

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. 13,538

APPLICATION OF READ AND STEVENS, INC.,)
FOR A NONSTANDARD OIL PRORATION UNIT,)
LEA COUNTY, NEW MEXICO)

ORIGINAL

REPORTER'S TRANSCRIPT OF PROCEEDINGS

EXAMINER HEARING

BEFORE: WILLIAM V. JONES, JR., Hearing Examiner

August 11th, 2005

Santa Fe, New Mexico

This matter came on for hearing before the New Mexico Oil Conservation Division, WILLIAM V. JONES, JR., Hearing Examiner, on Thursday, August 11th, 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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August 11th, 2005
Examiner Hearing
CASE NO. 13,538

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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:

JAMES G. BRUCE
 Attorney at Law
 P.O. Box 1056
 Santa Fe, New Mexico 87504

* * *

1 WHEREUPON, the following proceedings were had at
2 10:30 a.m.:

3 EXAMINER JONES: Okay, let's call Case 13,538,
4 Application of Read and Stevens, Inc., for a nonstandard
5 oil proration unit, Lea County, New Mexico.

6 Call for appearances.

7 MR. BRUCE: Mr. Examiner, Jim Bruce of Santa Fe,
8 representing Read and Stevens, Inc. I have two witnesses.

9 EXAMINER JONES: Any other appearances?

10 Will the witnesses please stand to be sworn?

11 (Thereupon, the witnesses were sworn.)

12 MR. BRUCE: Mr. Examiner, I think you're aware,
13 this Application was originally filed administratively, and
14 due to an objection it was placed on the hearing docket,
15 and we will address those issues today.

16 JOHN C. MAXEY, JR.,

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

19 DIRECT EXAMINATION

20 BY MR. BRUCE:

21 Q. Could you please state your name for the record?

22 A. John Maxey.

23 Q. And who do you work for and in what capacity?

24 A. Read and Stevens, I'm a petroleum engineer.

25 Q. Have you previously testified before the Division

1 as an engineer?

2 A. Yes, I have.

3 Q. And are you familiar with matters related to this
4 Application?

5 A. Yes, I am.

6 MR. BRUCE: Mr. Examiner, I'd tender Mr. Maxey as
7 an expert petroleum engineer.

8 EXAMINER JONES: How do you spell your last name?

9 THE WITNESS: M-a-x-e-y.

10 EXAMINER JONES: Mr. Maxey is qualified as an
11 expert petroleum engineer.

12 Q. (By Mr. Bruce) Mr. Maxey, could you refer to
13 your Exhibit 1 and identify that for the Examiner?

14 A. Okay. Exhibit 1 is a survey plat of Section 17,
15 19 South, 39 East. You'll notice a location staked, an
16 orthodox location, in the lower right-hand corner of the
17 plat.

18 Q. An orthodox location?

19 A. An orthodox, yes. And this plat is a survey of
20 all of Section 17. Section 17 is truncated on the east
21 side, because of the state line, the Texas state line.

22 So what I've attempted to depict on this plat
23 was, the dashed lines within the section are your standard
24 governmental quarter-quarter sections, with the exception
25 of the ones on the east side which are truncated by the

1 state line.

2 And the solid line is what we had applied for
3 originally, administratively, was to take care -- set up
4 some nonstandard proration units to try to handle the way
5 this section was cut off on the east side.

6 Q. Okay, so Section 17 is comprised of what, the
7 west half and then plus lots 1 through 4?

8 A. That's correct.

9 Q. And we'll get into this in a minute, but the west
10 half is fee land, I believe? And Mr. Watson can confirm
11 this.

12 A. Yes.

13 Q. And then the lots are federal land?

14 A. That's correct, 1 through 4.

15 Q. And you are proposing to drill what type of well?

16 A. A San Andres oil well.

17 Q. And spacing for that would normally be on the
18 statewide 40 acres?

19 A. That's correct.

20 Q. And what would the well setbacks be for that?

21 A. 330.

22 Q. Okay. Now, looking at this -- So what you want
23 to do is, rather than have eight 40-acre units and then
24 have some odd-shaped units comprised of the federal lots,
25 you basically want to form eight oversized well units?

1 A. That's correct, to help enhance our options on
2 spacing.

3 Q. Okay. Also, if you look -- if you formed a well
4 unit, say, just out of lot 4, well locations could be kind
5 of constrained in there, could they not?

6 A. Yes, if you were to utilize the 40-acre locations
7 in the west half, probably the likely scenario would be to
8 take two of the lots, put them together for a long
9 proration unit north-south and a narrow one east-west.

10 The thing I didn't want to get into as an
11 engineer is, the nearest production to this is nearly two
12 miles away. So if this thing develops back to the east,
13 into Texas, what will happen is, we'll be forced to drill
14 some wells on some very narrow spacing. And we don't want
15 to do that right now. We could have some very small
16 drainage patterns there, making the wells uneconomic.

17 Q. Having the larger well units would also give you
18 flexibility in well locations, would it not?

19 A. That's correct.

20 Q. So to take a step back, the administrative
21 application that you filed was to approve eight nonstandard
22 units, correct?

23 A. That's correct.

24 Q. Today we are only here for the one nonstandard
25 unit in the southeast part of this section?

1 A. That's correct.

2 Q. Okay. And that's the way -- The administrative
3 application went to Mr. Stogner, I believe?

4 A. That's right.

5 Q. And he set it for hearing only for this well?

6 A. That's right, when he came back with the hearing
7 notice, it was only for the one in the southeast.

8 Q. Okay. Could you move on to your Exhibit 2 and --

9 A. Okay.

10 Q. -- discuss this just a little -- in a little more
11 detail?

12 A. Exhibit 2 is a land plat I've blown up, and I
13 just wanted to illustrate -- This was part of the
14 application, as a matter of fact, it was Exhibit A of the
15 application, administrative application.

