

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. 13,526

APPLICATION OF CHESAPEAKE OPERATING,)
INC., FOR APPROVAL OF A UNIT AGREEMENT,)
LEA COUNTY, NEW MEXICO)

ORIGINAL

REPORTER'S TRANSCRIPT OF PROCEEDINGS

EXAMINER HEARING

BEFORE: DAVID R. CATANACH, Hearing Examiner

July 28th, 2005

Santa Fe, New Mexico

2005 AUG 11 AM 8:53

This matter came on for hearing before the New Mexico Oil Conservation Division, DAVID R. CATANACH, Hearing Examiner, on Thursday, July 28th, 2005, at the New Mexico Energy, Minerals and Natural Resources Department, 1220 South Saint Francis Drive, Room 102, Santa Fe, New Mexico, Steven T. Brenner, Certified Court Reporter No. 7 for the State of New Mexico.

* * *

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July 28th, 2005
 Examiner Hearing
 CASE NO. 13,526

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<u>MICHAEL S. BRAUN</u> (Landman)	
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A P P E A R A N C E S

FOR THE DIVISION:

GAIL MacQUESTEN
Deputy General Counsel
Energy, Minerals and Natural Resources Department
1220 South St. Francis Drive
Santa Fe, New Mexico 87505

FOR THE APPLICANT:

KELLAHIN & KELLAHIN
117 N. Guadalupe
P.O. Box 2265
Santa Fe, New Mexico 87504-2265
By: W. THOMAS KELLAHIN

* * *

1 WHEREUPON, the following proceedings were had at
2 8:27 a.m.:

3
4
5 EXAMINER CATANACH: At this time I will call Case
6 13,526, the Application of Chesapeake Operating, Inc., for
7 approval of a unit agreement, Lea County, New Mexico.

8 Call for appearances.

9 MR. KELLAHIN: Mr. Examiner, I'm Tom Kellahin of
10 the Santa Fe law firm of Kellahin and Kellahin, appearing
11 this morning on behalf of the Applicant, and I have one
12 witness to be sworn.

13 EXAMINER CATANACH: Okay, can I get the witness
14 to please stand to be sworn in?

15 (Thereupon, the witness was sworn.)

16 MR. KELLAHIN: Mr. Catanach, Mr. Braun and I were
17 asked to take on a task that I had thought was impossible,
18 and it appears that it might be possible now.

19 We were asked at the last minute to form a state
20 exploratory unit. Chesapeake holds two expiring state
21 leases. They're due to expire on August 1st.

22 With the assistance of Pete Martinez at the State
23 Land Office, we have obtained preliminary approval. And
24 with the assistance of Yates Petroleum Corporation, Chuck
25 Moran, we've received this morning from Ocean the necessary

1 partial joinder of the unit, so that Chesapeake will have
2 the required 75-percent commitment of the working interest
3 ownership.

4 And with that document, then, Mr. Martinez
5 assures us that we are eligible for final approval of the
6 unit.

7 I've asked Mr. Braun, who's done all the detailed
8 land work, to come this morning and to be available to
9 answer any questions and help me describe to you what we
10 have done with this case.

11 In addition, we have some geologic exhibits that
12 were prepared by Mr. Doug Bellis of Chesapeake. Mr. Bellis
13 is on vacation, and I do not have his testimony in the form
14 of an affidavit. I do, however, have his exhibits and what
15 he e-mailed to me as his geologic write-up. If you desire
16 to have that attested to by Mr. Bellis, I can do that
17 subsequent to the hearing.

18 In addition, because of the time constraints, the
19 Land Office has requested that we impose upon the Division
20 in order to obtain an approved order by the Division of
21 this unit before the end of the day tomorrow. I know
22 that's highly unusual, and we would appreciate you
23 considering accommodating us.

24 The last exhibit I have presented to you is a
25 suggested draft form of approval, using the Division's

1 normal format for approval of state units, and with your
2 permission we'll submit that shortly.

3 EXAMINER CATANACH: Okay.

4 MR. KELLAHIN: With that introduction --

5 EXAMINER CATANACH: By the way, after speaking
6 with you yesterday I checked on the status of the Director,
7 and I am told by Ms. Florene Davidson that he will not be
8 in today or tomorrow.

9 However, he's supposedly coming in on Saturday
10 morning to check to see if there's anything that needs to
11 be done. So I told Florene that we could just leave the
12 order ready to be signed on Saturday, if that's suitable to
13 you guys.

