

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

**APPLICATION OF COG OPERATING LLC
FOR A NON-STANDARD SPACING AND
PRORATION UNIT AND COMPULSORY POOLING,
LEA COUNTY, NEW MEXICO**

**CASE NO. 15327 (De Novo)
ORDER NO. R-14023-A**

ORDER OF THE COMMISSION

THIS MATTER came before the Oil Conservation Commission ("Commission") on the application of COG Operating LLC ("COG" or "Applicant") to approve the compulsory pooling of a limited vertical portion of a pool in a proposed non-standard spacing and proration unit. The Commission, having conducted a public hearing on November 5, 2015, and having considered the testimony, the record, and the arguments of the parties, and being otherwise fully advised, enters into the following findings, conclusions and order.

THE COMMISSION FINDS THAT:

1. Notice has been given of the application and the hearing of this matter, and the Commission has jurisdiction of the parties and of the subject matter herein.

2. COG submitted an application for approval of a 200 acre non-standard oil spacing and proration unit and project area (the "Unit") for oil production from the Yeso formation [Maljamar; Yeso, West Pool (Pool code 44500)] comprising the S/2 N/2 of Section 9 and the SW/4 NW/4 of Section 10, Township 17 South, Range 32 East NMPM, Lea County, New Mexico. Applicant further seeks an order pooling all mineral interests in the Yeso formation underlying this Unit from a vertical depth of approximately 5000 feet to the base of the Blinebry member.

3. The Unit will be dedicated to COG's Sneed 9 Federal Com. Well No. 23H (the "proposed well"; API No. 30-025-41410), a horizontal well to be drilled from a surface location 1650 feet from the North line and 330 feet from the West line (Unit E) of Section 9 to a bottom-hole location 1650 feet from the North line and 990 feet from the West line (Unit E) of Section 10, Township 17 South, Range 32 East NMPM, Lea County, New Mexico. The completed interval of this well will be at a standard location within the Unit.

4. The proposed oil well is within the Maljamar; Yeso, West Pool and is therefore subject to Division Order No. R-13382, as amended. Wells in this pool are also subject to Rule 19.15.15.9(A) NMAC, which provides for 330-foot setbacks from the unit boundaries and standard 40-acre units each comprising a governmental quarter-quarter

**BEFORE THE OIL CONSERVATION
DIVISION
Santa Fe, New Mexico
Exhibit No. 2
Submitted by: COG OPERATING LLC.
Hearing Date: March 29, 2016**

section. The proposed Unit and project area consists of five (5) adjacent quarter-quarter sections oriented west to east. In Order No. R-13382-E, the Division found:

- a. The Yeso formation is stratigraphic, lenticular and highly compartmentalized with very low porosity and low permeability and a high degree of heterogeneity. Finding (72).
- b. Drilling on the equivalent of 10-acre spacing was necessary in the Yeso formation to prevent waste and protect correlative rights. Finding (83).

5. COG seeks approval through hearing of the same Unit to be dedicated to the proposed well before Division as Case No. 15327. Division issued Order No. R-14023 dated July 22, 2015. In this Order, Division denied the application due to a lack of authority, under the Rules, which would allow the Division to compulsory pool a fraction of a pool even if the approved project area or unit contains depth severance clauses.

6. In support of the Application, COG filed a Pre-hearing Memorandum. The Pre-hearing Memorandum stated:

- a. Every interest owner in the proposed Unit supports COG's proposal to limit the pooled intervals to the Paddock and Blinebry members of the Yeso formation, including the interest owner below the base of the Blinebry interval to be excluded by COG's application;
- b. Geologic evidence from the development of the Yeso formation in the subject area demonstrates that the deeper Tubb and Drinkard intervals below the Blinebry are rarely productive and the Tubb specifically contains tight sandstone, is wet and does not contain recoverable hydrocarbons;
- c. COG proposed a horizontal well over 400 feet above the base of the Blinebry and sought an order from the Division pooling only those interest owners above the Blinebry;
- d. The Division denied the application stating "There is no rule that allows the Division to compulsory pool a fraction of a pool even if the approved project area contains depth severance clauses;"
- e. COG's application is consistent with the Commission's statutory pooling authority and definition of a proration unit as the application seeks to pool the uncommitted interests in an area in a pool that will potentially contribute hydrocarbons to the proposed well and exclude the interest owner in the lower interval that will not contribute hydrocarbons to the proposed well;
- f. Granting of COG's application is necessary to protect correlative rights and prevent waste by including only the interests in the productive intervals;
- g. The Commission has the statutory authority to "do whatever may be reasonably necessary to carry out the purposes of [the Oil and Gas Act], whether or not indicated or specified in any section of the act;"
- h. Excluding from pooling the interest owners in the non-productive intervals is consistent with Commission precedent in Order No. R-13228-F.