16 This exhibit just breaks down the land ownership.
17 The north half -- excuse me -- yes, the north half of the
18 northwest quarter is fee. You can see it broken into four
19 pieces, four fee pieces, and they're described with an
20 arrow pointing to each one.

21 And then of course the very east side, the narrow
22 strip, being the federal tract.

23 Q. Okay. So lots 1 through 4 are a single federal
24 tract, in essence; is that correct?

25 A. Yes.

1 Q. And the other -- so what you would -- when you --
2 If you obtain approval to form the nonstandard units, what
3 will be done -- there will have to be a communitization
4 agreement for the eastern well units; but for the western
5 well units, they would all be single tracts and no
6 special --

7 A. That's right.

8 Q. -- communitization or pooling --

9 A. Right --

10 Q. -- would be necessary --

11 A. -- that's correct.

12 Q. -- in this area?

13 A. I believe that Mr. Stogner also -- the second
14 reason for the -- excuse me, the first reason in his letter
15 for this hearing was because we were not on one standard
16 lease, and we were going to have to have a com unit --

17 Q. Okay.

18 A. -- or com agreement, I'm sorry.

19 Q. Let's move on to your Exhibit 3. What does that
20 depict?

21 A. This is a structure map of the top of the San
22 Andres structure in the area. And just trying to
23 familiarize everybody with what we're doing, Section 17 is
24 the section that we have our location in. You'll notice
25 I've written on there where the Texas/New Mexico state line

1 is. You can clearly see the east -- that strip of sections
2 up against the line are -- they're all truncated.
3 Something has to be done as far as proration units. And
4 you can see that we're drilling a subtle nose. There are
5 several that run through there.

6 And this map was put together with some
7 subsurface data, which is sparse in the area, and we were
8 helped out with a couple of 2-D seismic lines in the area
9 too. So the project is not very delineated with subsurface
10 data. There's some room to maneuver, and we hope this
11 develops, this idea we have for the nose.

12 Q. Where is the nearest production?

13 A. It would be up in the Foster field, just off the
14 map to the north, pretty much -- and it's just on the east
15 side of Hobbs, really, is where it is.

16 Q. Okay, is there any -- So what did you say, about
17 two -- two or more miles?

18 A. Yeah, just about two -- just above this map, or
19 this map --

20 Q. Okay.

21 A. -- so over two miles.

22 Q. So if this idea pans out, you would like to drill
23 additional wells in Section 17?

24 A. Yes.

25 Q. And with the larger well units, of course, there

1 would be a slightly higher allowable for this, would there
2 not?

3 A. There would.

4 Q. What is the approximate depth of the San Andres
5 here?

6 A. Forty- -- we're going 4800 feet, so --

7 Q. The allowable is what, 80 barrels a day, I think?

8 A. I believe that's correct at that depth, yes.

9 Q. Okay. So a slightly oversized unit would
10 increase that allowable --

11 A. Yes.

12 Q. -- a little bit? Which you hope to achieve, I
13 presume?

14 A. Yes, definitely hope to achieve that.

15 Q. And again, by having these oversized units you
16 can obtain -- or rather -- Let's look at it this way: If
17 you're looking at, say, a 26-acre well unit, your well
18 locations would mainly be north-south, because you couldn't
19 be more than 330 feet to the east or west lines of one of
20 those lots; is that correct?

21 A. That's correct. And if we have -- if this does
22 develop, we will want to probably offset as close as we can
23 to the east, across the Texas line, so -- And then if we
24 move to the west, we'll probably want to stay close to the
25 discovery also, and what we do is sandwich that well in

1 there, in those narrow proration units, if that's how this
2 were set up.

3 Q. In your opinion, are the nonstandard units
4 justified on an engineering basis?

5 A. Yes, they are.

6 Q. Do you believe that the granting of this
7 Application is in the interest of conservation and the
8 prevention of waste?

9 A. Yes, I do.

10 Q. And were Exhibits 1 through 3 prepared by you or
11 under your supervision?

12 A. Yes.

13 MR. BRUCE: Mr. Examiner, I'd move the admission
14 of Exhibits 1 through 3.

15 EXAMINER JONES: Exhibits 1 through 3 are
16 admitted into evidence.

17 EXAMINATION

18 BY EXAMINER JONES:

19 Q. Mr. Maxey, if you did apply for nonstandard
20 spacing and nonstandard -- you could also apply for
21 nonstandard locations for the wells on the extreme eastern
22 side, couldn't you?

23 A. You mean from the --

24 Q. If they were --

25 A. -- standpoint of setbacks?

1 Q. Yeah.

2 A. Yes, I could. I'm still dealing with a very
3 narrow strip of land there, but what I'm trying to not get
4 into is if this situation, this play, develops, that if I
5 were on a nonstandard unit that just was comprised of the
6 federal strips --

7 Q. Uh-huh.

8 A. -- I would be in a very narrow range there when I
9 stepped out to the west side, I will probably move 330 off
10 of the proration unit that we just drilled in. So I'm 660
11 away from this well that's spotted.

12 And then on the east side, in Texas, I'm going to
13 come up to -- as close as I can on the Texas -- under their
14 proration rules. And so I've got a well that's going to be
15 on a 27-acre lot that's -- my drainage radius is
16 drastically cut down.

17 Whereas if I'm going with equidistant nonstandard
18 proration units, I have an option to drill eight wells in
19 there, and under the administrative rules I can drill one
20 infill on an administrative process. So I have quite a bit
21 of flexibility on how this thing develops on spacing.

22 And the San Andres can be flooded. If this were
23 to develop as a potential for secondary recovery, I'm going
24 to have better spacing as far as waterflood recovery.

25 Q. As far as equidistance between wells?

1 A. Well -- Yes, as far as the spacing for trying to
2 maybe establish as we develop the patterns on something
3 that's going to be more reliable as injectors and
4 producers, versus being constrained on this because of the
5 state line and these narrow proration units on the east
6 side.