14 MR. KELLAHIN: That'll be fine. I'll be at work
15 on Saturday, and I'll contact him and make sure that I can
16 get a copy of it.

17 EXAMINER CATANACH: Okay.

18 MR. KELLAHIN: But we're going to go ahead today
19 and file for final approval with the Land Office, and I'll
20 tell Mr. Martinez that the plan is to hopefully have the
21 approved order on Saturday for his files, and we'll see if
22 that satisfies his requirements.

23 With your permission, then, I'll ask Mr. Braun
24 some questions, and we'll proceed through the information.

25 EXAMINER CATANACH: Okay.

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MICHAEL S. BRAUN,

the witness herein, after having been first duly sworn upon his oath, was examined and testified as follows:

DIRECT EXAMINATION

BY MR. KELLAHIN:

Q. Mr. Braun, for the record, sir, would you please state your name and occupation?

A. Michael S. Braun. I'm a consulting landman.

Q. On prior occasions have you testified and qualified as an expert petroleum landman before the Division?

A. Yes.

Q. And pursuant to your employment and that expertise, have you been retained by Chesapeake Operating, Inc., to consolidate the necessary land matters and deal with those details in order to attempt to form what they have called the South Chavlea State Exploratory Unit?

A. Yes.

Q. And at this point in time, do you believe you've accomplished those necessary tasks?

A. Yes.

MR. KELLAHIN: We tender Mr. Braun as an expert petroleum landman.

EXAMINER CATANACH: He is so qualified.

Q. (By Mr. Kellahin) Let's start with what is

1 marked as Exhibit Number 1, Mr. Braun. Would you identify
2 for the Examiner what this document is?

3 A. This is the State Land Office form, State
4 Exploratory Unit agreement, and it has been prepared naming
5 Chesapeake as the unit operator, describing the lands
6 within the unit, and including Exhibits "A", "B" and "C",
7 which are standard form exhibits to the unit agreement.

8 Q. To the best of your knowledge, has this
9 particular copy of the State-approved unitization agreement
10 form been modified to incorporate the changes that the
11 Commissioner of Public Lands requested be made based upon
12 the preliminary application?

13 A. Yes.

14 Q. When we turn through the exhibit, do you have an
15 Exhibit "A" that outlines the tracts to be included within
16 the exploratory unit?

17 A. Yes. Exhibit "A", the dashed line indicates the
18 unit boundary. Within the dashed line, or within the unit
19 boundary or the separate tracts or individual leases, all
20 of which are State of New Mexico oil and gas leases,
21 they're enumerated by tract number. It correlates to
22 Exhibit "B", which indicates each individual lease. It's
23 lessor/lessee serial number, expiration date, et cetera.

24 Q. Turning past Exhibit Number 1, would you identify
25 for us what is marked as Exhibit Number 2?

1 A. Exhibit Number 2 is the unit operating agreement,
2 and this is for our proposed South Chavlea State
3 Exploratory Unit. It describes the lands covered by the
4 unit the various operating procedures that would govern the
5 parties who would commit to the unit agreement and lists in
6 Exhibit A the working interest owners, their percentage
7 interest, if so committed to the unit.

8 Exhibit "B" is -- I mean, excuse me, Exhibit "A"
9 1 is an exhibit very similar to Exhibit "B" of the unit
10 agreement. It details each of the leases. And then
11 various other exhibits. COPAS, Exhibit "C"; gas-balancing
12 agreement, Exhibit "D". Excuse me, Exhibit "D" is the
13 insurance provision for the operator, the nonoperators.
14 Exhibit "E" is the gas-storage and balancing agreement.
15 And Exhibit "F" is a form of memorandum of operating
16 agreement to be filed in the county.

17 Q. Do you have a subsequent exhibit that breaks out
18 all the interests so that -- We'll talk about that in a
19 minute, but do you have a spreadsheet that shows all the
20 individual tract interests?

21 A. Yes.

22 Q. And we can talk about the status of commitment
23 based upon that exhibit.

24 Let's turn now, Mr. Braun, to Exhibit Number 3.
25 Would you identify for us what this letter is?

1 A. This is a letter from the State of New Mexico,
2 Public Land -- State Land Office, and it is a preliminary
3 approval letter which gives preliminary approval of the
4 proposed exploratory unit, subject to certain changes,
5 corrections and amendments to our original proposal. It's
6 dated July 13th, 2005.

7 Q. Have you gone through this letter and satisfied
8 yourself that as of today we have all the necessary
9 documents to submit to the Commissioner of Public Lands to
10 satisfy all the conditions of final approval?

