

**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. 15602

**APPLICATION OF MEWBOURNE OIL COMPANY FOR A NON-STANDARD
OIL SPACING AND PRORATION UNIT AND COMPULSORY POOLING, LEA
COUNTY, NEW MEXICO.**

CASE NO. 15628

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

ORDER NO. R-14526

ORDER OF THE DIVISION

BY THE DIVISION:

This case came on for hearing at 8:15 a.m. on March 30, 2017, at Santa Fe, New Mexico, before Examiner Phillip R. Goetze and on April 27, 2017, before Examiner William V. Jones.

NOW, on this 26th day of December, 2017, the Division Director, having considered the testimony, the record and the recommendations of Examiner Goetze,

FINDS THAT:

(1) Due public notice has been given, and the Division has jurisdiction of this case and of the subject matter.

(2) Cases No. 15600, 15601, 15602, 15628, 15629, and 15630 were consolidated at the hearing for the purpose of testimony; however, one order will be issued for Cases No. 15602 and 15628.

(3) In Case No. 15602, Mewbourne Oil Company (the "Applicant" or "Mewbourne") seeks approval of a non-standard 160-acre, more or less, oil spacing and proration unit and project area (the "Applicant's Unit") in the Bone Spring formation (Antelope Ridge; Bone Spring, West Pool (Pool code 2209)) consisting of the E/2 W/2 of Section 15, Township 23 South, Range 34 East, NMPM, in Lea County, New Mexico. Applicant further seeks an order pooling all uncommitted interests in the Unit for the Bone Spring formation.

(4) The Applicant's Unit would be dedicated to the Pronghorn 15 B3CN Federal Com Well No. 1H (API No. 30-025-44011), a horizontal well to be drilled from a surface location 185 feet from the North line and 1700 feet from the West line (Unit C) of Section 15, to a terminus 330 feet from the South line and 1800 feet from the West line (Unit N) of Section 15, both in Township 23 South, Range 34 East, NMPM. The completed interval of the proposed well will be orthodox.

(5) In Case No. 15628, Black Mountain Operating, LLC (the "Intervenor" or "Black Mountain") seeks approval of a non-standard 240-acre, more or less, oil spacing and proration unit and project area (the "Intervenor's Unit") in the Bone Spring formation (Antelope Ridge; Bone Spring, West Pool (Pool code 2209)) consisting of the E/2 W/2 of Section 15, and the E/2 SW/4 of Section 10, both in Township 23 South, Range 34 East, NMPM, in Lea County, New Mexico. Intervenor further seeks an order pooling all uncommitted interests in the Unit for the Bone Spring formation.

(6) The Intervenor's Unit would be dedicated to the Duke Federal 10 Well No. 10H (API No. 30-025-pending), a horizontal well to be drilled from a surface location 2470 feet from the South line and 1906 feet from the West line (Unit K) of Section 10, Township 23 South, Range 34 East, NMPM, to a terminus 330 feet from the South line and 1546 feet from the West line (Unit N) of Section 15, Township 23 South, Range 34 East, NMPM. The completed interval of the proposed well will be orthodox.

(7) Both proposed wells are within the Antelope Ridge; Bone Spring, West Pool. Spacing in this pool is governed by Division Rule 19.15.15.9(A) NMAC, which provides for standard 40-acre units, each comprising a governmental quarter-quarter section. The Applicant's Unit and project area consists of four adjacent quarter-quarter sections. The Intervenor's Unit and project area consists of six adjacent quarter-quarter sections.

(8) Based on Division records, Mewbourne is the operator of the Pronghorn 15 B3DM Federal Com Well No. 1H (API No. 30-025-42968) which is producing in the Antelope Ridge; Bone Spring, West Pool and has a 160-acre project area (dedicated acreage) consisting of the W/2 W/2 of Section 15, Township 23 South, Range 34 East, NMPM.