7 Q. So from just looking at this, you could drill the
8 40-acre tracts on the west and then you drill those 27-acre
9 tracts on the -- next to the state line. A lot of San
10 Andres goes down to 20-acre spacing anyway, you know, and
11 you'd be drilling 27-acre spacing to start with. Of
12 course, they'll be narrow.

13 Q. They'll be narrow, and if the drainage pattern
14 establishes itself such that I'm drilling half-million-
15 dollar wells now, at the costs that we incur today, and I'm
16 drilling on 27-acre spacing, it sets up a situation where
17 I'm not really drilling economic wells or potentially
18 economic wells. I don't know yet how these are going to
19 come on.

20 Q. I see, I see. I was assuming that you -- that
21 these weren't going to be -- you knew a little bit about
22 the San Andres out here, but you don't know that much about
23 it?

24 A. I -- No, I don't know that much in this area. We
25 have the Foster field to the north, but the Foster field is

1 comprised of four wells -- five wells, excuse me -- and
2 they're spread out over about a mile and a half. So that
3 information is sparse.

4 And I don't -- The closest dry hole we have in
5 the San Andres is back up -- it's on the map, back up to
6 the north northwest. See it in the corner of Section 7?

7 Q. Okay.

8 A. And as a matter fact, we participated -- or at
9 least we have the information from that well, and that's
10 the closest, really, subsurface data that I've got.

11 Q. Okay.

12 A. So my concern is that, you know, if we had a lot
13 more information, if we had something that was a
14 development well and we were dealing with these narrow
15 proration units -- You know, the situation may change.

16 But as of right now, to step out here and we're
17 in this corner, based on the science we have, I just didn't
18 want to start out in a box, my first well being on a 27-
19 acre -- You know, they can go down to 20-acre spacing, some
20 San Andres do, but that's well into the life of a project,
21 and you understand the reservoir and you're making an
22 economic decision based on a lot of data, and we have
23 sparse data.

24 Q. Of course the oil price is pretty good right now.

25 A. The oil price is good, that's right. And that

1 gets back to, you know, when you look at a top- -- if you
2 could tell me they're top-allowable wells, or somebody
3 could, you know, I'm sure you could sit here and look at
4 this and say, Hey, this isn't going to hurt us, this 27-
5 acre.

6 But I just don't know. This was a dry hole; the
7 closest subsurface data I have is a dry hole. So I may be
8 making -- You know, if I end up making a well that's making
9 10 barrels a day, that's still going to be tough.

10 Q. Is this structure map above sea level or below
11 sea level? It must be above sea level, because you said
12 that was a kind of a subtle nose.

13 A. Well, it's based on --

14 Q. You said --

15 A. These are subsea depths on this map.

16 Q. Okay, hm.

17 A. Negative 860.

18 Q. That means you're drilling in a channel then,
19 kind of; is that right?

20 A. Let's see.

21 Q. Well, the geologist would -- I don't know if Mr.
22 Watson is a geologist or --

23 A. No, he's a landman.

24 Well, we're moving updip to the west; that's why
25 the negative numbers are getting smaller.

1 Q. Okay, yeah, but your first well is going to be to
2 the east, so you're going to move downdip --

3 A. Well, there's an updip pinchout, we feel like --

4 Q. Oh, okay.

5 A. -- because if you follow this up to the north,
6 into the Foster field, they drilled some updip tight wells.
7 So you're right, looking at that -- I see what you're
8 saying now. To the west is a pinchout, and to the east is
9 a downdip oil-water contact.

10 Q. Okay.

11 A. So that's how we're -- We're trying to base it on
12 some of the subsurface data up to the north in the Foster.

13 Q. Okay. Now --

14 A. And that's not depicted on here. Our geologist
15 did not take what he perceived an oil-water contact over
16 two miles to the north and just brought it down, he didn't
17 do that.

18 Q. Okay.

19 A. It's a stratigraphic play.

20 EXAMINER JONES: Is Mr. Watson going to testify?

21 MR. BRUCE: Yes.

22 EXAMINER JONES: Okay, I'll save a couple
23 questions for him.

24 Q. (By Examiner Jones) But what about -- Have you
25 already applied for these other units to -- In other words,

1 are you trying to get com agreements on these? Are you
2 waiting for the outcome of this hearing --

3 A. I think Bob is going to address the --

4 Q. Okay, he's going to address that.

5 A. -- the com agreements.

6 Q. I'll save that one.

7 A. Yeah.

8 Q. And --

9 A. If I told you something, it may not be the
10 right --

11 EXAMINER JONES: Okay, yeah, I understand. You
12 were qualified as an engineer.

13 So the applications that have come to Mr. Stogner
14 is just for this one so far?

15 MR. BRUCE: I think the administrative
16 application was for all, but because of the objection it
17 was kicked out.

18 But it was set for hearing for this one. So at
19 this point we're just seeking this one, and then we will
20 decide on the others.

21 EXAMINER JONES: And we can talk to Mr. Watson
22 about the notice issues, I guess.

23 (Off the record)

24 EXAMINER JONES: I don't think we have any more
25 questions for Mr. Maxey.

1 MR. BRUCE: Okay, I do have one.

2 FURTHER EXAMINATION

3 BY MR. BRUCE:

4 Q. Mr. Maxey, if approval is granted, is there a
5 timing issue?

6 A. There is an issue. I talked to our drilling
7 contractor, and you probably heard in these hearings that
8 it's very difficult to get a drilling rig.

9 We have a good relationship with Patterson
10 Drilling. They had contacted me a couple of months ago.
11 We've got a window. I talked with them before coming up
12 here, and we've got 48 days.