11 A. Yes, I have.

12 Q. If you'll turn to Exhibit 4, would you identify
13 for Mr. Catanach what Exhibit 4 is?

14 A. Exhibit 4 is a copy of all documents filed for
15 the well record of our proposed initial test well for the
16 proposed unit. The well is named the Chavlea 19 State
17 Number 1 well, and these are copies of documents that are
18 on file with the Conservation Division in the form of the
19 proposal to drill a well.

20 Q. Is this one of the document sets that the
21 Commissioners asked you to submit for final approval of the
22 unit for their purposes?

23 A. This is.

24 Q. When I look at the locator map, there's a C-102
25 associated with this well. Has there been an amendment

1 that's being processed and filed for the acreage dedication
2 associated to the initial unit well?

3 A. Yes, this original form C-102 was filed with a
4 dedicated acreage plat indicating the south half of Section
5 19 to be dedicated to the initial well. However,
6 Chesapeake intends to, and I believe is in the process of,
7 amending that acreage dedication plat to include the west
8 half of Section 19 as the dedicated acreage to the initial
9 well.

10 Q. That's one of the requests that Chuck Moran of
11 Yates asked Chesapeake to make, is to re-orient the spacing
12 unit so that the Yates tract, which was the east half of
13 Section 19, does not have acreage dedicated to the initial
14 discovery well?

15 A. Yes.

16 Q. Let's turn now to the spreadsheet, and let's
17 describe to Mr. Catanach what the status is with regards to
18 the various tracts. It may be helpful, Mr. Braun, if you
19 go back and, in association with Exhibit Number 5, let's
20 take the unit agreement, Exhibit 1, fold it back until you
21 can get the unit map, Exhibit "A", which will give us a
22 visual reference of how these tracts are organized.

23 A. This spreadsheet is a worksheet that I have used
24 to calculate the total acres proposed within the unit. If
25 I could start with the first column, it lists the tract

1 number, which is correlative to the Exhibit "A" Tract
2 number on the unit agreement. Column B is the number of
3 acres within that tract.

4 Column C -- or column 3, is the participation
5 percentage that that tract would represent in comparison to
6 the total unit acreage.

7 Column 4 is an indication of whether that
8 particular tract has been committed to the unit and its
9 gross acres committed to the unit. Therefore you end up
10 with a column total at the bottom of total number of acres
11 committed to the unit.

12 The next column is the Chesapeake share of the
13 unit, based upon acreage owned by Chesapeake within the
14 unit boundaries, as a percentage of the total acres within
15 the unit.

16 The next column is Chesapeake's committed acreage
17 to the unit, as a percentage of the total unit. And
18 likewise, you have similar two-column sections for each of
19 the parties that own a leasehold within the unit: Yates,
20 the Roderic Crandall Testamentary Trust, Me-Tex Oil and
21 Gas, Inc., and Marshall and Winston, Inc.

22 And in each case Yates has indicated in the first
23 -- their first column as their share of the unit, would be
24 the total acreage owned by Yates within the unit boundary.
25 And then the next column for Yates is Yates' committed

1 share, wold be only those tracts that they have agreed to
2 commit to the unit, and that percentage and how it bears to
3 the total acreage within the unit.

4 To summarize, Chesapeake has committed all their
5 acreage within the unit boundary to the unit, providing
6 them with a 73.326220-percent interest within the unit.

7 Yates did own 17.782520-percent acreage leasehold
8 within the unit, has committed not all of their acreage but
9 some of it, which gives them a 4.521307-percent interest
10 within the unit.

11 The Crandall interest, they have not made up
12 their mind whether they're going to -- they're still
13 contemplating whether to commit to the -- any acreage to
14 the unit.

15 The same is with Me-Tex Oil and Gas, Inc., still
16 in the process of making a decision.

17 And Marshall and Winston, Inc., has committed
18 their one-only tract to the unit, and providing them a
19 2.260653-percent interest in the unit, and that's a
20 percentage of the total tracts committed to date.

21 So if I haven't totally confused you, I hope that
22 with this -- to date this morning, we have Chesapeake with
23 93.218040-percent interest within the unit as to tracts
24 committed to the unit, Yates with 4.521307 percent, and
25 Marshall and Winston with 2.260653 percent, representing

1 approximately 80 percent of the tracts within the unit that
2 have been committed to the unit.

3 Q. Is it your understanding from Mr. Martinez at the
4 State Land Office, if you can get signatures for
5 ratifications of at least 75 percent of the working
6 interest ownership, then the Commissioner of Public Lands
7 will give you final approval for a unit?

