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

APPLICATION OF YATES PETROLEUM COMPANY FOR AN ORDER (1) DIRECTING PRIDE ENERGY COMPANY TO REIMBURSE YATES FOR THE WELL COSTS INCURRED BY YATES IN ITS ATTEMPT TO THE RE-ENTER THE STATE "X" WELL NO. 1 LOCATED IN SECTION 12, TOWNSHIP 12 SOUTH, RANGE 34 EAST, NMPM, PRIOR TO THE TIME PRIDE ASSUMED OPERATIONS OF THE WELL, AND (2) DIRECTING PRIDE ENERGY COMPANY TO ACCOUNT FOR AND PAY ALL SUMS IT IS NOW IMPROPERLY HOLDING PURSUANT TO EXPIRED ORDERS OF THE DIVISION AND COMMISSION, *AND* (3) REQUIRING PRIDE ENERGY COMPANY TO PLUG AND ABANDON THE STATE "X" WELL NO. 1, LEA COUNTY, NEW MEXICO.

CASE NO. 13531
De Novo

HEARING MEMORANDUM

BACKGROUND:

In September 2003, Yates Petroleum Corporation ("Yates")[1] commenced re-entry operations on the State "X" Well No. 1 **(API No. 30-025-01838)** located 1980 feet from the North line and 660 feet from the West line (Unit E) of Section 12, Township 12 South, Range 34 East, NMPM, Lea County, New Mexico. These re-entry operations were conducted pursuant to a Division-approved Application for Permit to Drill ("APD"). The well is located on lands leased to Yates. On September 10, 2003, Pride Energy Company ("Pride") filed an application seeking, among other things, an order of the Oil Conservation Division canceling the Yates drilling permit, haulting Yates drilling operations, pooling the W/2 of Section 12, and designating Pride operator of the State "X" Well No. 1 and the Yates acreage on which it is located. Thereafter, Yates agreed to voluntarily move the rig off location and stop its work on this well pending a decision by the Division on the Pride application. By Order No. R-12108, dated March 2, 2004, the Division granted Pride's application and removed Yates as operator of this well. Copies of all of the Division and Commission orders related to the dispute are attached

[1] Yates Petroleum Corporation, Yates Drilling Company, ABO Petroleum Corporation and MYCO Industries, Inc. are hereinafter collectively referred to as "Yates." Together the Yates parties own 100% of the working interest in State of New Mexico Oil and Gas Lease No. V-5855 that covers the N/2 and SE/4 of Section 12, Township 12 South, Range 34 East, NMPM, Lea County, New Mexico.

to this memorandum.

On *de novo* appeal, the Commission entered Order No. R-12108-A which again pooled these lands and named Pride operator of the State "X" Well No. 1. This Order also required Pride to reimburse Yates for reasonable costs incurred by Yates in connection with its re-entry operations on this well prior to filing of the Pride application. Order No. R-12108-A, Finding 10.

To clarify what costs were to be reimbursed, Yates sought and was granted a rehearing on this issue. Following rehearing, the Commission entered Order No. R-12108-C, dated December 9, 2004, which authorized the reimbursement of "actual well costs incurred by Yates in conducting re-entry operations on the subject well after August 25, 2003 and prior to October 7, 2004, the time when Yates voluntarily ceased operations on the subject well." Order No. R-12108-C, Order Paragraph 9.

Prior to commencing re-entry operations on this well on February 15, 2005, Pride was fully aware of what it was required to reimburse to Yates. The Commission had twice directed it to reimburse these costs and Yates had provided Pride with an itemized schedule of these costs.[2]

To force Pride to reimburse the funds it had been directed to pay, Yates had to file the application in this case seeking an order from the Division requiring Pride to pay the funds it was improperly holding. Pride filed for *de novo* review of this order to enable it to once again argue against certain costs covered by prior Commission orders.

Now with this *de novo* appeal, Pride asks the Commission to order Yates to pay for a second time certain costs that are the sole result of the actions of Pride. These costs, for which it now seeks reimbursement, were incurred only because the Division and Commission repeatedly authorized Pride to conduct activities on the Yates lease over the vigorous objections of Yates. If Yates had been allowed to continue its re-entry operations on this well, these costs would not have been twice incurred.

Reimbursement of Costs:

Pride has twice obtained orders pooling this spacing unit, twice allowed the pooling order to expire, twice failed to recomplete this well, and now has to clean up the site and plug the

[2] The costs to which Pride objects were identified in Exhibit A to its letter to the Commission dated January 19, 2006. A copy of this list is attached to the Stipulated Facts filed in this case. See Stipulated Fact No. 17.

well.[3] Now Pride asks the Commission to pass certain costs that are the sole result of its actions to Yates. The Commission should deny this request.[4]

Because of the Division and Commission-ordered change of operator, certain costs related to the re-entry of the State "X" Well No. 1 have had to be incurred twice. The question presented in this appeal is who will bear these costs? Will it be Pride or Yates? This is the central issue before the Commission in this case and the only issue discussed at the June 11, 2007 Prehearing conference in this case.

There is no dispute that some of the costs incurred by Yates while conducting operations on the well were incurred a second time by Pride while it was in charge of these operations. There is also no dispute as to the reasonableness of these charges. Although Pride objects to these costs, its objections are not directed at the amount of these individaul charges. See Order No. R-12547, Findings (10) through (14). Pride does not assert that the amount of any charge is unreasonable, it just objects to being required to twice pay certain costs incurred in these re-entry attempts – once by paying these costs as operator and again by reimbursing these costs to Yates.[5]

However, if Pride's request in this case is granted, Yates would have to bear the costs incurred while Yates was conducting re-entry operations on the well and Yates would then have borne them a second time when it paid its share of Pride's AFE costs pursuant to Commission

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[3] Today, the location needs to be cleaned and the well plugged. To assure this is done, Yates has again had to file an application with the Division. (Case No. 13940: Application of Yates Petroleum Corporation, Yates Drilling Company, ABO Petroleum Corporation, and MYCO Industries, Inc. for an order directing Pride Energy Company to plug and abandon the State "X" Well No. 1, Lea County, New Mexico).