7. COG presented direct testimony from two expert witnesses: Sean Johnson, landman for COG's New Mexico Shelf Asset Team, and Harvin Broughton, lead geologist for COG's New Mexico Shelf Team.

8. The Oil Conservation Division ("Division") filed an entry of appearance as an intervener and appeared at hearing through its attorney, but presented no testimony. No one else entered an appearance or otherwise opposed this Application

9. Mr. Johnson testified that COG is seeking to compulsory pool only the upper portion of the Yeso formation due to vertical depth severance ownership in two of the three tracts that comprise the Unit. Mr. Johnson identified one party, Este, Ltd, with mineral interest ownership in the tracts who were approached by COG regarding the vertical depth severance of the Yeso formation. Mr. Johnson presented a correspondence by Este, Ltd stating their support of the Unit as proposed by COG and compulsory pooling only the upper portion of the Maljamar; Yeso, West Pool.

10. Ownership in the S/2 NW/4 of Section 9 and the SW/4 NW/4 of Section 10 is severed at the base of the Blinebry interval as the result of assignments issued by Este Ltd. (See Johnson Testimony; Exhibit 4). This entity only owns below the base of the Blinebry interval while the remaining working interest owners in the subject acreage own throughout the entire Yeso formation.

11. Mr. Johnson testified that notice was provided to lessees or operators of surrounding tracts as affected parties of the proposed non-standard spacing unit. Notice was also provided to all interest owners subject to pooling proceedings as affected parties of the proposed compulsory pooling within the Unit.

12. Mr. Johnson testified that the COG seeks charges for supervision (combined fixed rates) of \$7000 per month while drilling and \$700 per month while producing.

13. Mr. Broughton testified, that in the northwest area of the shelf extending from the Delaware Basin, the Yeso formation is approximately 1500 feet thick and contains four distinct members (from shallowest to deepest): the Paddock member, the Blinebry member (the target interval for the proposed well), the Tubb member and the Drinkard member.

14. Mr. Broughton testified that the Blinebry member in this area is suitable for development by horizontal drilling with no indications of faults, pinch-outs or other geological impediments to interfere with a horizontal completion. The proposed orientation of the horizontal well west to east has resulted in good production for other wells in this area and is appropriate for this Unit.

15. Mr. Broughton further stated that all quarter-quarter sections to be included in the Unit are expected to be productive in the Blinebry member, so that the Unit, as requested, will not impair correlative rights.

16. Mr. Broughton testified that the lower portion of the Yeso formation, the Tubb and Drinkard members, have poor reservoir characteristics making these members extremely unfavorable for hydrocarbon potential.

THE COMMISSION CONCLUDES THAT:

1. The Commission has jurisdiction over the parties and the subject matter of this case.
2. Proper public notice has been given.
3. Although there is no rule that specifically allows the Division to compulsory pool a fraction of a pool, the Oil and Gas Act and Rules provide the Commission with the following relevant authority:
 - a. The Oil and Gas Act authorizes the Commission to compulsory pool oil and gas interests in "all *or any part of* such lands or interests or both in *the spacing or proration unit* as a unit." NMSA 1978, §70-2-17.C (emphasis added).
 - b. Division rules define a proration unit as "the area in a pool that can be effectively and efficiently drained by one well..." 19.15.2.7.P(17) NMAC.
 - c. The Commission's primary statutory duty is to prevent waste and protect correlative rights. *See* NMSA 1978, § 70-2-11(A). The Oil and Gas Act empowers the Commission to "make and enforce rules, regulations and orders, and *do whatever may be reasonably necessary* to carry out the purposes of this act, *whether or not indicated or specified in any section of the act.*" NMSA 1978, § 70-2-11(A) (emphasis added). *See also Santa Fe Exploration v. Oil Conservation Comm'n*, 114 N.M. 103, 835 P.2d 819 (1992).
4. COG's application is consistent with the Commission's statutory pooling authority and definition of a proration unit as the application seeks to pool the uncommitted interests in an area in a pool that will potentially contribute hydrocarbons to the proposed well and exclude the interest owner in lower interval that will not contribute hydrocarbons to the proposed well
5. Applicant has shown that:
 - a. The Tubb interval below the base of the Blinbry contains tight sandstone that is wet and does not contain recoverable hydrocarbons. *See* Broughton Testimony; Exhibit 19.
 - b. The deepest Drinkard interval has not been the target of development in the subject area and it is unlikely to be productive of recoverable hydrocarbons. *See* Broughton Testimony; Exhibits 15 and 17.