13 And they -- Due to timing with filing this
14 administrative application and the hearing and so forth,
15 they have pushed us to the furthest window in that area.
16 If we miss the 48-day window now, they're moving out,
17 they're going over -- I believe into Texas. But they've
18 moved the rig to Carlsbad.

19 They'll come back through this area, drill our
20 well and -- actually drill a couple of wells for another
21 company, then drill our well. And then they were going to
22 move.

23 So I'm just starting to worry about that a little
24 bit.

25 EXAMINER JONES: Okay, thank you.

1 ROBERT H. WATSON,
2 the witness herein, after having been first duly sworn upon
3 his oath, was examined and testified as follows:

4 DIRECT EXAMINATION

5 BY MR. BRUCE:

6 Q. Would you please state your name and city of
7 residence for the record?

8 A. My name is Bob Watson, I'm the land manager -- I
9 live in Roswell, New Mexico -- land manager for Read and
10 Stevens.

11 Q. Have you previously testified before the
12 Division?

13 A. Yes, I have.

14 Q. And were your credentials as an expert petroleum
15 landman accepted as a matter of record?

16 A. Yes, they were.

17 Q. And are you familiar with the land matters
18 involved in this Application?

19 A. Yes, I am.

20 MR. BRUCE: Okay. Mr. Examiner, I'd tender Mr.
21 Watson as an expert petroleum engineer -- I mean petroleum
22 landman.

23 EXAMINER JONES: Mr. Watson is qualified as an
24 expert petroleum landman.

25 MR. BRUCE: And Mr. Examiner, if you could keep

1 Exhibit 2, the land plat, out, it will help go through Mr.
2 Watson's testimony.

3 Q. (By Mr. Bruce) Mr. Watson, what does Exhibit 4
4 reflect?

5 A. Exhibit 4 is a list that I prepared out of the --
6 all offset mineral owners or operating parties that touch
7 the boundary, the north, the northwest, the west, the
8 southwest and to the south of Section 17. There's nothing
9 reflected in here to the east, of course, because that's
10 the State of Texas.

11 Q. Now, this list gives all the offsets, at least on
12 a 40-acre basis, to Section 17?

13 A. Right, for the full section. Anything that
14 touches the boundary of Section 17, this is that list.

15 Q. Okay. And when notice was sent out for the
16 administrative application -- and we'll get into the notice
17 for the hearing -- notice was sent to the people on this
18 list?

19 A. Yes, you'll notice that some of them -- there are
20 no addresses for some of these parties. This information
21 was assembled from a check of the courthouse, official
22 public notice. This is an area that has not been drilled
23 recently. There are a lot of lost owners. There's no
24 track of them, no trace of them. Many of them are probably
25 deceased, and there's no record of heirs in the public

1 record, so -- You'll notice that several of them have no
2 address. But we did try to double-check the list and get
3 current addresses for everyone that we could find, so that
4 we had a good address for notification purposes.

5 Q. Okay. Now, you sent out notices not only for the
6 administrative part but for this Application. Did a number
7 of interest owners waive any objection?

8 A. Yes, this list, approximately 35 to 40 waiver
9 letters were returned with no objection.

10 Q. And are those submitted as Exhibit 5?

11 A. Yes, that is Exhibit 5.

12 Q. Okay. Now in particular, just with respect to
13 this Application and this well unit, you didn't really need
14 to notify all of -- everyone on this list?

15 A. Right, this was -- initially, like I say, when we
16 thought we would make application for all eight units, we
17 felt that would be cost-effective and to get approval at
18 one hearing, so we did the full -- we -- Basically what
19 happened is, we notified many more parties than were
20 necessary.

21 Q. So if you look at Exhibit 2, the parties you did
22 need to notify were the people in lot 3 and the north half,
23 southwest quarter of Section 17 --

24 A. (nods)

25 Q. -- and then the people in lot 1 and the northwest

1 quarter of Section 20, I believe?

2 A. Right.

3 Q. The people -- I suppose -- I believe you also
4 gave notice to the unleased owners in Section -- in all of
5 17, but -- Is that correct?

6 A. Yes, that's correct.

7 Q. Okay. Now, looking at Exhibit 4 again, one of
8 the parties you notified up at the top -- and it doesn't
9 give a tract basis, but it gives the name of Leede
10 Operating, I see that they are outside, really, the
11 affected area by this Application; is that correct?

12 A. Right, they -- Well, actually they have some -- a
13 leasehold in the north half of Section 17, which is not
14 offsetting our proration unit. They're also in the
15 southeast quarter of Section 7, which is not offsetting us,
16 so...

17 Q. Okay. Now, JTD Resources was notified. Do they
18 own an interest in the well unit?

19 A. Yes, they are going to be a 50-percent partner in
20 the well with us.

21 Q. Okay, and what about DOH Oil Company?

22 A. DOH Oil Company is the original lessee of the
23 federal tracts of lots -- which is lots 1, 2, 3 and 4 in
24 Section 17. JTD Resources, who is our partner, has a term
25 assignment with DOH Oil Company, and they have contributed

1 that federal lease to this -- to the prospect, and -- as
2 part of the prospect.

3 Q. And then -- So you notified them, you notified
4 the unleased owners in Section 17. I presume most of the
5 leases in the south half of 17 -- are those Read and
6 Stevens leases --

7 A. Right.

8 Q. -- fee leases?

9 A. In fact, the very south 80 acres of Section 17,
10 you'll notice that there's four 80-acre tracts that are
11 stacked from north to south in Section 17. That comprises
12 roughly the west half of 17. The southernmost 80 is fully
13 leased by Read and Stevens and JTD Resources. So we are
14 offsetting ourselves, essentially.

15 Q. Okay. Now, there have been a couple of
16 objections which you're aware of, Mr. Watson, and I forget
17 the names of the people but one of them was an Avis K.
18 Miller Trust --

19 A. Right.

20 Q. -- and then there was another lady?

21 A. Yes, a Mary Brady.

22 Q. Mary Brady.

23 A. Right.

24 Q. Where are their interests?

25 A. Those interests are located under the east half

1 of Section 18, to the west of 17.