[4] Before Pride's second force pooling application was heard by the Division, Yates objected to the proceedings until all issues, including well cost issues, under the first pooling order had been resolved. (Order No. R-12108-A). Although Yates vigorously objected to the second force pooling hearing, its argument was dismissed by the hearing examiner because Pride made payment under Order No. R-12108-A prior to the issuance of the second pooling order. It would be completely inequitable at this time to allow an issue that was required to be settled prior to the issuance of the second force pooling order to be heard and appealed at this time. Yates would be denied due process under the second force pooling if Pride's request is granted.

[5] Pride only advances part of this argument, for as observed by the Division a portion of these costs could be billed to the other interest owners in the spacing unit who elect to participate in the well. See, Order No. R-12547, Finding 15.

pooling orders.[6] The question is whether it is reasonable for Pride, the party who sought the change of operator, to bear these costs, or should the party who was removed as operator by the Division and Commission at the request of Pride now be further penalized by being required to bear certain cost of these operations for a second time.[7]

Yates believes the questions raised by Pride in this *de novo* appeal have already been answered by the Division and Commission in each of the pooling orders entered in this dispute. In Order No. R-12108, R-12108-A and R-12108-C, the Division and Commission, after a full review of all of the facts and the equities of this dispute, have told Pride to reimburse these costs to Yates.

Attorney Fees:

Pride advised Yates on June 28th that it will also seek the reimbursement of Pride's attorney fees in these cases. Although this issue was not addressed at the pre-hearing conference, it does not present a question that requires witness support. This appeal has been pending for months and Yates is anxious to get all Oil Conservation Commission issues between the parties resolved. If this additional issue is properly raised, and if the Commission is satisfied that it can dispose of this issue based on the written submittals of the parties, Yates does not object to the consideration of this matter. Should the Commission determine that additonal presentations of the evidence, argument, or briefing are needed, Yates will provide whatever additional information the Commission desires.

Pride's claim for attorney fees was raised before the Examiner and denied because there was no evidence to demonstrate that these costs were authorized by contract or statute and were therefore determined to be unreasonable. See Order No. R-12547, Finding (20). "New Mexico adheres to the so-called American rule that, absent statutory or other authority, litigants are responsible for their own attorney's fees." ***Montoya v. Villa Linda Mall***, 110 N.M. 128, 129, 793

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[6] Yates paid its share of Pride's AFE costs for Pride's first re-entry attempt. If Pride is not required to reimburse costs as required in the Commission's original pooling order, Yates will bear these costs twice. Based on the limited information it was receiving on Pride's first attempt to recomplete this well, Yates elected not to participate in Pride's second re-entry attempt.

[7] For example, while Yates was the operator of the State "X" Well No. 1, it paid the insurance costs which Pride reimbursed and for which it now seeks a refund. However, when Yates paid its share of Pride's AFE costs for the first re-entry attempt, it also paid its share of Pride's insurance costs. To grant Pride's request and require Yates to reimburse these funds to Pride means that Yates has to pay twice cost that would not have been incurred except for actions of Pride, the Division and Commission to which Yates vigorously objected.

P.2d 258, 259 (1990). The American rule recognizes the authority of statute, court rule, or contractual agreement. *See* 1 Robert L. Rossi, *Attorneys' Fees* § 7:1, at 336 (2d ed. 1995). No evidence has been produced that would to entitle Pride to the recovery of these costs and this request, if it is properly before the Commission in this appeal, should be denied.

CONCLUSION:

To remove Yates as operator of a well on its own lease on which it was conducting re-entry operations pursuant to a Division-approved Application for Permit to Drill and then require it to pay a second time certain costs that were incurred only because of the actions of Pride, is clearly unreasonable. Pride sought to remove Yates as operator of this well. Its application was granted. One result of this order was that certain costs would have to be incurred twice. The question presented in this appeal is who will bear these costs? Who will pay twice? Will it be Pride or Yates? The Commission should not now further penalize Yates by requiring it to pay twice for the Pride fiasco.

Yates requests that the Commission deny the issue concerning the duplicate costs raised by Pride in this appeal, deny Pride's request for attorney fees, and otherwise affirm the provisions of Division Order No. R-12547 - which Pride does not challenge.

Respectfully submitted,

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ATTORNEYS FOR YATES PETROLEUM CORPORATION

CERTIFICATE OF SERVICE

I certify that on June 29, 2007 I served a copy of the foregoing Hearing Memorandum by Hand Delivery or Facsimile to:

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STATE OF NEW
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. 13153
ORDER NO. R-12108

APPLICATION OF PRIDE ENERGY COMPANY FOR CANCELLATION OF A DRILLING PERMIT AND RE-INSTATEMENT OF A DRILLING PERMIT, AN EMERGENCY ORDER HALTING OPERATIONS, AND COMPULSORY POOLING, LEA COUNTY, NEW MEXICO.

ORDER OF THE DIVISION

BY THE DIVISION;

This case came on for hearing at 8:15 a.m. on October 23, 2003, at Santa Fe, New Mexico, before Examiner David R. Catanach.

NOW, on this 2nd day of March, 2004, the Division Director, having considered the testimony, the record, and the recommendations of the Examiner,

FINDS THAT:

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

(2) The applicant, Pride Energy Company ("Pride"), seeks an order pooling all mineral interests from the surface to the base of the Mississippian formation underlying the W/2 of Section 12, Township 12 South, Range 34 East, NMPM, Lea County, New Mexico, thereby forming a standard 320-acre spacing unit for all formations and/or pools spaced on 320 acres within this vertical extent, which presently include, but are not necessarily limited to, the Undesignated Four Lakes-Mississippian Gas Pool and the Undesignated Four Lakes-Morrow Gas Pool. This unit is to be dedicated to the plugged and abandoned State "X" Well No. 1 (API No. 30-025-01838) to be re-entered by the applicant at a standard surface location 1980 feet from the North line and 660 feet from the West line (Unit E) of Section 12.

