, the application should be **GRANTED.**

(34) Arrington presented engineering calculations that showed that a successful reentry of the Green Eyed Squealy Worm Well No. 1 could result in the recovery of an additional 1 BCF of natural gas and 48,000 barrels of oil (Arrington Exhibit 9, Testimony of Bucy at 53) at an estimated value of \$2.37 million. See Arrington Exhibit 8; Testimony of Bucy at 52-53.

(35) David H. Arrington Oil & Gas, Inc. should be designated the operator of the subject well and of the units.

(36) Pursuant to Division Rule 35.A, any pooled working interest owner who does not pay its share of estimated well costs should have withheld from production its share of reasonable well costs plus an additional 200 percent thereof as a reasonable charge for the risk involved in the re-entry of the Green Eyed Squealy Worm Well No. 1.

(37) Reasonable charges for supervision (combined fixed rates) should be fixed at \$8,000.00 per month while drilling and \$800 per month while producing, provided that these rates should be adjusted annually pursuant to Section III.1.A.3. of the COPAS form titled "Accounting Procedure-Joint Operations." The operator should be authorized to withhold from production the proportionate share of both the supervision charges and the actual expenditures required for operating the well, not in excess of what are reasonable, attributable to each pooled working interest.

**FINDING:** To avoid the drilling of unnecessary wells, to protect correlative rights, prevent waste and afford to the owner of each interest in the units the opportunity to recover or receive without unnecessary expense its just and fair share of hydrocarbons, Arrington's application should be **GRANTED** by pooling all uncommitted interests, whatever they may be, in the oil and gas within the units.

**IT IS THEREFORE ORDERED THAT:**

(1) The application of Marshall & Winston, Inc. in Case No. 14538 for an order canceling the authority of David H. Arrington Oil & Gas, Inc., to operate the Green Eyed Squealy Worm Well No. 1 (API No. 30-025-36013), is hereby **DENIED**.

(2) The application of David H. Arrington Oil & Gas, Inc. in Case No. 14497 is hereby **GRANTED** and all uncommitted interests whatever they may be from the surface to the base of the Upper Morrow formation underlying the South half of Section 26 Township 15 South, Range 34 East, NMPM, Lea County, New Mexico, are hereby pooled in the following manner:

The S/2 to form standard 320-acre spacing and proration unit for any formations and/or pools spaced on 320-acres within this vertical extent which presently include but are not necessarily limited to the including the North Edison-Morrow Gas Pool (76360), the Undesignated North Hume-Morrow Gas Pool (78850); and

The SE/4 to form a standard 160-acre spacing and proration unit for all formations and pools developed on 160-acre spacing.

(3) These units shall be dedicated to the David H. Arrington Oil & Gas, Inc.'s Green Eyed Squealy Worm Well No. 1 (API No. 30-025-36013), located 1974 feet from the South line and 1129 feet from the East line in the NE/4 SE/4 of said Section 26.

(4) David H. Arrington Oil & Gas, Inc., the Applicant in Case No. 14497, is hereby designated the operator of the well and of these units.

(5) The operator of said unit shall commence the reentry the well within 90 days of the entry of this order, and shall thereafter continue reentry operations on the well with due diligence to re-establish production from the Morrow formation.

(6) In the event the operator does not commence the reentry of the proposed well on or before the date prescribed in Ordering Paragraph No. (5), Ordering Paragraph No. (1) shall be of no effect, unless said operator obtains a time extension from the Division Director for good cause.

(7) Should the proposed reentry of the well not be completed within 90 days after commencement thereof, the operator shall appear before the Division Director and show cause why Ordering Paragraph No. (2) should not be rescinded.

(8) Upon final plugging and abandonment of the proposed well, the pooled unit created by this Order shall terminate, unless this Order has been amended to authorize further operations.

(9) After pooling, uncommitted working interest owners are referred to as "pooled working interest owners." ("Pooled working interest owners" are owners of working interest in the units, including unleased mineral interests, who are not parties to an operating agreement governing the units.) After the effective date of this order, the operator shall furnish the Division and each known pooled working interest owner in the units an itemized schedule of estimated well costs of drilling, completing, and equipping the proposed well ("well costs").

(10) Within 30 days from the date the schedule of estimated well costs is furnished, any pooled working interest owner shall have the right to pay its share of estimated well costs to the operator in lieu of paying its share of reasonable well costs out of production as hereinafter provided, and any such owner who pays its share of estimated well costs as provided above shall remain liable for operating costs but shall not be liable for risk charges. Pooled working interest owners who elect not to pay their share of estimated well costs as provided in this paragraph shall thereafter be referred to as "non-consenting working interest owners."

(11) The operator shall furnish the Division and each known pooled working interest owner (including each non-consenting working interest owner) an itemized schedule of actual well costs within 90 days following completion of the proposed 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 the schedule, the actual well costs shall be deemed to be the reasonable well costs. If there is an objection to actual well costs within the 45-day period, the Division will determine reasonable well costs after public notice and hearing.

(12) Within 60 days following determination of reasonable well costs, any pooled working interest owner who has paid its share of estimated well costs in advance as provided above shall pay to the operator its share of the amount that reasonable well costs exceed estimated well costs and shall receive from the operator the amount, if any, that estimated well costs that it has paid exceeds its share of reasonable well costs.

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

- (a) the proportionate share of reasonable well costs attributable to each non-consenting working interest owner; and
- (b) as a charge for the risk involved in drilling the well, 200 percent of the above costs (see Division Rule 35.A).

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

(15) Reasonable charges for supervision (combined fixed rates) are hereby fixed at \$8,000.00 per month while drilling and \$800.00 per month while producing, provided that this rate shall be adjusted annually pursuant to Section III.1.A.3 of the COPAS form titled "*Accounting Procedure-Joint Operations.*" The operator is hereby authorized to withhold from production the proportionate share of both the supervision charges and the actual expenditures required for operating the well, not in excess of what are reasonable, attributable to each pooled working interest owners.

(16) Except as provided in Ordering paragraphs (13) and (15) above, all proceeds from production from the well that are not disbursed for any reason shall be placed 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 the escrow agent within 30 days from the date of first deposit with the escrow agent.

(17) 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 this order. Any well costs or charges that are to be paid out of production shall be withheld only from the working interests' share of production, and no costs or charges shall be withheld from production attributable to royalty interests.

(18) Should all parties to this compulsory order reach voluntary agreement subsequent to entry of this order, that portion of this order authorizing compulsory pooling shall thereafter be of no further effect.

(19) The operator of the well and unit shall notify the Division in writing of the subsequent voluntary agreement of all parties subject to the compulsory pooling provisions of this Order.

(20) Jurisdiction is hereby 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 COMMISSION

JAMI BAILEY  
Chair

ROBERT BALCH  
Commissioner

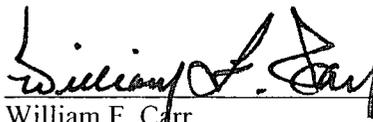
SCOTT DAWSON  
Commissioner

SEAL

CERTIFICATE OF SERVICE

I certify that on January 11, 2012, I served a copy of the foregoing document to the following by Facsimile.

James Bruce, Esq.  
Post Office Box 1056  
Santa Fe, New Mexico 87504  
FAX NO. (505) 982-2151



William F. Carr  
Larry J. Montañó