2 Q. Okay. And although -- I believe you've seen a
3 letter where the trustee of the Miller trust objected.
4 Were they entitled to notice of this Application?

5 A. Well, essentially that name did not appear on my
6 takeoff, and I've since discovered in talking with the
7 trust officer there, there was a deed, the Avis Miller --
8 Avis Miller was a resident of Oklahoma, and I believe she
9 died in the Oklahoma City area. Her will was probated in
10 Oklahoma. There was nothing ever filed in Lea County for
11 public notice purposes.

12 But I did send him a notice, thinking that he was
13 the trustee for some other Millers under that same tract.
14 Turned out -- different Millers. I don't know if they're
15 related, but he did get a notice. It was not specifically
16 addressed to Avis K. Miller, however, because she was not
17 listed on my list as being a mineral owner --

18 Q. Okay, so --

19 A. -- and there was no constructive notice in Lea
20 County of that fact either.

21 Q. Okay. So the -- I believe his name was Mike
22 Terman, the trust officer?

23 A. That's correct.

24 Q. But they do not directly offset your proposed
25 well unit?

1 A. No, they do not.

2 Q. Okay. And then Ms. Brady, she does not directly
3 offset this well unit either?

4 A. No, she does not.

5 Q. Okay. And then if you'd turn a few pages into,
6 say, the fifth page of this title report, the people in the
7 northwest quarter of Section -- well, the northern part of
8 Section 20 would be entitled to notice, and notice was
9 given to those people also; is that correct?

10 A. Yes, they were.

11 Q. Okay.

12 A. They were notified.

13 Q. Okay. Now, what does Exhibit 6 represent, Mr.
14 Watson?

15 A. Exhibit 6, okay. Yeah, Exhibit 6 is an affidavit
16 signed by myself that I have made a good-faith effort to
17 locate and notify the -- all the interest owners that would
18 be affected by this hearing, and --

19 Q. And was Exhibit 4 -- the people that were
20 notified were the people listed on Exhibit 4?

21 A. Right, the people on Exhibit 4 is that list of
22 people notified.

23 MR. BRUCE: Mr. Examiner, I ran out of time. I
24 have the green cards in my briefcase. I ask permission to
25 copy them and submit them to the Division.

1 Q. (By Mr. Bruce) Also, Mr. Watson, was a notice
2 prepared and placed for publication in the Hobbs newspaper?

3 A. Yes, it was.

4 Q. And we do not have the affidavit back yet, do we?

5 A. No, it has not been returned.

6 MR. BRUCE: Mr. Examiner, because of that I --
7 even though Mr. Maxey says we need to drill soon, I would
8 ask that the matter be placed on the docket for August 25th
9 so that the affidavit of publication can be submitted at
10 that hearing, to show that the unlocatable people that Mr.
11 Watson discussed have been given publication notice.

12 EXAMINER JONES: Okay.

13 Q. (By Mr. Bruce) And finally, Mr. Watson, what is
14 Exhibit 7?

15 A. Exhibit 7 is a communitization agreement that has
16 been filed with the Bureau of Land Management for our
17 initial proration unit in the southeast quarter of Section
18 17. It's composed of lot 4, which is the federal tract,
19 and the east 26.36 acres of the south half, southwest of
20 17, which is the fee tract.

21 Q. And it was approved by the BLM?

22 A. Yes, it has been approved by the BLM.

23 Q. And this com agreement was signed by Read and
24 Stevens, JTD Resources, and DOH Oil Company?

25 A. Yes.

1 Q. Mr. Watson, is it your opinion that all necessary
2 parties have been notified of this Application?

3 A. Yes, to the best of my knowledge they have.

4 Q. And in your opinion, is the granting of this
5 Application in the interest of conservation and the
6 prevention of waste?

7 A. Yes.

8 Q. And were Exhibits 4 through 7 prepared by you or
9 under your supervision?

10 A. Yes, they were.

11 MR. BRUCE: Mr. Examiner, I'd move the admission
12 of Exhibits 1 through -- I mean, excuse me, 4 through 7.

13 EXAMINER JONES: Exhibits 4 through 7 will be
14 admitted to evidence.

15 EXAMINATION

16 BY EXAMINER JONES:

17 Q. Mr. Watson, on this Exhibit 7 -- Well, I take
18 that back.

19 For notice purposes, you noticed the offset
20 spacing units. Now, the spacing units, is it as you
21 propose them? In other words, you noticed all the way over
22 to the -- to Section 18 for this?

23 A. Yes.

24 Q. Okay.

25 A. We notified all unleased mineral owners in

1 Section 17 that were not already leased by us, and that's
2 where Leede, Leede Exploration, was, had some of those
3 leases.

4 There were a few, I think, on the list that were
5 listed as some -- there's some -- you'll see there's three
6 parties there with no address. Those are -- that ownership
7 goes back 40 or 50 years. Those are the people we could
8 not contact. We had no way -- I mean, there were efforts
9 made to try to track down -- most of those people -- We
10 were never able to find any lead on any of those people or
11 their heirs.

12 Q. Okay. So you basically -- as you propose to
13 develop this Section 17 for the east -- the east four
14 proposed spacing units, you have to do com agreements --

15 A. Right.

16 Q. -- but not for the west four --

17 A. Right.

18 Q. -- because they're common --

19 A. Right?

20 Q. -- fee owners?

21 A. Yeah those are undivi- -- those -- the interests
22 as to the fee tracts in 17 are undivided as to the -- as to
23 each 80-acre tract. There's a different -- there's a
24 separate ownership, or different ownership, for each 80-
25 acre tract, but they're all undivided or common for the

1 full 80 acres.