(3) Pride also seeks an order canceling Yates Petroleum Corporation's drilling

BEFORE THE OIL CONSERVATION COMMISSION
Santa Fe, New Mexico
Case Nos. 13531 Exhibit No. 2
Submitted by:
Yates Petroleum Corporation
Hearing Date: July 13, 2006

permit (Division Form C-101, Application for Permit to Drill, Re-Enter, Deepen, Plugback, or Add a Zone ("APD")) for the State "X" Well No. 1 (designated by Yates Petroleum Corporation as the Limbaugh "AYO" State Well No. 1), which was approved by the Division on August 26, 2003. In addition, Pride seeks re-instatement of its drilling permit for the State "X" Well No. 1, which was approved by the Division on July 16, 2003, and subsequently cancelled by the Division on August 26, 2003. Pride also seeks an emergency order preventing Yates Petroleum Corporation from conducting any re-entry operations on the State "X" Well No. 1.

(4) Yates Petroleum Corporation ("Yates") appeared at the hearing through legal counsel in opposition to the application.

(5) For the purpose of this order, the subject existing wellbore, designated by Yates as the Limbaugh "AYO" State Well No. 1, and designated by Pride as the State "X" Well No. 1, will hereinafter be referred to as the State "X" Well No. 1.

(6) Prior to the hearing, both Pride and Yates filed various pleadings with the Division regarding the drilling permits for the State "X" Well No. 1 and the subject compulsory pooling application. These filings, and the Division's actions regarding these requests, are summarized as follows:

(a) on September 10, 2003, Pride filed the compulsory pooling application for the State "X" Well No. 1 that is the subject of Case No. 13153. Additionally on this date, Pride filed a request ("Pride's motion") that the Division enter an emergency order requiring Yates to cease all re-entry operations on the State "X" Well No. 1. Yates commenced re-entry operations on the State "X" Well No. 1 on or about September 5, 2003;

(b) on September 10, 2003, Yates filed a response to Pride's motion, and also filed a motion to dismiss Pride's compulsory pooling application ("Yates' motion");

(c) on September 12, 2003, the Division Examiner issued a decision on the motions of Pride and Yates. In that decision, the Division Examiner determined that Pride's request for an emergency order requiring Yates to cease re-entry operations on the State "X" Well No. 1 should be deferred until such time as an evidentiary hearing on the merits of Pride's application in Case No. 13153 was conducted. Additionally, the Division Examiner denied the Yates motion to dismiss Case No. 13153;

(d) on September 17, 2003, Yates filed an application for hearing *De Novo* before the Oil Conservation Commission to appeal the decision of the Hearing Examiner;

(e) subsequently, Ms. Lori Wrotenbery, the Director of the Oil Conservation Division and Chair of the Oil Conservation Commission, entered a decision in Yates' *De Novo* application. In that decision, Ms. Wrotenbery determined that the Division did not dispose of any issues existing in the case, and that the Examiner decision gave few reasons for denying Yates' motion to dismiss Prides' application. Consequently, Ms. Wrotenbery ordered that:

"Case No. 13153 is remanded to the Division Hearing Examiner for full consideration of the legal issues that may be raised by Yates' Motion to Dismiss, with a decision to be issued on that matter prior to any hearing of the factual issues related to Pride's compulsory pooling application"; and

(f) subsequent to the entry of the Director's decision, the Division Examiner met with legal counsel for Yates and Pride. In that meeting, it was determined and agreed to by all parties that the evidentiary hearing in Case No. 13153 would proceed prior to the Division entering any additional decisions on the Yates and Pride motions.

(7) Findings Nos. 8-16, as follow, depict the events that occurred prior to the hearing. This information was obtained through Pride's testimony and Division records.

(8) On May 25, 2001, the Oil Conservation Division's Hobbs District Office ("Hobbs OCD") approved Yates' APD to re-enter the plugged and abandoned State "X" Well No. 1 to test the Mississippian formation. The N/2 of Section 12 was to be dedicated to the well forming a standard 320-acre spacing and proration unit for the Undesignated Four Lakes-Mississippian Gas Pool. The approved APD stated that the permit would expire on May 25, 2002 unless re-entry operations were underway by that date.

(9) On April 15, 2002, Yates applied for a one-year extension of its drilling permit for the State "X" Well No. 1. Yates' request was granted by the Hobbs OCD on April 18, 2002.

(10) On May 30, 2003, the Hobbs OCD notified Yates by letter that its APD for the State "X" Well No. 1 had expired and that any subsequent re-entry and drilling operations on this well would require an additional permit from the Hobbs OCD.

(11) On July 15, 2003, Pride filed an APD with the Hobbs OCD to re-enter the State "X" Well No. 1 to test the Mississippian formation. The W/2 of Section 12 was to be dedicated to the well forming a standard 320-acre spacing and proration unit. This APD was approved by the Hobbs OCD on July 16, 2003.

(12) On July 15, 2003, Pride sent a well proposal to Yates for the State "X" Well No. 1. In this letter, Pride invited Yates to voluntarily participate in the re-entry of the well.

(13) On August 26, 2003, the Hobbs OCD cancelled Pride's APD for the State "X" Well No. 1. In the letter to Pride, the Hobbs OCD stated that "upon further review of the area, the North half of this section is leased to another operator."

(14) On August 26, 2003, Yates filed a new APD with the Hobbs OCD to re-enter the State "X" Well No. 1 to test the Mississippian formation. Yates' APD was approved by the Hobbs OCD on August 26, 2003.

(15) On September 5, 2003, Yates moved a rig onto the State "X" Well No. 1 and commenced re-entry operations.

(16) Prior to the hearing on October 23, 2003, Yates voluntarily moved off the State "X" Well No. 1, and as far as the Division is aware, Yates is not currently performing any re-entry operations on the well.

(17) Pride presented the following-described evidence regarding the lease status and interest ownership within Section 12:

(a) the SW/4 of Section 12 is a single state lease (State Lease No. V-6256). Pride is the leaseholder of this acreage; and

(b) the N/2 and SE/4 of Section 12 is a single state lease (State Lease No. V-5855). Yates is the leaseholder of this acreage. Additional working interest owners in this lease include Yates Drilling Corporation, Abo Petroleum Corporation, and MYCO Industries, Inc. (collectively "Yates").