(9) Applicant appeared at the hearing through counsel and presented land and geologic evidence to the effect that:

- (a) the Bone Spring formation in this area is suitable for development by horizontal drilling;
- (b) Applicant's proposed well is approximately one mile in length and is to be completed in the 3rd Bone Spring sand of the Bone Spring formation.
- (c) the proposed orientation of the horizontal well from North to South is appropriate for the Applicant's Unit;
- (d) all standard units to be included in the Applicant's Unit are expected to be productive in the Bone Spring formation, so that formation of the Unit as requested will not impair correlative rights;
- (e) Mewbourne has acquired approximately 74 percent of the working interest commitment within Section 15;
- (f) the Authorization for Expenditures (AFE) for the proposed one-mile well (dated August 26, 2016), has a total well cost of \$4,899,000;
- (g) Mewbourne demonstrated a history of effective development with one-mile length wells in this area including producing horizontal wells in Sections 9 and 15;
- (h) Mewbourne stated that it had no mineral interest in Section 10;
- (i) Mewbourne identified problems with the use of 1½-mile horizontal wells in other regions that has resulted in less efficient recovery of hydrocarbon due to drilling and completion complications associated with the additional one-half mile extension;
- (j) Mewbourne stated that if the Intervenor's proposed wells are approved and drilled, the resulting configuration would create a parcel in Section 10 (equaling approximately two quarter-quarter sections) that will become isolated and, therefore, uneconomical to develop with a horizontal well;
- (k) Mewbourne should be designated the operator of the proposed well and the proposed unit;
- (l) notice by certified mail was provided to all uncommitted interest owners in the proposed unit whose interests were evidenced by a conveyance instrument, either of record or known to Applicant when the application was filed, and to heirs known to Applicant of

deceased persons who appear as owners in such instruments, and whose whereabouts could be ascertained by exercise of reasonable diligence; and

- (m) those potentially affected parties whose whereabouts could not be ascertained were noticed by publication as provided in Rule 19.15.4.12(B) NMAC.

(10) Intervenor appeared at the hearing through counsel and presented land and geologic evidence to the effect that:

- (a) the Bone Spring formation in this area is suitable for development by horizontal drilling;
- (b) the Intervenor's proposed well is planned for horizontal length of 1½ miles and is to be completed in the 3rd Bone Spring sand of the Bone Spring formation;
- (c) the proposed orientation of the horizontal well from North to South is appropriate for the Intervenor's Unit and allows for the extension of the Intervenor's proposed well into the S/2 of Section 10;
- (d) all standard units to be included in the Intervenor's Unit are expected to be productive in the Bone Spring formation, so that formation of the Unit as requested will not impair correlative rights;
- (e) Black Mountain has acquired approximately 24 percent of the working interest commitment within Section 15;
- (f) the AFE for the proposed 1½-mile well (dated December 9, 2016) has a total well cost of \$7,210,337;
- (g) Black Mountain testified that when compared to a one-mile well, the 1½-mile horizontal well can achieve higher estimated ultimate recovery (EUR) of reserves and longer well life;
- (h) Black Mountain provided evidence of the performance of 1½-mile horizontal wells in the area completed in the shallower 2nd Bone Spring sand and Avalon Shale (upper Bone Spring formation);
- (i) Black Mountain estimated an increase of the EUR for the 1½-mile horizontal completion to be approximately 13,000 barrels of oil and 28 million cubic feet of gas with the inclusion of the setback areas at the common boundary of Sections 10 and 15;

- (j) Black Mountain also presented testimony supporting greater economic benefits for the 1½-mile well completion due to lower drilling cost per foot, reduced surface impacts and increased production life;
- (k) Black Mountain should be designated the operator of the proposed well and the Unit;
- (l) notice by certified mail was provided to all uncommitted interest owners in the proposed unit whose interests were evidenced by a conveyance instrument, either of record or known to the Intervenor when the application was filed, and to heirs known to the Intervenor of deceased persons who appear as owners in such instruments, and whose whereabouts could be ascertained by exercise of reasonable diligence; and
- (m) those potentially affected parties whose whereabouts could not be ascertained were noticed by publication as provided in Rule 19.15.4.12(B) NMAC.

(11) Based on Division records, Applicant's Pronghorn 15 B3CN Federal Com Well No. 1H (API No. 30-025-44011) has an active federal Application for Permit to Drill or Re-enter submitted on November 18, 2016, and approved on July 14, 2017.

(12) At hearing, both Mewbourne and Black Mountain offered evidence and testimony as to the protracted negotiations conducted between the two parties prior to the filing of Mewbourne's pooling application.

(13) In testimony, both Mewbourne and Black Mountain requested that 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.

(14) In testimony, both Mewbourne and Black Mountain stated reasonable charges for supervision (combined fixed rates) should be fixed at \$7,500 per month while drilling and \$750 per month while producing, provided that these rates should be allowed to adjust annually pursuant to the overhead section of the COPAS form titled "*Accounting Procedure-Joint Operations*".