2 So yes, if you move north one location, if you --
3 I mean if your drilling plan turned out to go north, you
4 would have -- you'd essentially have four com agreements
5 along the east edge of Section 17 in the same fashion that
6 we've done in the southeast quarter.

7 Q. Okay. And if you find your reservoir is pretty
8 good here, you can -- because of the state spacing rules
9 for 40-acre spacing, you can drill four wells if you have
10 to, if you need to?

11 A. Right, yes.

12 Q. In each one of those proposed spacing units?

13 A. The way we'd have it divided -- or initially the
14 way we had it divided, it comes out to about 53 acres per
15 unit. But yeah, the west part of that, yeah, that would be
16 -- if this was approved, you would have -- you could drill
17 eight wells in Section 17 on 53-acre spacing, essentially,
18 if that was approved.

19 Q. And if they turn out to be good wells, you would
20 double the spacing, and that would be 27 acres per well
21 instead of 20 acres per well?

22 A. Yeah, I guess if the reservoir justified it,
23 yeah, you could -- yeah, and drill double -- double the
24 amount of wells, right.

25 Q. Okay. Mr. Maxey talked about some of the

1 implications of the drilling over in Texas. Are you
2 familiar with that, what he's talking about?

3 A. Generally, I'm probably, but not in any great
4 detail. We do have some operations in Texas and, you know,
5 I do work with those from time to time, but I don't know
6 that I specifically could ask -- could answer a lot of, you
7 know, detailed questions about their spacing or their
8 Railroad Commission regulations. I mean, I just have a
9 general knowledge of that and I get into it when I need to.
10 But as to this area, I don't have any specific -- don't
11 have a lot of specific information.

12 Q. Does it relate to equidistance between wells?

13 A. Yeah, I'm sure -- Yes, it has to do with the
14 requirement for distance between wellbores, you know,
15 footage requirements, that sort of thing. That's basically
16 all I know about -- you know, at this point.

17 EXAMINER JONES: Okay. Gail, do you have any
18 other questions?

19 EXAMINATION

20 BY MS. MacQUESTEN:

21 Q. I'm afraid I have to show my confusion. Could
22 you help me understand Exhibits 1 and 2?

23 A. 1 and 2, let's see.

24 Q. This is Exhibit 1.

25 A. Right.

1 Q. Is this showing Section 17 only?

2 A. I believe that's essentially all of 17. I don't
3 have that one in front of me, I'm sorry. May I look at
4 your copy?

5 Q. Let's stand here.

6 A. Yes, the hached lines -- or the solid lines is
7 what we were initially going to apply for. This is eight
8 of the 53 acres that the -- the dotted lines show -- This
9 is lots 1, 2, 3 and 4. This is your federal tract here,
10 from north to south. These are your four 80s that -- on
11 your fee ownership that essentially -- yeah, this is
12 essentially all of Section 17, right in the middle.

13 Q. Does this map correspond to this area --

14 A. Right.

15 Q. -- Exhibit 2?

16 A. Right, this is this, right here. And then here
17 is 18. Here's your east half of 18. This is where we had
18 -- the objection letter came from, this area right here --

19 Q. Okay.

20 A. -- whereas our location is right here in the
21 southeast corner on this federal lot number 4, is where
22 we're located.

23 Q. So the unit we're talking about today in this
24 Application would be this unit --

25 A. Right --

1 Q. -- in the --

2 A. -- that's 53 acres, yes. This is 27 acres
3 federal --

4 Q. -- southeast corner?

5 A. Right, 27 acres federal. If you come over here,
6 26 acres fee. That gives you the 53 acres, so that's what
7 we're applying for.

8 Q. And who did you notify for the hearing today?

9 A. For the hearing we notified people here, here,
10 here, here and here, because initially we were going to
11 make -- we were going to apply for the approval of all. So
12 everywhere -- Here's your boundary here, so anywhere we
13 touched, we -- there was about -- turned out to be about 80
14 people that we notified.

15 Q. So you did notify some --

16 A. Right, we --

17 Q. -- interest owners in 18 --

18 A. Right.

19 Q. -- but only those that touched directly some part
20 of 17?

21 A. Actually, your ownership in the east half of 18
22 is also common. This is all fee, private ownership. These
23 people own undivided interest under the entire east half.
24 So yeah, we just took everybody that was unleased in 18 --
25 in fact, we do own some leases in 18 that we have leased.

1 But yes, we contacted -- anybody that was contacted here
2 owns in the entire east half, so, you know...

3 Q. Where did the objections come from?

4 A. East half of 18. One lady had 3.3 acres, and
5 there's some question as to -- that's what -- we credited
6 her with a little over three acres.

7 The other ownership we're not sure, because
8 there's some title questions on the -- This is the Avis
9 Miller trust. She does not show up in the ownership,
10 because there was nothing filed of record in Lea County
11 showing her that she had the ownership. So there's --
12 questionable as to what she owns. So -- but those were the
13 -- That's where the objections came from, were the east
14 half of 18.

15 Q. So the individual who protested, Mary Brady --

16 A. Uh-huh.

17 Q. Was she notified?

18 A. Yes, she was notified. She received our initial
19 notification. She called and had questions. I talked to
20 her initially and tried to answer all of her questions.
21 She deals in minerals. I think she's an heir of -- Like I
22 said, her father was an operator in the area, so apparently
23 they have quite a few royalty and mineral interests to
24 track.

25 So I tried to answer all of her questions at that

1 point. And a few weeks -- a week or so, 10 days later, she
2 wrote the letter to the OCD. We have a copy of that. And
3 I called her back and I said, you know, Can I -- apparently
4 I didn't explain well enough and I said, Can I try to
5 answer some more of your questions? So we talked at length
6 there.

7 And at that point she also talked to Mr. Maxey
8 about -- She initially had some drainage concerns, which I
9 -- in my opinion, I said, I don't think there's going to be
10 any drainage concerns here.