(18) Pride contends that:

(a) Pride was issued a valid APD to re-enter the State "X" Well No. 1 on July 16, 2003. This APD stated

that the permit would expire one year from the approval date unless re-entry operations were underway on the well. The Hobbs OCD illegally cancelled this permit by letter dated August 26, 2003;

(b) Yates' APD filed August 26, 2003 and approved by the Hobbs OCD on August 26, 2003, was improperly granted;

(c) Yates does not "own" the wellbore located in the NW/4 of Section 12. This well was drilled and abandoned in 1957, and the lease under which the well was drilled has long since expired. Applicable case law provides that at the expiration of a lease, the wellbore reverts back to the surface owner, in this case the Commissioner of Public Lands for the State of New Mexico. Since Yates does not "own" the wellbore, it is available for forced pooling;

(d) Pride has a property interest in its APD, not in the NW/4 of Section 12. It is that interest that is subject to due process considerations; and

(e) the compulsory pooling statute (NMSA 1978, 70-2-17) provides sufficient flexibility to allow the operator of a pooled unit to conduct operations anywhere on that unit, regardless of whether the owner of the land on which the well is located has consented thereto.

(19) Yates contends that:

(a) the NW/4 of Section 12 is not available to be forced pooled by Pride because it is already included within a voluntary standard spacing unit comprised of the N/2 of Section 12;

(b) Pride has no interest in the N/2 of Section 12, nor does it have any interest in the State "X" Well No. 1;

(c) by virtue of being the lessee of State Lease No. V-5855, Yates does have the right to utilize this previously plugged and abandoned wellbore;

(d) Pride's APD dated July 10, 2003 by itself does not convey to Pride an interest in the NW/4 of Section 12, nor does it convey to Pride an interest in the State "X" Well No. 1; and

(e) the cancellation of Pride's APD does not constitute a violation of its due process rights. For Pride's due process rights to be violated, it must first have rights in the subject acreage that are impaired by the Division's actions. Pride does not have a constitutionally protected property right in the NW/4 of Section 12.

(20) Pride presented geologic evidence that demonstrates that:

(a) the primary target within the State "X" Well No. 1 is the Mississippian formation;

(b) in July, 2001 Pride completed the State "M" Well No. 1, located 660 feet from the South and West lines (Unit M) of Section 1, Township 12 South, Range 34 East, NMPM, in the Mississippian formation. This well, which is a direct north offset to the State "X" Well No. 1, has produced from the Mississippian formation since being completed, and is currently producing at a rate of approximately 350 MCF of gas per day;

(c) there is a fault located on the western boundary of Section 12 that traverses this section generally in a north-south direction. The down-throne side of the fault is located on the east side of the fault line;

(d) the Mississippian reservoir, which is present on the down-throne side of the fault, appears to have developed along this north-south trending fault in Section 12. The greater porosity within this reservoir is located in close proximity to the fault, and has been enhanced by tectonic fracturing. This is evidenced by the porosity development within the State "X" Well No. 1, which shows 36 feet of gross pay development, and 25 feet of pay with at least 7% porosity. This well is located approximately 700 feet east of the fault;

(e) due to the location and orientation of this Mississippian reservoir, the W/2 of Section 12 appears to have sufficient porosity development, and is therefore likely to be productive, in this interval;

(f) the porosity within this Mississippian reservoir diminishes as you move east away from the fault. This is evidenced by the lack of porosity within the State QE "13" Well No. 1 located 660 feet from the South line and 1980 feet from the West line (Unit N) of Section 13, Township 12 South, Range 34 East, NMPM. This well is located approximately 2,640 feet east of the fault; and

(g) a well drilled within the SW/4 of Section 12 will be located a greater distance away from the fault than the State "X" Well No. 1. Consequently, drilling a well within this quarter section is a much riskier prospect than simply re-entering and testing the State "X" Well No. 1.

(21) Pride testified that the orientation of the Mississippian reservoir in Section 12 is better suited to a stand-up proration unit comprising the W/2 of Section 12, and that due to the lack of porosity development within the E/2 of Section 12, this area will likely be non-productive in the Mississippian formation.

(22) Upon consideration of the evidence presented by both parties in this case, the Division finds that:

(a) for a period of approximately two years following the completion of the State "M" Well No. 1, Yates possessed a valid permit to re-enter the State "X" Well No. 1. During this time period, Yates took no action with regards to the well;

(b) Yates allowed its drilling permit for the State "X" Well No. 1 to expire on May 25, 2003;

(c) at the time Pride filed its APD for the State "X" Well No. 1, there was no other valid APD in effect for the well. In addition, the NW/4 of Section 12 was not contained within a spacing unit, and was therefore available to be included within a W/2 dedication, either by virtue of being voluntarily committed or forced pooled;

(d) Pride's APD was duly approved by the Hobbs OCD in accordance with Division rules; and

(e) in accordance with a procedure widely practiced in the oil and gas industry, Pride proposed the re-entry of the State "X" Well No. 1 to Yates, the only other working interest owner in the W/2 of Section 12. After it received no response from Yates, Pride then proceeded, in accordance with the compulsory pooling statute (NMSA 1978, 70-2-17), to file an application to pool the interest of Yates within the W/2 of Section 12.

(23) Upon consideration of the evidence regarding the cancellation of Pride's APD for the State "X" Well No. 1, the Division finds that:

(a) when an APD is filed, the Division does not determine whether the applicant can validly claim the right to drill or re-enter the well that is the subject of the application. The courts of the State of New Mexico have exclusive jurisdiction to determine such matters. It is the responsibility of the operator filing an APD to do so under a good faith claim to title and a good faith belief that it is, or in this case will be, authorized to drill or re-enter the well applied for. See Commission Order No. R-11700-B (March 26, 2002);

(b) it appears that Pride had a good faith belief that it would be authorized to re-enter the State "X" Well No. 1 when it filed its APD and simultaneously sent a well proposal to Yates;

(c) the principal reason for the cancellation of Pride's drilling permit by the Hobbs OCD appears to have been that the N/2 of Section 12 was leased to Yates. It is a common industry practice to submit APD's that embrace more than one lease and/or more than one lessee in a standard spacing unit. This situation generally does not preclude the approval of an APD because the applicant is then provided with flexibility to consolidate the interests within the spacing unit, either by voluntary agreement or forced pooling;

(d) the Hobbs OCD cancelled Pride's drilling permit for the State "X" Well No. 1 without giving Pride notice of the intended action; and

(e) the Hobbs OCD did not state sufficient cause to cancel Pride's drilling permit for the State "X" Well No. 1 and violated Pride's due process rights by canceling Pride's drilling permit without notice and opportunity to show why the drilling permit should not be cancelled.