(15) ICA Energy, Inc. appeared at hearing through counsel, but did not offer testimony or oppose the granting of this application. Patterson Properties and CML Exploration LLC appeared at hearing through counsel and offered a statement in support of the pooling application submitted by Mewbourne. All three parties are mineral interest owners in the acreage being considered in these cases. No other party appeared at the hearing, or otherwise opposed the granting of either application.

The Division concludes as follows:

(16) With competing pooling applications for the development of the same area, the Oil Conservation Commission has established precedent in Commission Order No. R-10731-B (Cases No. 11666 *De Novo* and No. 11677 *De Novo*) for comparing and assessing the evidence presented in support of the applications. The order identified the following list of criteria for use in the selection of the application with the best qualifications:

- (a) a comparison of geologic evidence presented by each party as it relates to the proposed well location and the potential of each proposed prospect to efficiently recover the oil and gas reserves underlying the property [Findings Paragraph (23)(f)];
- (b) a comparison of the risk associated with the parties' respective proposal for the exploration and development of the property [Findings Paragraph (23)(h)];
- (c) a review of the negotiations between the competing parties prior to the applications to force pool in order to determine if there was a "good-faith" effort [Findings Paragraph (23)(g)];
- (d) a comparison of the ability of each party to prudently operate the property and, thereby, prevent waste [Findings Paragraph (23)(i)];
- (e) a comparison of the differences in well cost estimates (AFE) and other operational costs presented by each party for their respective proposal [Findings Paragraph (23)(j)]; and
- (f) an evaluation of the mineral interest ownership held by each party at the time the application was heard [Findings Paragraph (23)(d) and (e)].

Of these criteria described in Order No. R-10731-B, the Commission stated that the comparison of the geologic evidence and prospect differences between the two applications is "*the most important consideration in awarding operations to competing interest owners*" [Findings Paragraph (23)(f)].

(17) Upon review of the evidence presented at hearing, the Division finds no significant difference in the geologic evidence and the related potential to efficiently recover the oil and gas reserves underlying the property. Both Mewbourne and Black Mountain presented geologic interpretations that were equivalent including the selection by each party for the same North-South orientation for their proposed horizontal wells.

(18) Additionally, both parties assigned the same risk factor including requesting similar overhead charges for drilling and operation, provided sufficient

evidence that negotiations were conducted in good faith, and submitted well cost estimates that were comparable based on the respective drilling program offered by each party.

(19) Black Mountain presented a plan of development with a 1½-mile horizontal well, but this operator could not offer any evidence of prior experience for completing a well of this length in the State of New Mexico.

(20) Mewbourne provided sufficient evidence establishing a greater capacity to prudently operate the property based on successful drilling operations for the targeted interval in this area along with active production from its existing horizontal well completed in the 3rd Bone Spring sand and located in the W/2 W/2 of Section 15.

(21) Mewbourne proved a larger control of the working interest for Section 15 with approximately 74 percent committed to Mewbourne while Black Mountain could provide documentation of approximately 24 percent committed to their proposed well.

(22) Finally, the Division identified a potential for "stranded acreage" in Section 10 should the three 1½-mile horizontal wells proposed by Black Mountain be approved. The continued development of Section 15 with one-mile horizontal wells as proposed by Mewbourne will prevent waste while protecting the correlative rights of mineral interest owners in Section 10.

(23) Mewbourne Oil Company should be designated operator of the Pronghorn 15 B3BO Federal Com Well No. 1H and the proposed spacing unit and project area.

(24) The application of Black Mountain Operating, LLC in this case should be denied.

(25) Approval of the proposed non-standard Unit will enable Applicant to drill a horizontal well that will efficiently produce the reserves underlying the Unit, thereby preventing waste, and will not impair correlative rights.

(26) 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.

(27) 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.

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

(29) 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 its just and fair share of hydrocarbons, the application of Mewbourne in Case No. 15602 should be approved by pooling all uncommitted interests, whatever they may be, in the oil and gas within the Unit.

(30) 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.

(31) Reasonable charges for supervision (combined fixed rates) should be fixed at \$7,500 per month while drilling and \$750 per month while producing, provided that these rates may be adjusted annually pursuant to the overhead section of the COPAS form titled "Accounting Procedure-Joint Operations."