- c. COG's proposal to pool only the Paddock and Blinebry intervals of the Yeso formation where ownership is common is necessary to prevent owners below the base of the Blinebry who will not contribute oil or gas to the proposed wellbore from receiving a share of production. *See Broughton Testimony; Exhibit 18A.*

6. The Commission finds that pooling only the Paddock and Blinebry intervals of the Maljamar; Yeso West Pool (Code 44500) underlying the proposed non-standard spacing unit and project area is just and reasonable, and is necessary to protect correlative rights and prevent waste for the following reasons:

- a. There is a depth severance underlying the subject acreage that causes ownership above the base of the Blinebry to differ from the ownership below the base of the Blinebry. *See Johnson Testimony; Exhibit 4.*
- b. COG presented evidence that the Tubb interval below the base of the Blinebry does not contain recoverable hydrocarbons. *See Broughton Testimony; Exhibit 19.*
- c. Requiring COG to pool the entire vertical extent of the Maljamar; Yeso West Pool will result in an owner below the base of the Blinebry (Este Ltd.) receiving a share of the production from the wellbore even though the intervals below the base of the Blinebry will not contribute oil or gas to the proposed wellbore. *See Broughton Testimony; Exhibit 18A.*
- d. Este, Ltd., the only party that does not own throughout the entire Maljamar; Yeso West Pool underlying the proposed non-standard spacing unit, received notice of this pooling application and believes this application is necessary to protect correlative rights. *See Exhibits 4 and 5.*
- e. Approval of the proposed non-standard spacing and proration unit in the Paddock and Blinebry intervals of the Yeso formation will enable Applicant to drill a horizontal well that will efficiently produce the reserves underlying the Unit and protect correlative rights.

7. In order to protect correlative rights and prevent waste, Applicant's proposal to create the non-standard unit and pool a vertical portion of the Yeso formation should be approved based on the facts of this specific case.

8. A non-standard oil spacing and proration unit should be approved within the Yeso formation from the top (upper contact) of the Paddock member to the base (lower contact) of the Blinebry member covering the 200 acres of the proposed Unit.

9. All uncommitted interests in the oil and gas within the Unit should be pooled.

10. Two or more separately owned tracts are embraced within the Unit, and/or there are royalty interests and/or undivided interests in oil and gas minerals in one or more tracts included in the Unit that are separately owned.

11. Applicant is owner of an oil and gas working interest within the Unit. Applicant has the right to drill and proposes to drill the proposed well to a common source of supply within the Unit at the proposed location.

12. There are interest owners in the Unit that have not agreed to pool their interests.

13. To avoid the drilling of unnecessary wells, protect correlative rights, prevent waste and afford to the owner of each interest in the Unit the opportunity to recover or receive without unnecessary expense a just and fair share of hydrocarbons, this application should be approved by pooling all uncommitted interests, whatever they may be, in the oil and gas within the Unit.

14. COG should be designated the operator of the proposed well and the Unit.

15. 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% thereof as a reasonable charge for the risk involved in drilling the proposed well.

16. Reasonable charges for supervision (combined fixed rates) should be fixed at \$7000 per month while drilling and \$700 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."

17. Commission finds that this case has not demonstrated, through evidence and testimony, sufficient cause to institute a precedent for future applications with similar circumstances. Therefore, all similar applications for compulsory pooling that seek vertical segregation of an established pool will be required to come before the Division or Commission on case-by-case basis.

IT IS THEREFORE ORDERED THAT:

1. Pursuant to the application of COG Operating LLC, a 200 acre non-standard oil spacing and proration unit (the "Unit") is hereby established for oil production from the Yeso formation [Maljamar; Yeso, West Pool (Pool code 44500)] comprising the S/2 N/2 of Section 9 and the SW/4 NW/4 of Section 10, both located in Township 17 South, Range 32 East, NMPM, Lea County, New Mexico.

2. The Unit is further defined as being limited to depths from the top of Paddock member to the base of the Blinebry member of the Yeso formation using the stratigraphic equivalent of the top of the Paddock member at a measured depth of 5517 feet and the base of the Blinebry member at a measured depth of 6852 feet as encountered in the log run of the Branex COG Federal Well No. 10 (API No. 30-025-40871) located 1650 feet from the South line and 330 feet from the West line (Unit L), Section 9, Township 17 South, Range 32 East, NMPM and entered as COG Exhibit No. 3

3. All uncommitted interests, whatever they may be, in the oil and gas in the Unit, are hereby pooled.

4. The Unit shall be dedicated to Applicant's Sneed 9 Federal Com. Well No. 23H (the "proposed well"; API No. 30-025-41410), a horizontal well to be drilled from a surface location 1650 feet from the North line and 330 feet from the West line (Unit E) of Section 9 to a bottom-hole location 1650 feet from the North line and 990 feet from the West line (Unit E) of Section 10, Township 17 South, Range 32 East NMPM, Lea County, New Mexico. The well's completed location will be orthodox within the Unit.