(24) Because the drilling permit issued to Pride for the State "X" Well No. 1 was not duly cancelled, the drilling permit subsequently issued to Yates for the same well is invalid.

(25) Yates chose not to present geologic evidence in this case.

(26) The geologic evidence presented by Pride demonstrates that within Section 12, the W/2 contains the majority of the productive acreage in the Mississippian formation.

(27) The evidence further demonstrates that Pride's proposed spacing unit orientation within Section 12 conforms better, geologically, to the Mississippian reservoir underlying Section 12.

(28) The evidence further demonstrates that Pride has proceeded in a prudent manner to develop the gas reserves in the Mississippian formation underlying the W/2 of Section 12, and has conformed to Division rules and regulations in its actions.

(29) Approval of the subject application will afford Pride the opportunity to recover its equitable share of the gas reserves in the Mississippian formation underlying the W/2 of Section 12, will prevent the drilling of unnecessary wells, and will otherwise protect correlative rights.

(30) The application of Pride should be approved.

(31) Pride's APD for the State "X" Well No. 1 dated July 10, 2003 should be reinstated.

(32) Yates' APD for the State "X" Well No. 1 dated August 25, 2003 should be cancelled.

(33) The motion of Yates to dismiss Case No. 13153 should be denied.

(34) Two or more separately owned tracts are embraced within the proposed W/2 spacing unit (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.

(35) Applicant is an owner of an oil and gas working interest within the Unit. Applicant has the right to re-enter and proposes to re-enter the State "X" Well No. 1 (the "proposed well") to test the Mississippian formation at a standard well location within the NW/4 of Section 12.

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

(37) 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, this application should be approved by pooling all uncommitted interests, whatever they may be, in the oil and gas within the Unit.

(38) Applicant should be designated the operator of the subject well and of the Unit.

(39) 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 re-entering and drilling the well.

(40) Reasonable charges for supervision (combined fixed rates) should be fixed at $5,000.00 per month while drilling and $600.00 per month while producing, provided that these rates should be adjusted annually pursuant to Section III.1.A.3. of the COP AS form titled *"Accounting Procedure-Joint Operations."*

IT IS THEREFORE ORDERED THAT:

(1) Pursuant to the application of Pride Energy Company, all uncommitted interests, whatever they may be, in the oil and gas from the surface to the base of the Mississippian formation underlying the W/2 of Section 12, Township 12 South, Range 34 East, NMPM, Lea County, New Mexico, are hereby pooled to form a standard 320-acre gas spacing and proration unit for all formation or pools spaced on 320 acres within this vertical extent, which presently include, but are not necessarily limited to, the Undesignated Four Lakes-Mississippian Gas Pool and the Undesignated Four Lakes-Morrow Gas Pool. The Unit shall be dedicated to the plugged and abandoned State "X" Well No. 1 (API No. 30-025-01838) to be re-entered by the applicant at a standard surface location 1980 feet from the North line and 660 feet from the West line (Unit E) of Section 12.

(2) The operator of the Unit shall commence re-entry and drilling operations on or before June 1, 2004 and shall thereafter continue drilling the well with due diligence to test the Mississippian formation.

(3) In the event the operator does not commence re-entry and drilling operations on or before June 1, 2004, Ordering Paragraph (1) shall be of no effect, unless the operator obtains a time extension from the Division Director for good cause.

(4) Should the subject well not be drilled and completed within 120 days after commencement thereof, Ordering Paragraph (1) shall be of no further effect, and the unit created by this Order shall terminate unless the operator appears before the Division Director and obtains an extension of time to complete the well for good cause demonstrated by satisfactory evidence.

(5) Upon final plugging and abandonment of the subject well, the pooled unit created by this Order shall terminate, unless this order has been amended to authorize further operations.

(6) Applicant is hereby designated the operator of the subject well and of the Unit.

(7) 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 re-entering, drilling, completing and equipping the subject well ("well costs").

(8) 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."

(9) 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.

(10) 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.

(11) The operator is hereby authorized to withhold the following costs and charges from production:

(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.

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

(13) Reasonable charges for supervision (combined fixed rates) are hereby fixed at $5,000.00 per month while drilling and $600.00 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.

(14) Except as provided in Ordering Paragraphs (11) and (13) above, all proceeds from production from the well that are not disbursed for any reason shall be placed in escrow in Lea County, New Mexico, to be paid to the true owner thereof upon demand and proof of ownership. The operator shall notify the Division of the name and address of the escrow agent within 30 days from the date of first deposit with the escrow agent.

(15) Any unleased mineral interest 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.

(16) 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.

(17) The operator of the well and Unit shall notify the Division in writing of the subsequent voluntary agreement of all parties subject to the forced pooling provisions of this order.

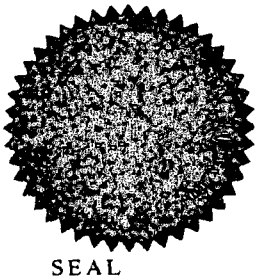
(18) Pride Energy Company's APD for the State "X" Well No. 1 dated July 10, 2003 is hereby re-instated.

(19) Yates Petroleum Corporation's APD for the State "X" Well No. 1 dated August 25, 2003 is hereby cancelled *ab initio*.

(20) Yates Petroleum Corporation's Motion to Dismiss Case No. 13153 is hereby denied.

(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.



