

**MINUTES OF THE MEETING
OF THE OIL CONSERVATION COMMISSION
HELD ON OCTOBER 20-21, 2011**

The Oil Conservation Commission met at 9 o'clock a.m. on October 20, 2011 in Porter Hall, Wendell Chino Building, 1220 S. St. Francis Drive, Santa Fe, New Mexico.

PRESENT: SCOTT DAWSON, Member
ROBERT BALCH, Member
JAMI BAILEY, Chair

Cheryl Bada served as the Commission counsel.

The meeting was called to order by Chairman Bailey. The minutes of the September 22, 2011 Commission meeting were approved and adopted.

Reopened Case 14161, the application of Targa Midstream Service LP to amend Order No. R-13052, was called for final action. Chairman Bailey announced that the final order in this case is not ready to be signed, and final action in this case will be continued to the Commission meeting scheduled for November 17, 2011.

Case 14744, the application of the New Mexico Oil Conservation Division for notice of rulemaking concerning the repeal, adoption and amendment of rules issued pursuant to the Oil and Gas Act, NMSA 1978, Sections 70-2-1 through 70-2-38. The hearing concerns the following changes in Title 19, Chapter 15 of the New Mexico Administrative Code: amend Parts 14 and 16. Chairman Bailey announced that, under Division Rule 19.15.3.12 NMAC, certain procedures must be followed in rulemaking hearings including: providing a sign-in sheet for parties wishing to present non-technical testimony or public statements; providing for technical testimony and cross-examination if a pre-hearing statement has been received; and allowing opening and closing statements. She said that if the hearing continues for more than one day, public statements will be taken at the end of each session.

Appearances were made by Gabrielle Gerholt for the Oil Conservation Division (OCD); William F. Carr for the New Mexico Oil and Gas Association (NMOGA) with Michael Feldewert representing the Holland and Hart Law Firm and Carol Leach for Concho; Ocean Munds-Dry for Lynx Petroleum Consultants, Inc. (Lynx); Karin Foster for the Independent Petroleum Association of New Mexico (IPANM); and Patrick Fort for Jalapeno Corporation (Jalapeno).

Ms. Gerholt addressed several preliminary issues. She said that David Brooks' power point testimony was put on slides which she presented as an exhibit to the Commission. She submitted amended Exhibits 2 and 13 which were accepted without objection. She made a motion that the testimony of Jalapeno and Harvey E. Yates Company (HEYCO) witnesses be limited to the issue of a project area for horizontal wells and that compulsory pooling and risk factor testimony not be allowed, because these issues were not included in the notice of this hearing. Mr. Fort responded that he believes the Oil Conservation Commission does not have authority to create project areas under State law. Ms. Gerholt gave the definition of "proration unit" that is in the OCD Rules and Regulations and explained why she believes the compulsory pooling rule applies to horizontal project areas. Harvey E. Yates, Jr. clarified Jalapeno's position on project areas and voiced the concern that project areas are being imposed on existing proration units. He asked if he could address this issue in a public statement if he is not allowed to

testify. After a brief discussion, the Commission unanimously decided to deny Ms. Gerholt's motion to limit testimony.

Ms. Gerholt submitted Exhibit 1, the affidavit of notice of this hearing, which was accepted. She made an opening statement explaining the reason for the proposed amendment to the rules and identifying the OCD witnesses and their presentations. Mr. Carr made an opening statement explaining NMOGA's participation in meetings with majors and independents on the subject matter after which a draft amendment was presented to the OCD. He stated that NMOGA is in support of OCD's proposed amendment.

Ms. Gerholt's first witness was Richard Ezeanyim, Chief Engineer and Chief Hearing Officer with the OCD in Santa Fe, New Mexico. He explained the purpose of the hearing is to adopt amendments to the current rules, which do not adequately address horizontal well drilling. He stated that in June of 2011 a work group was formed to study proposed amendments to the current rules for horizontal well drilling. He said that NMOGA's draft was used as a starting point. He stated his belief that the proposed amendments will prevent waste and protect correlative rights. The witness was excused.