8 A. Yes.

9 Q. And you have met that threshold here?

10 A. Yes.

11 Q. Let's turn now to the technical documents, Mr.
12 Braun. Describe for us what is identified as Number 6.

13 A. Exhibit 6 is the authorization for expenditure
14 estimate of Chesapeake, the proposed unit operator, in the
15 drilling of the initial test well for the unit. It
16 describes the drilling of an 11,400-foot Morrow test with a
17 total completed well cost of \$1.587 million.

18 Q. Turn to Exhibit Number 7. Have you reviewed
19 Exhibit Number 7, Mr. Braun?

20 A. Yes.

21 Q. To the best of your knowledge, does it now
22 include all the additional details that Mr. Martinez asked
23 Chesapeake to describe in its geologic summary when we
24 submit this for final approval by the Commission of Public
25 Lands?

1 A. Yes, it does.

2 MR. KELLAHIN: By way of explanation, Mr.
3 Catanach, if you'll take a moment and unfold Exhibit Number
4 10, you can see a Morrow isopach. I think that's the
5 cross-section, Mr. Catanach. That is the cross-section
6 of -- if you'll look at the cross-section first, that is
7 Mr. Bellis's cross-section of this area where he's tied in
8 key component wells. And from this information he was able
9 to construct an isopach. So if you'll turn to Exhibit
10 Number 8, you can see from Exhibit Number 8 how he has
11 organized the technical data to show you this Morrow
12 channel and its orientation through this area.

13 The outline of the unit itself is the area shaded
14 in purple. There's an old noncommercial attempt in the
15 north half of Section 24. It shows 28 feet and it shows a
16 small volume of gas produced. When you look at Mr.
17 Bellis's geologic summary, there's a paragraph that
18 describes and discusses that well.

19 And so when Mr. Bellis is looking at formulating
20 a proposed unit area, he's identified with open black
21 circles five potential location within the outline of the
22 unit. And you can see most of those open black circles are
23 within the 20-foot-or-greater isopach thickness of the
24 channel that he has depicted on the exhibit.

25 Of these potential locations, Mr. Bellis's

1 summary will show you that he has keyed in on his
2 preference to pick the location in Section 19, which is in
3 the southwest southwest of 19. You'll see that circle is
4 right towards the eastern edge of the 30-foot contour line.

5 His reason for doing this is explained by looking
6 at Exhibit Number 9. Exhibit 9, then, is -- and I believe
7 your copy is a colored copy, Mr. Catanach -- it is the same
8 isopach that has been geologically overlaid on a 3-D
9 seismic timeline.

10 The point here is to illustrate Mr. Bellis's
11 opinion that there is a structural component to the channel
12 and that it's necessary for him to move towards the eastern
13 edge of the thickness in order to gain structural
14 elevation, which has a particular random pattern as you
15 look at the timeline for the 3-D seismic pattern. But that
16 random pattern shows that among the opportunities in the
17 channel, the point of highest structural position is going
18 to be the well in the southwest southwest of 19, if you're
19 choosing among the five locations to choose from.

20 So that's his argument, and that's his
21 preference.

22 And then finally, Mr. Examiner, Exhibit 11 is my
23 attempt to draft a proposed order for the Division to
24 approve this unit and allow us, then, to go back to the
25 Commissioner of Public Lands and get the unit finally

1 approved and move forward. We have made plans to put a
2 spudder on the location on Sunday so that we can have
3 drilling activities occurring across the end of the
4 expiration period of the two expiring leases that are
5 associated with the unit.

6 Q. (By Mr. Kellahin) And for the record, Mr. Braun,
7 if you'll take a moment and help me remember the tracts on
8 Exhibit "A" of Exhibit 1 that are associated with the
9 expiring leases --

10 A. Tracts Number 6 and 7 are two separate State of
11 New Mexico leases with an expiration date of August the
12 1st, 2005. So if you would look at Exhibit A to the unit
13 agreement, you would notice Tract 6 to include the northern
14 part of Section 24 and the tract in the southern part of
15 Section 24. And then Tract 7 being the north half -- in
16 our plat here, being the north half of Section 25. Those
17 two leases are slated to expire August the 1st.

18 MR. KELLAHIN: With your permission, Mr.
19 Catanach, if you'll allow me after the hearing to make
20 copies of Mr. Braun's letter that Ocean provided this
21 morning, so that we can include that as Exhibit Number 10,
22 we will then have Yates' ratification of the tract they've
23 chosen to commit to the unit.