11 So then at that point she wanted to talk to Mr.
12 Maxey, and he talked to her about that. And so we thought
13 we had her satisfied and -- but I don't know what basis she
14 would be objecting. We didn't understand why she was
15 continuing to object.

16 But at that point it got into a different area.
17 She -- I offered to just buy a lease from her. I said, Can
18 we just lease your interest? I made her an offer to lease,
19 and she turned down the offer.

20 And I said, Well, I don't want to go beyond that
21 at this point. I said, you know, Our -- the leasing -- the
22 lease matter is a different issue from the hearing
23 altogether.

24 So I eventually withdrew my offer to lease
25 because -- and I did get the idea that she really didn't

1 have a problem with the hearing, but she wanted us to buy a
2 lease from her on her terms, and I said, No, I don't -- we
3 don't want to do that at this point. We don't -- you know,
4 Section 18 is not an area we want to buy any more leases
5 under at this point, and -- especially since I had made her
6 an offer and she had turned it down, so...

7 But that's the way that developed. But she's not
8 an offset mineral owner to our revised Application at this
9 point, so --

10 Q. She would be considered an offset operator had
11 you gone with the original proposal for that --

12 A. Yeah, had we stayed with the original, yes, she
13 would have been an offset.

14 But we've scaled that back to just this southeast
15 corner, so...

16 Q. How about the Avis K. Miller Trust? What lands
17 do they --

18 A. East half of 18 also. And like I say, this was
19 -- we didn't know about her interest until Mr. Terman, who
20 was the trust officer, faxed a copy of a deed that -- and
21 this particular deed was not filed in Lea County, and we
22 had no record of it or no knowledge of it until that point.

23 When we first initially sent out this lease,
24 these notifications, she was not on our list, she didn't
25 appear in our records anywhere. And his objection was that

1 we did not officially notify the Trust, when in fact we did
2 send a notification to him, thinking he was trust officer
3 for the -- this would be for the David Cullum Miller and
4 Russell Bryan Miller parties that are on the list. We sent
5 those to him, thinking he was trust officer for those two
6 interests.

7 And I've since learned that the David Miller
8 interest was sold to the Round Hill Royalty group, which is
9 immediately above them on the list, and the Russell Miller
10 interest is no longer administered by the bank. And so
11 that's when he sent the copy of the deed for the Avis
12 Miller Trust.

13 And like I say, I didn't have any knowledge of
14 that until that point.

15 And like I say, we considered it -- didn't
16 consider it to be an issue at this point now that we have
17 -- we're just going for the one location approval, so...

18 Q. Now, if the unit you're asking for today is
19 approved, won't that affect how the west half of 17 is
20 developed, once you've carved out that one unit?

21 A. Yes, it would. It would, but we would -- you
22 know, we would address those as -- not knowing which way --
23 you know, not knowing the outcome of our initial well and
24 whether we would be moving to the north, to the west or
25 possibly to the south, you know, that's an unknown at this

1 point.

2 But yes, it could -- it could have an effect on
3 -- that would set a precedent for Section 17, if we were to
4 get approval for that.

5 But at that point we would do -- I don't know if
6 we would do another notification. We probably -- We'd have
7 to do another round of notifications in Section 18 and
8 address these -- you know, and address these concerns at
9 that point.

10 Q. If we grant the unit that you're asking for
11 today, does that mean that we would ultimately have to
12 grant the eight units in your original proposal, or could
13 there be a different configuration?

14 A. I'm not sure I can answer that.

15 I would think that that would set the pattern,
16 that would be a logical pattern to follow through Section
17 17 for each well drilled. I mean, I don't know why you
18 would -- yeah, you wouldn't want to alter that from that, I
19 don't think.

20 MS. MacQUESTEN: Okay, I don't have any other
21 questions. Thanks.

22 EXAMINER JONES: I don't have any more for Mr.
23 Watson.

24 I'd like to call Mr. Maxey one more time for a
25 couple of questions.

1 JOHN C. MAXEY, JR. (Recalled),
2 the witness herein, having been previously duly sworn upon
3 his oath, was examined and testified as follows:

4 EXAMINATION

5 BY EXAMINER JONES:

6 Q. Okay, since this is a precedent-setting for this
7 section, I was going to ask you, when you evaluate a
8 drilling location you look at several risk factors,
9 correct?

10 A. Yeah, new -- like a new develop- -- I mean --

11 Q. I mean -- okay, for instance, is there a -- What
12 risk factors are the biggest here?

13 A. Okay, I misunderstood your earlier question about
14 the stratigraphic trap, so I want to make sure I understood
15 your question.

16 I think our biggest risks here, we -- Our
17 subsurface information is a ways up to the north. We do
18 have that well I spoke of earlier about a mile and a half
19 away, that was a dry hole, that helps.

20 I think our biggest risk here is, it's a
21 stratigraphic trap, really knowing how that develops, and
22 that updip pinchout. We don't want to get too close to our
23 best estimate -- more like a guess, this far away from the
24 information. We don't want to get too close to that updip
25 side and the pinchout, but we don't want to get too far

1 down, because up to the north in the Foster field there is
2 more water production out of the downdip well.

3 So that's the two biggest risks, other than just
4 drilling a dry hole. I mean, just flat out the porosity is
5 not there. That's the two biggest risks.

6 We are making an assumption that these traps are
7 running on the flank of this structure. We do have a nose,
8 or it appears that the seismic is helping on that. And
9 really, to try to answer your question, I think our two
10 biggest risks would be the updip pinchout and the downdip
11 water leg.

12 Q. Okay. So if you do hit a strat trap here and you
13 hit a reservoir, are you worried about it being low
14 porosity or low permeability? Is that a problem?

15 A. Well, that's -- you know, in the San Andres
16 that's always an issue. I mean, it's not like a Devonian
17 well. If you hit porosity in a Devonian well, usually
18 you've got a great well.