The next witness was David Brooks, Assistant General Counsel and Legal Examiner for the OCD in Santa Fe. He described the difference in the "producing interval" used in the current rule and the "completed interval" in the proposed rule. He stated that if the completed interval is adopted, there will be a decrease in NSL applications. He explained why definitions of a "horizontal well" and "project area" are necessary. He described the difference between a standard and non-standard project area and suggested additional language for the proposed rule amendments. He discussed the proposal on allowables for project areas with multiple proration units. He talked of setbacks and simultaneous dedication. He said that the existing well density rules are designed for vertical wells. He explained that the compulsory pooling rule will apply to horizontal wells and project areas, and he believes the appropriate course is to address the compulsory pooling of horizontal well project areas on a case by case basis. He described the difference between a project area and a unitized area. The direct testimony of Mr. Brooks was concluded, and his cross-examination was postponed at this time.

Public statements were presented as follows:

Rachel Jankowitz with the New Mexico Department of Game and Fish – in support of any action the Commission can take to facilitate horizontal drilling, as she believes it will protect wildlife because of the reduction of the amount of surface impact.

A request was made and granted to take witnesses out of order because of travel constraints.

Ms. Munds-Dry's witness was Larry Scott, President of Lynx Petroleum Consultants, Inc. in Hobbs, New Mexico. He told of a case before the Commission last year in which he was offered forced pooling for a horizontal well. He said the examiner granted the compulsory pooling; he appealed the decision, and the Commission denied the compulsory pooling. He said the operator had the subject well completed and producing by the time the appeal was held. He said he has reviewed the proposed rules and has developed the opinion that the compulsory pooling of interests in a horizontal well project area will not protect correlative rights. He said that if compulsory pooling is allowed in a horizontal well project area, it should not be in the form of unitization. He said that aggressive operators in southeast New Mexico might use the compulsory

pooling for the taking of acreage. Ms. Gerholt cross-examined the witness, and he was excused.

Mr. Fort's witness was Arlene Rowland, Vice President for Harvey E. Yates Company in Roswell, New Mexico. She stated that she does not believe the Legislature has authorized the Commission to allow compulsory pooling for horizontal well project areas. She said that the compulsory pooling rule only applies to a spacing or proration unit, not to a horizontal well project area. She suggested some changes to the proposed rule amendments. She asked that the charge for the risk involved in drilling compulsory pooled wells be adjusted downward. Ms. Gerholt, Mr. Feldewert and Chairman Bailey cross-examined the witness, and she was excused.

Mr. Carr's witness was Ken McQueen, Director for the San Juan Region with Williams Exploration and Production in Tulsa, Oklahoma. He described the limitations of the current horizontal well rule. He described different completion techniques used in horizontal wells. He said the proposed rules will make it easier for operators to access gas reserves economically. Ms. Gerholt cross-examined the witness, and he was excused.

Mr. Brooks was recalled for cross-examination. Mr. Fort, Commissioner Dawson, Commissioner Balch and Chairman Bailey cross-examined the witness, and he was excused.

Richard Ezeanyim was recalled to present technical testimony. He defined a horizontal well as a directional well with one or more laterals and listed the advantages and disadvantages of horizontal wells. He presented examples of horizontal wells and explained the difference between "producing interval" under the current rule and "completed interval" under the proposed rule. He said that spacing rules in pools will not apply to horizontal wells. Chairman Bailey cross-examined the witness, and he was excused.

Ms. Leach's witness was Jan Preston Spradling, Senior Landman with Concho Resources, Inc. in Midland, Texas. She described Concho's history of drilling horizontal wells. She said she was a member of the OCD task force that formulated the draft rule being presented at this hearing and was also a member of the NMOGA Regulatory Practices committee that initiated the draft rule. She said that Concho supports the proposed rule changes. She said the proposed rule does not change in any way the process for obtaining a compulsory pooling order. She advised that compulsory pooling rules allow operators to challenge the 200% risk factor in compulsory pooling cases. She said that horizontal wells allow operators to recover more reserves. Mr. Fort cross-examined the witness, and she was excused.