SEAL

STATE OF NEW MEXICO
OIL CONSERVATION DIVISION

Lori Wrotenbery

LORI WROTENBERY
Director

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

IN THE MATTER OF THE HEARING CALLED BY THE OIL CONSERVATION COMMISSION FOR THE PURPOSE OF CONSIDERING:

CASE NO. 13153, *de novo*

APPLICATION OF PRIDE ENERGY COMPANY FOR CANCELLATION OF A DRILLING PERMIT AND REINSTATEMENT OF A DRILLING PERMIT, AN EMERGENCY ORDER HALTING OPERATIONS, AND COMPULSORY POOLING, LEA COUNTY, NEW MEXICO

ORDER NO. R-12108-A

ORDER OF THE OIL CONSERVATION COMMISSION

BY THE COMMISSION:

THIS MATTER came before the Oil Conservation Commission (the Commission) for hearing on August 12, 2004 at Santa Fe, New Mexico on the application of Yates Petroleum Corporation for *de novo* review, and the Commission, having heard the evidence and arguments of counsel and carefully considered the same, now, on this 9th day of September, 2004,

FINDS:

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

2. In the original application in this case, Pride Energy Company (Pride) sought an order canceling a permit issued to Yates Petroleum Corporation (Yates) to re-enter the abandoned State X Well No. 1 (API No. 30-025-07838) (the subject well), located 1980 feet from the North line and 660 feet from the West line (Unit E) of Section 12, Township 12

South, Range 34 East. NMPM, Lea County, New Mexico. Pride also sought reinstatement of a drilling permit previously issued to it to re-enter the same well, and an emergency order preventing Yates from conducting any operations on the well.

3. Pride additionally sought an order pooling all uncommitted mineral interests underlying the W/2 of Section 12, Township 12 South, Range 34 East, NMPM, Lea County, New Mexico, from the surface to the base of the Mississippian formation, forming a standard 320-acre gas spacing and proration unit (the Unit) for all formations or pools spaced on 320 acres within this vertical extent, which presently include, but are not necessarily limited to, the undesignated Four Lakes-Mississippian Gas Pool and the undesignated Four Lakes-Morrow Gas Pool, such unit to be dedicated to the well.

4. Both Yates and Pride appeared at the hearing through counsel and presented land and technical testimony. Pride presented the testimony of John W. Pride, a petroleum landman and one of the principals of Pride, and Jeff Ellard, a geologist employed by Pride. Yates presented the testimony of Charles E. Moran, a landman employed by Yates, John Amiet, a geologist employed by Yates, and David F. Boneau, a petroleum engineer employed by Yates.

Undisputed Facts

5. Based on the statements of counsel and testimony offered by the parties, the Commission concludes that the following facts pertinent to this case are undisputed:

(a) Yates is the owner of the entire working interest in the north half and southeast quarter of Section 12, Township 12 South, Range 34 East.

(b) Pride is the owner of the entire working interest in the southwest quarter of Section 12.

(c) The subject well is located in the northwest quarter of Section 12 on land leased exclusively to Yates.

(d) Pride is the operator of the State M Well No. 1 (API No. 30-025-20689) (the State M), located 660 feet from the south and west lines of Section 1, Township 12 South, Range 34 East, which well is completed in, and producing from, the Mississippian formation. That well is dedicated to a spacing unit comprising the west half of Section 1, pursuant to a voluntary unit agreement to which Pride and Yates are both parties.

(e) On May 24, 2001 Yates filed an Application for Permit to Drill (APD) to re-enter the subject well, which it designated the "Limbaugh AYO State Well No. 1", and to which it proposed to dedicate a spacing unit comprising the north half of Section 12. The Division approved that APD on May 25, 2001.

(f) On April 15, 2002, in anticipation of the forthcoming expiration of its APD, Yates filed a sundry notice to extend its APD for an additional year, until May 25, 2002. The Division approved the requested extension on April 18, 2002.

(g) On May 25, 2003, Yates' APD to re-enter the subject well expired.

(h) On July 10, 2003, Pride filed an APD to re-enter the subject well under the name "State X Well No. 1," to which it proposed to dedicate a spacing unit comprising the west half of Section 12, including the southwest quarter, which is leased to Pride.

(i) Pride's APD was approved by the Division on July 16, 2003.

(j) On August 25, 2003, Yates filed a new APD to re-enter the subject well, again designating the well as the "Limbaugh AYO State No. 1" and again proposing to dedicate to the well a spacing unit comprising the north half of Section 12.

(k) On August 26, 2003, Chris Williams, District Supervisor of OCD District 1, approved Yates' APD for the subject well, and prepared a letter to Pride canceling Pride's APD.

(l) Yates has stipulated that it will undertake no operations with respect to the subject well pending the Commission's decision, thereby mooting Pride's request for an emergency order prohibiting such operations.

Technical Evidence

6. Although the history and land ownership are basically undisputed, as indicated in the foregoing findings, there exists controversy concerning the technical aspects of the case.

7. Mr. Ellard, Pride's geologist, testified that the objective in re-entering the subject well would be the Austin cycle of the upper Mississippian (the target reservoir), in which production was encountered in the State M, to the north of the subject well.

8. Mr. Ellard further testified that the target reservoir was formed by shedding of fragmented rock from a raised fault block produced by faults lying to the west of these two wells. In wells farther to the south and east, away from the faulting, where the rock was not fragmented, the formation is present, but with insufficient porosity to be productive.

9. Mr. Ellard opined that producible hydrocarbons would most likely be located closest to the fault because, of the material shed from the upthrown side of the fault, that material composed of larger particles, and therefore characterized by greater porosity and permeability, would be deposited in close proximity to the fault.

10. Mr. Ellard placed the fault that created this reservoir on a bearing more or less north to south and located a short distance to the west of the State M and the subject well, generally along and close to the section line between Section 12 and the adjacent Section 11. On this basis, he opined that the subject well would more likely drain producible hydrocarbons from the quarter section lying south of the subject well (the southwest quarter of Section 12), than from the quarter section lying east of the subject well (the northeast quarter of Section 12).

11. Mr. Ellard testified that it is not possible to determine with any degree of accuracy the extent of the target reservoir with the information presently available. However, he opined, based on comparison of the old log of the subject well with the old log of the State M, that the subject well would likely encounter a comparable thickness of pay in the target reservoir (25 feet as compared to 30 feet in the State M).