5. The operator of the Unit shall commence drilling the proposed well on or before December 31, 2016, and shall thereafter continue drilling the proposed well with due diligence to test the Paddock member of the Yeso formation.

6. In the event the operator does not commence drilling the proposed well on or before December 31, 2016, Ordering Paragraphs (1) and (3) shall be of no effect, unless the operator obtains a time extension from the Division Director for good cause demonstrated by satisfactory evidence.

7. Should the proposed well not be drilled and completed within 120 days after commencement thereof, then Ordering Paragraphs (1) and (3) shall be of no further effect, and the Unit and project area created by this order shall terminate, unless operator appears before the Division Director and obtains an extension of the time for completion of the proposed well for good cause shown by satisfactory evidence. If the proposed well is not completed in all of the standard spacing units included in the proposed project area (or Unit) then the operator shall apply to the Commission for an amendment to this Order to contract the Unit so that it includes only those standard spacing units in which the well is completed.

8. Upon final plugging and abandonment of the proposed well and any other well drilled on the Unit pursuant to Division rule 19.15.13.9 NMAC, the pooled Unit created by this Order shall terminate, unless this Order has been amended to authorize further operations.

9. COG Operating LLC (OGRID 229137) is hereby designated the operator of the well and the Unit.

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

11. 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."

12. The operator shall furnish the Commission and each known pooled working interest owner (including non-consenting working interest owners) 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 Commission, and the Commission 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 Commission will determine reasonable well costs after public notice and hearing.

13. Within 60 days following determination of reasonable well costs, any pooled working interest owner who has paid its share of estimated 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 the estimated well costs it has paid exceed its share of reasonable well costs.

14. The operator is hereby authorized to withhold the following costs and charges from production from each well:

- 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% of the above costs.

15. The operator shall distribute the costs and charges withheld from production, proportionately, to the parties who advanced the well costs.

16. Reasonable charges for supervision (combined fixed rates) for the well are hereby fixed at \$7000 per month while drilling and \$700 per month while producing, provided that these rates shall be adjusted annually pursuant to Section III.1.A.3 of the COPAS form titled "*Accounting Procedure-Joint Operations*." The operator is 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 pooled working interest owners.

17. Except as provided in Paragraphs (14) and (16) above, all proceeds from production from the proposed well that are not disbursed for any reason shall be held for the account of the person or persons entitled thereto pursuant to the Oil and Gas Proceeds Payment Act (NMSA 1978 Sections 70-10-1 through 70-10-6, as amended). If not disbursed, such proceeds shall be turned over to the appropriate authority as and when required by the Uniform Unclaimed Property Act (NMSA 1978 Sections 7-8A-1 through 7-8A-31, as amended).

18. Any unleased mineral interests 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.

19. Should all the parties to this compulsory pooling order reach voluntary agreement subsequent to entry of this Order, this Order shall thereafter be of no further effect.

20. The operator of the well and the Unit shall notify the Commission in writing of the subsequent voluntary agreement of all parties subject to the compulsory pooling provisions of this Order.

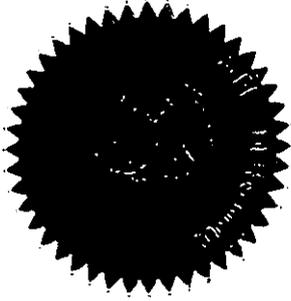
21. The operator shall provide to the Division, within a year of commencing production from the proposed well, evidence that the final fracture configuration of the completion has remained within vertical limits of the Unit as described in Ordering Paragraph 2. If the operator is unable to provide sufficient information for Division to determine the limits of fracturing, then the operator shall appear before Commission to restate the justification for the vertical segregation of the Yeso formation as delineated in the Maljamar; Yeso, West Pool.

22. The Commission recognizes that the formation of this Unit is uniquely based on the specific facts of the case and directs the Applicant to pursue other agreement options, such as a Joint Operating Agreement, to negotiate participation of mineral interest owners in order to avoid unnecessary subdivisions of existing pools.

23. Jurisdiction of this case is retained for the entry of such further orders as the Commission may deem necessary.

DONE at Santa Fe, New Mexico, on this 10th day of December, 2015.

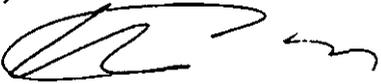
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