19 In the San Andres, it's all over the board. I
20 mean, you can hit great porosity, you can hit intermediate,
21 you can hit some tight stuff and have stinky wells.

22 Q. Okay.

23 A. So yes, there's a reservoir factor, reservoir
24 rock quality factor. That really didn't play in -- We're
25 trying to hit a trend. If this -- If we're correct, we

1 have an updip pinchout that runs north-south -- based on
2 what we've seen in the north, we believe it runs north-
3 south -- and we have a downdip water leg that's going to be
4 north-south. So we have something between those two
5 constraints that trends north and south.

6 Q. Uh-huh.

7 A. And yes, we could drill something that's very
8 tight, intermediate porosity that's marginal, just -- yeah,
9 there is that risk, more so than a -- like a Devonian.

10 Q. Okay, if it is tight and you do have oil and some
11 porosity, but it's just low permeability, you'll need more
12 wells if you can justify them, right?

13 A. If we can justify them. At that point we'll try
14 to figure out -- Based on the data we get from the hole,
15 the logs, the thickness of the zone, the porosity and
16 permeability, we'll try to get probably six months', at
17 least, production, if it's something like you've described,
18 and try to figure out what kind of a drainage area -- what
19 area will drain.

20 And that will help us in making a decision on it,
21 should we drill an infill in this proration unit, should we
22 step out to the next proration unit? That type of
23 decision.

24 Q. Okay. Can you imagine how you would be -- Let's
25 say you proceed and you hit a well here and you go ahead

1 and drill another proration unit over on the -- directly to
2 the west. Can you foresee any effect on the mineral owners
3 in Section 18?

4 A. No. Really, if you look at this, the difference
5 -- When I talked to Mary Brady, her first concerns, the
6 reason she had objected and had not contacted me prior to
7 ask me any questions, she told me that she's primarily
8 familiar with Texas. She had been pooled across a lease
9 line in Texas.

10 I'm not as familiar with Texas, but it is
11 different, because you can form -- it's pretty much common
12 occurrence to form different-size proration units in a
13 section, and there's a common setback and distance between
14 wells, like Mr. Watson said.

15 And she was concerned that we were going to maybe
16 drain her lease. And several times I said, This is not an
17 unorthodox location. Are you -- You know, I tried to
18 alleviate her concerns about drainage. And she was
19 wondering, Well, can you drain my minerals from over a half
20 a mile away? Because I said, This is over a half a mile
21 away from your lease line. And so she was very concerned
22 with drainage.

23 And I thought -- I spent 45 minutes explaining
24 how we drill wells, how they're constructed, and I tried in
25 layman's terms, as best I could, to explain the reservoir

1 and the dynamics of production. And I thought -- When we
2 were done, she was amenable to withdrawing her objection,
3 but then she never did. I saw no problem.

4 As a matter of fact, if you just looked at
5 drilling one well on each proration unit, if you left it
6 the way it is, where -- the way it's divided now, it would
7 be more of a factor on draining her minerals, because we
8 could drill two wells in the 40-acre proration units, the
9 second being on an administrative order, and we could have
10 16 -- we could have 18 wells -- or excuse me, 16 wells in
11 the west half, under what's there now.

12 My problem is on the east side with that strip.
13 If we were to adopt what we're proposing, you would have
14 eight wells in the west side.

15 Q. So you're mainly concerned that the reservoir is
16 not very good here, and that's why you want these bigger
17 proration units?

18 A. Yes, because it -- I get constrained on the east
19 side of that federal strip if we try to leave everything
20 the way it is and just use the federal strip to divide up
21 in a proration unit, some sort to make this think work --

22 Q. You're afraid that those wells that you would
23 drill on nonstandard -- little, 27-acre nonstandard
24 proration units and nonstandard locations, would be not
25 economical?

1 A. Well, to go back to one of your questions about
2 risk, I'm automatically making a higher hurdle in trying to
3 drill an economic well on those small proration units. I
4 mean, I've got to have a good well right off the bat on one
5 of those narrow proration units to make this thing work,
6 because I'm going to drain each side of it. I mean, I'll
7 eventually step out on either side of that and drain it.

8 What may be a -- so that -- Trying to answer your
9 question. If you develop the field and you have one well
10 on the Texas side, one well on the -- one well to the west
11 of that initial strip, when you put one in the middle you
12 have a very small drainage radius. And what I'm saying is,
13 it's more efficient to divide this section up like this,
14 because we have been truncated in the east side, it's going
15 to be more efficient to drain reserves from the San Andres,
16 because on statewide we'd go 40 acres down to 20, if we
17 thought -- deemed necessary. All we're doing here is
18 proposing to go 54 acres down to 27 acres.

19 There's -- When you look at the drainage radius
20 of 27 acres versus 50-some-odd acres, compared to what
21 statewide is, it's only about a 16-percent increase in your
22 drainage radius that -- changing this proration unit. It
23 ratchets up.

24 Q. Okay, I understand, okay. That answers my
25 question.

1 A. I hope I --

2 Q. Yeah.

3 A. I'm a little too familiar with it, I forget to
4 explain things.

5 EXAMINER JONES: Okay, thank you very much.

6 That's all the questions we have.

7 MR. BRUCE: I have nothing further, Mr. Examiner.

8 EXAMINER JONES: Okay. With that, we will
9 continue this case until the August 25th hearing.

10 (Thereupon, these proceedings were concluded at
11 11:25 a.m.)

12 * * *

13
14
15
16
17 I do hereby certify that the foregoing is
18 a complete record of the proceedings in
the Examiner hearing of Case No. _____
heard by me on _____

19 _____, Examiner
20 Oil Conservation Division
21
22
23
24
25

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 August 13th, 2005.



STEVEN T. BRENNER
CCR No. 7

My commission expires: October 16th, 2006