Mr. Feldewert's witness was Charles Creekmore, Staff Landman with ConocoPhillips in Farmington, New Mexico. He said he was part of the NMOGA sub-committee that drafted the rules and presented them to the Regulatory Practices Committee and also served on the OCD task force. He discussed standard and non-standard project areas and notice requirements. He talked of drainage, lateral re-entries and new drills. He said the new rule will allow new wells to be drilled without affecting existing Joint Operating Agreements. He proposed some corrections to typos in the proposed rule. Mr. Fort cross-examined the witness, and he was excused.

The meeting was recessed at 4:30 p.m.

The meeting was reconvened at 9:00 a.m. on October 21, 2011. The meeting was called to order by Chairman Bailey. She said the Commission would like to recall certain

witnesses, and David Brooks was recalled. Commissioner Balch inquired whether designating the well with several multiple laterals would impact current regulations regarding multiple completions in a wellbore or would impact commingling. Mr. Brooks said that the OCD rules state that a horizontal or directional well will not be considered a dual completion, but that is in some part of the rules that is not being changed. He said he assumes they will be producing through different channels or the operators will apply for downhole commingling. The witness was excused.

Richard Ezeanyim was recalled and was asked by Commissioner Balch if there are existing rules to deal with multiple completions in a well. He said there are rules in place for downhole commingling. He said if a multi-lateral produces from different sources of supply, the operator will be required to apply for downhole commingling. Ms. Gerholt quoted the original rule as saying that commingled production will be prohibited unless an operator applies for downhole commingling. The witness was excused.

Mr. Fort's witness was Harvey E. Yates, Jr., President of Jalapeno Corporation in Roswell. He told of his experience with forced pooling and horizontal drilling in New Mexico. He presented the history of the origin of forced pooling and spacing rules. He said he does not believe the Commission has jurisdiction to impose another proration unit or project area over the original proration unit. He said he is recommending that the forced pooling portion of the rules be limited. He explained his interpretation of what the new rule will allow concerning the drilling of horizontal wells in the area of an existing well. He said if compulsory pooling is allowed in previously established drilling units, it will facilitate the taking of property and will impair contracts. He discussed the 200% risk penalty and pointed out that the statute does not require the assessing of the full 200%, only up to 200%. He suggested that during a compulsory pooling hearing involving a horizontal well, the Division should investigate the actual drilling risks. He said that some operators use forced pooling as a gathering of leases. Ms. Gerholt, Mr. Feldewert, Commissioner Dawson, Commissioner Balch and Chairman Bailey cross-examined the witness, and he was excused.


Chairman Bailey announced that Division Rule 19.15.3.11.B.2 NMAC requires that all exhibits that will be presented at the hearing be attached to the pre-hearing statement and submitted five business days before the hearing. She said the Commission will accept all of the amended and additional exhibits presented at this hearing but, in the future, the OCD rule will be observed.

The Commission counsel advised the Commission to confine itself to the case that was advertised and not address the issue of compulsory pooling, but pointed out that other legal issues were brought up in Mr. Yates' testimony, so the case will be left open in order that the attorneys can brief the Commission on these issues. The Chairman asked that proposed findings of fact, conclusions of law and briefs be submitted by November 21, 2011. The briefs need to address whether the Commission has authority to allow compulsory pooling in horizontal well project areas.

Closing statements were made by Mr. Fort, Mr. Carr and Ms. Gerholt. Chairman Bailey asked for public statements, and there were none. The case was continued to the Commission meeting scheduled for December 8, 2011.

The meeting was adjourned at 11:24 a.m.

**STATE OF NEW MEXICO
OIL CONSERVATION COMMISSION**



JAMI BAILEY, Chair