24 And with doing so, that would then conclude our
25 presentation.

1 EXAMINER CATANACH: Okay. What do we want to
2 admit, Exhibits 1 through 9 at this time? Oh, I'm sorry --

3 MR. KELLAHIN: It would be 1 through 11.

4 EXAMINER CATANACH: Exhibits 1 through 11 will be
5 admitted, and you may provide that Yates letter after the
6 hearing.

7 EXAMINATION

8 BY EXAMINER CATANACH:

9 Q. Do you anticipate any further joinder from these
10 parties?

11 A. I really don't have a feeling yet as to their
12 decision. I've had some verbal conversations with the
13 Crandall Trust, and I just don't have an indication whether
14 they -- I have not talked to any representative of Me-Tex
15 Oil and Gas.

16 MR. KELLAHIN: Those two companies have been
17 provided with documentation --

18 THE WITNESS: Yes.

19 MR. KELLAHIN: -- concerning their choice?

20 THE WITNESS: Yes, they have.

21 EXAMINER CATANACH: Did we provide them notice of
22 the hearing, Mr. Kellahin?

23 MR. KELLAHIN: I don't have any indication that I
24 provided notice from my office. But they were sent Federal
25 Express packages showing all their elections and advised

1 that this matter is a voluntary matter in which they have
2 the absolute right not to participate, and if they do so,
3 it's on a voluntary basis.

4 EXAMINER CATANACH: I'm not -- I don't recall
5 right offhand what the Rule says about the notice on
6 voluntary units. If their interest -- If they choose not
7 to participate in the unit, they're not affected at all?

8 MR. KELLAHIN: That's right, and we've always
9 taken that attitude. I've struggled for years with the
10 fact that I'm not clear why we bring these to you anymore.
11 Historically, before the Land Office had a technical staff,
12 way back in the days of Johnnie Walker and Pete Porter, the
13 Land Office imposed upon the Commission to have a hearing
14 process where issues about unitization could be discussed
15 with your technical staff. And now that the Land Office
16 has their own geologists and engineers, I'm at a loss to
17 understand why we do this.

18 But to directly answer your question, this is a
19 voluntary matter, and the decision you make on our
20 Application does not affect them. If they choose not to
21 participate, then we must come back later. And if their
22 tract is in a spacing unit, then we'd have to pool their
23 interest.

24 As with the Yates interest, they've made an
25 election as to one tract. The agreements -- the State unit

1 agreement, provides a mechanism within the contract that
 2 Yates can change their mind and come in later and make an
 3 election as to the east half of Section 19.

4 So the answer to your question is, there's
 5 nothing that we understand that you're about to do that
 6 adversely affects those parties.

7 EXAMINER CATANACH: And normally in this
 8 situation, we would include the application and include all
 9 of the acreage that you proposed, but still that wouldn't
 10 have any effect on them, even if we included them in the
 11 unit.

12 MR. KELLAHIN: That's exactly right.

13 EXAMINER CATANACH: So -- Okay. All right, we'll
 14 just let it go. I think it's okay. I mean, I don't see
 15 that it's a problem.

16 MR. KELLAHIN: I'd be the first to tell you, Mr.
 17 Catanach, if I didn't think this would work.

18 EXAMINER CATANACH: Okay. Anything further?

19 Okay, there being nothing further, Case Number
 20 13,526 will be taken under advisement.

21 And this hearing is adjourned.

22 (Thereupon, these proceedings were concluded at
 23 8:55 a.m.)

24 I do hereby certify that the foregoing is
 * * * a complete record of the proceedings in
 the Examiner hearing of Case No. 13526
 heard by me on April 27, 2005
Daniel R. Catanach, Examiner
 STEVEN T. BRENNER, CCP
 (505) 989-9317 Conservation Division

CERTIFICATE OF REPORTER

STATE OF NEW MEXICO)
) ss.
COUNTY OF SANTA FE)

I, Steven T. Brenner, Certified Court Reporter and Notary Public, HEREBY CERTIFY that the foregoing transcript of proceedings before the Oil Conservation Division was reported by me; that I transcribed my notes; and that the foregoing is a true and accurate record of the proceedings.

I FURTHER CERTIFY that I am not a relative or employee of any of the parties or attorneys involved in this matter and that I have no personal interest in the final disposition of this matter.

WITNESS MY HAND AND SEAL July 28th, 2005.



STEVEN T. BRENNER
CCR No. 7

My commission expires: October 16th, 2006