12. Mr. Amiet, Yates' geologist, agreed generally with Mr. Ellard's interpretation of the nature of the target reservoir and the mechanism of deposition, including the assessment that the extent of the target reservoir could not be determined with available information, but disagreed with Mr. Ellard's placement of the fault that produced the up-thrown block from which the reservoir material was presumably eroded.

13. Mr. Amiet testified that 3D seismic run along a west-to-east bearing close to the location of the subject well, and which was admitted in evidence, demonstrated that no significant fault down-thrown to the east existed in the westward proximity of the subject well. He opined that the fault that controls the location of the target reservoir runs to the north of the State M and trends northeast to southwest. Accordingly, he concluded that the subject well is more distant from the fault than is the State M, and the Pride acreage in the southwest quarter of Section 12 is yet more distant.

14. Mr. Amiet interpreted the logs from the subject well to show no more than 10 feet of reservoir in the target formation (as compared to 30 feet in the Ml), confirming his conclusion that the subject well is more distant from the fault.

15. Mr. Amiet testified that Yates had other 3-D seismic runs that tended to confirm his placement of the controlling fault, but he did not offer this other seismic information in evidence.

16. Mr. Amiet further testified that the prevailing contours on the down-thrown side of the controlling fault favored the flow of eroded material to the east, rather than to the south. On this basis, he opined that the Yates acreage in the east half of Section 12 is more likely to contain reservoir rock that might be drained by the subject well than is the Pride acreage in the southwest quarter.

17. Dr. Boneau, Yates' engineering witness, calculated the probable drainage area of the State M based on production data and log analysis, to be 145 acres. Assuming that the drainage characteristics of the subject well would be otherwise similar to those of the State M, he calculated that 97% of production in the target reservoir from the subject well would

be drawn from Yates acreage if Yates assumptions were correct, and 65% if Pride's assumptions were correct.

Analysis of Legal Issues

18. This case requires an analysis of the effect of the Division's action in approving an APD.

19. Pride filed an APD proposing a well at an orthodox location, and attached thereto a Dedication Plat (C-102) proposing to dedicate thereto a standard unit which was not then dedicated to any other well in the pool. Accordingly, Pride's APD was *prima facie* valid, and the Division properly approved it.

20. The Division, through its district supervisor, subsequently purported to revoke its approval of Pride's APD on the ground that Pride did not own an interest in the drill-site tract.

21. As this Commission observed in Order No. R-11700-B, entered in Cases No. 12731 and 12744, the Division has neither the responsibility nor jurisdiction to determine whether an applicant for a permit to drill has the requisite title to the land in question. Order No. R-11700-B, Finding 27.

22. The Commission further stated in Order No. R-11700-B that an applicant for a permit to drill must have a good faith claim of title. Order R-11700-B, finding 28.

23. Although the Division can and should cancel an APD when it properly determines that no such good faith claim exists, as the Commission determined, based on a District Court judgment, in Order No. R-11700-B, it should not make that determination, which necessarily cannot be made on the face of the APD or from Division records, without first giving the applicant notice and an opportunity for a hearing. Although the Commission doubts that the right conferred by approval of an APD is properly characterized as "property," it nevertheless concludes that such approval confers rights that should not be revoked arbitrarily.

24. In any event, a determination that Pride did not have a good faith claim could not have been made in this case. Here, unlike Cases No. 12731 and 12744, there is no title dispute. It is undisputed that Pride owns a working interest in the unit proposed in its APD, *i.e.*, the west half of Section 12, and that the west half of Section 12 is a standard unit permitted by applicable spacing rules. It is likewise undisputed that, at the time Pride filed its APD, Yates' previously approved APD calling for a north half spacing unit had expired.

25. Again, the Commission said in Order No. R-11700-B:

> An operator may first apply for a permit to drill a well and may thereafter pool (on a voluntary or compulsory basis) separately owned tracts to the well.

> Alternatively, the operator may first pool and later seek a permit to drill. The two are not mutually exclusive, and there is no preferred methodology.

Order R-11700-B, finding 35.

26. The Commission accordingly concludes that an owner who would have a right to drill at its proposed location in the event of a voluntary or compulsory pooling of the unit it proposes to dedicate to the well has the necessary good faith claim of title to permit it to file an APD even though it has not yet filed a pooling application. If an owner uses this right to "tie-up" acreage without proceeding diligently to seek voluntary or compulsory pooling, or if the acreage can more properly be developed by inclusion in a different unit, an aggrieved owner can file an application with the Division to cancel its approval of the APD, which the Division can do after notice and hearing.

27. It follows that Pride's approved APD in this case was improperly revoked, and Yates' subsequent APD was improperly approved. It does not necessarily follow, however, that Pride is entitled to the relief it seeks in this case.

28. As the Commission stated in Order No. R-11700-B:

> An application for a permit to drill serves different objectives than an application for compulsory pooling and the two proceedings should not be confused.

Order No. R-11700-B, finding 33.

29. In Order No. R-11700-B, the Commission ordered cancellation of an APD based on a judicial determination that the party who filed the APD had no title to the subject unit and therefore could not be an operator of a well within that unit. The Commission further ordered approval of an APD subsequently filed by a party whose title the court had approved. However, the Commission deferred the issue of the proper configuration of the unit to be dedicated to the proposed well for determination in a pending compulsory pooling proceeding.

30. Thus the existence of a properly approved APD should not be a basis for prejudging the issues in a compulsory pooling application. If the applicant prevails on its compulsory pooling application and is appointed operator in a compulsory pooling order, it is entitled to approval of an APD in any case. If the compulsory pooling application is denied, the applicant having in this case no other basis for a claim of title to the drill-site tract, cancellation of the APD would be a necessary consequence.

31. Ordinarily, Division precedent would require an owner opposing a compulsory pooling application on the ground that prudent development would counsel the formation of a different unit to file a competing application. However, in this case, compulsory pooling would be unnecessary to form a north half unit, as Yates proposes.

Accordingly, Yates should be permitted to offer evidence in support of its proposal as a defense to Pride's compulsory pooling application.

32. The Commission accordingly concludes that its decision in this case must be based on its evaluation of the technical testimony presented in support of, and against, Pride's compulsory pooling application, irrespective of the circumstances with regard to the approval of the respective APDs.