IT IS THEREFORE ORDERED THAT:

(1) The application of Black Mountain Operating, LLC in Case No. 15628 for an order pooling all mineral interests in the Bone Spring formation underlying the E/2 W/2 of Section 15 and the E/2 SW/4 of Section 10, both in Township 23 South, Range 34 East, NMPM, Lea County, New Mexico, thereby forming a non-standard 240-acre, more or less, oil spacing and proration unit and project area in the Antelope Ridge; Bone Spring, West Pool, with said unit to be dedicated to applicant's Duke Federal 10 Well No. 10H (API No. 30-025-pending), a horizontal well to be drilled from a surface location surface location 2470 feet from the South line and 1906 feet from the West line (Unit K) of Section 10, to a terminus 330 feet from the South line and 1546 feet from the West line (Unit N) of Section 15, both in Township 23 South, Range 34 East, NMPM, is hereby denied.

(2) A non-standard 160-acre, more or less, oil spacing and proration unit and project area (the "Unit") is hereby established for the Bone Spring formation (Antelope Ridge; Bone Spring, West Pool (Pool code 2209)) consisting of the E/2 W/2 of Section 15, Township 23 South, Range 34 East, NMPM, in Lea County, New Mexico.

(3) Pursuant to the application of Mewbourne Oil Company ("Mewbourne"), all uncommitted interests, whatever they may be, in the oil and gas in the Bone Spring formation underlying the Unit, are hereby pooled.

(4) The Unit shall be dedicated to the **Pronghorn 15 B3CN Federal Com Well No. 1H** (API No. 30-025-44011), a horizontal well to be drilled from a surface location 185 feet from the North line and 1700 feet from the West line (Unit C) of Section 15, to a terminus 330 feet from the South line and 1800 feet from the West line (Unit N) of Section 15, Township 23 South, Range 34 East, NMPM. The completed interval of the proposed well will be orthodox.

(5) The operator of the Unit shall commence drilling the proposed well on or before December 31, 2018, and shall thereafter continue drilling the proposed well with due diligence to test the Bone Spring formation.

(6) In the event the operator does not commence drilling the proposed well on or before December 31, 2018, Ordering Paragraphs (1) and (2) 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 (2) 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 spacing units included in the proposed Unit within 120 days after commencement of drilling, then the operator shall apply to the Division for an amendment to this Order to contract the Unit so that it includes only those 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) Mewbourne Oil Company (OGRID 14744) 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 Division 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 Division 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 Division, and the Division has not objected, within 45 days following receipt of the schedule, the actual well costs shall be deemed to be the reasonable well costs. If there is an objection to actual well costs within the 45-day period, the Division will determine reasonable well costs after public notice and hearing.

(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 each non-consenting working interest owner's share of production from each well:

- (a) the proportionate share of reasonable well costs attributable to each such 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 \$7,500 per month while drilling and \$750 per month while producing, provided that these rates may, at the operator's discretion, be adjusted annually pursuant to the overhead provisions of the COPAS form titled "*Accounting Procedure-Joint Operations*." The operator is authorized to withhold from each pooled working interest owner's share of production from the subject well, such owner's proportionate share of both the supervision charges and the actual expenditures required for operating the well, not in excess of what are reasonable.

(17) Except as provided 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

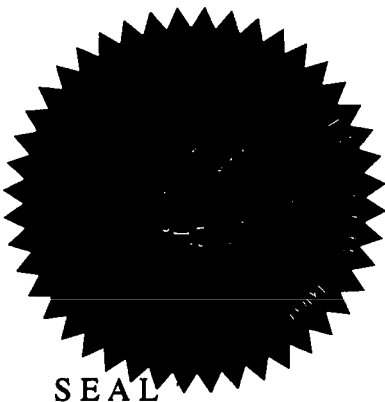
production shall be withheld only from the working interests' share of production, and no costs or charges shall be withheld from production attributable to royalty interests.

(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 Division in writing of the subsequent voluntary agreement of all parties subject to the compulsory pooling provisions of this Order.

(21) Jurisdiction of this case is retained for the entry of such further orders as the Division may deem necessary.

DONE at Santa Fe, New Mexico, on the day and year hereinabove designated.



STATE OF NEW MEXICO
OIL CONSERVATION DIVISION

David R. Catanach

DAVID R. CATANACH
Director