Analysis of Technical Issues

33. Expert witnesses for both parties concurred that, on the basis of the information presently available, the total quantity of reserves in the Mississippian formation underlying Section 12, or particular quarter sections thereof, cannot practicably be determined.

34. Neither of Yates' witnesses offered any convincing reason for supposing that the east half of Section 12 would be productive in the Mississippian. Dr. Boneau testified that the State M well would have a drainage area of 145 acres, and that the subject well is likely to be only half as good a well, suggesting a drainage radius for the subject well of less than 160 acres. Although Mr. Amiet projected the target reservoir into the northeast quarter of the section, he also testified that porosity would fall off rapidly as the distance from the fault increased, and he conceded that his projection of the alluvial fan that produced the target reservoir to the east depended upon the unproven assumption that the observed contours of the formation corresponded to the contours existing at the time of deposition.

35. If Pride's placement of the controlling fault as bearing north to south, and in close proximity to the subject well, is correct, then its conclusion that the southwest quarter of Section 12 will likely be productive in the Mississippian, and the east half of the section will not be productive, accords with the understanding of both geologists of the nature of this reservoir.

36. Although no good logs of the subject well are available, the Commission concludes that Mr. Pride's interpretation that there is likely a comparable amount of reservoir footage in the subject well to that encountered in the State M well is more convincing, and that interpretation is consistent with the north-south alignment of the controlling fault, and with the conclusion that the southwest quarter of Section 12 is likely to be productive.

37. If the southwest quarter proves to be productive, and the east half of the section does not, as both geologists would predict if the fault actually exists in the north-south orientation, then the establishment of stand up units in this section would violate Pride's correlative rights, because Pride would have to share any production it could extract from the southwest quarter with Yates, even though the Yates acreage would not be contributory. If lay down units are established, and the east half proves to be productive, Yates can recover for itself all of the east half production by drilling on the east-half unit.

38. Yates relies principally on its 3-D seismic to demonstrate that the critical fault is oriented northeast-southwest, and not north-south. Though Mr. Amiet testified that Yates has seismic data that confirms his suggested location of the fault, Yates did not offer any such seismic data in evidence. A trier of fact is entitled to assume that if a party does not offer relevant evidence that is in its possession, such evidence would not have supported that party's position.

39. Though Mr. Amiet testified that he interpreted the seismic data offered in evidence as disproving the existence of a north-south fault in the location suggested by Pride, he conceded that a small fault with a throw of as much as 100 feet might exist that might not be apparent from the seismic data. The existence of a fault with much reduced throw compared to that farther to the north would be consistent with Mr. Pride's testimony that the fault "dies" to the south.

40. The Commission concludes that Pride's geologic interpretation is, on the whole, more convincing that Yates' interpretation.

41. The Commission accordingly concludes that

(a) a compulsory pooled unit should be established consisting of the west half of Section 12, Township 12 South, Range 34 East. NMPM, Lea County, New Mexico, and that such unit should be dedicated to the subject well;

(b) Pride should be designated operator of the subject well and of the unit; and

(c) Yates APD for re-entry of the subject well should be cancelled.

42. The order should provide that any pooled working interest owner in the proposed unit 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 re-entering and drilling the well.

43. Reasonable charges for supervision of unit operations (combined fixed rates) should be fixed at $5,000.00 per month while drilling and $600.00 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"*

44. Yates commenced operations to re-enter the subject well prior to the filing of this application, based on an APD reflecting Division approval.

45. Pride should reimburse Yates for reasonable costs incurred by Yates in connection with such operation.

IT IS THEREFORE ORDERED THAT:

1. Pursuant to the application of Pride, all uncommitted interests, whatever they may be, in the oil and gas from the surface to the base of the Mississippian formation underlying the W/2 of Section 12, Township 12 South, Range 34 East, NMPM, Lea County, New Mexico, are hereby pooled to form a standard 320-acre gas spacing and proration unit (the Unit) for all formations or pools spaced on 320 acres within this vertical extent, which presently include, but are not necessarily limited to, the Undesignated Four Lakes-Mississippian Gas Pool and the Undesignated Four Lakes-Morrow Gas Pool. The Unit shall be dedicated to the subject well, located 1980 feet from the North line and 660 feet from the West line (Unit E) of Section 12.

2. The operator of the Unit shall commence re-entry operations on the subject well on or before December 31, 2004 and shall thereafter continue such operations with due diligence to test the Mississippian formation.

3. In the event the operator does not commence re-entry operations on or before December 31, 2004, this order shall be of no further effect, unless the operator obtains a time extension from the Division Director for good cause.

4. Should the subject well not be completed within 120 days after commencement thereof, this order shall be of no further effect, and the unit created by this order shall terminate, unless the operator obtains a time extension from the Division Director following notice and hearing.

5. Upon final plugging and abandonment of the subject well, the pooled unit created by this Order shall terminate unless this order has been amended to authorize further operations.

6. Applicant is hereby designated the operator of the subject well and of the Unit.

7. 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 re-entering, completing and equipping the subject well ("well costs").

8. 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."

9. Within 30 days after the effective date of this order, Yates shall furnish the Division and Pride an itemized schedule of actual well costs incurred by Yates in conducting re-entry operations on the subject well after August 25, 2003 and prior to the time when Yates received notice of the filing of the original application in this case. If no objection to such actual costs is received by the Division, and the Division has not objected within 45 days following receipt of the schedule, such costs shall be deemed to be the reasonable well costs. If there is an objection to the reasonableness of such costs within the 45-day period, the Division will determine the amount thereof that constitutes reasonable well costs after notice and hearing.

10. If Yates elects to pay in advance its share of costs of the re-entry of the subject well pursuant to this order, Yates may deduct the amount of such actual costs from its share of estimated well costs to be paid pursuant to ordering paragraph 8, but if the Division subsequently determines that any amount of such actual costs does not constitute reasonable well costs, Yates shall, within 60 days after such determination, pay to Pride the amount that such actual costs previously reimbursed to Yates exceed the amount thereof that the Division determines to be reasonable.

11. If Yates elects not to pay in advance its share of costs of the re-entry of the subject well pursuant to this order, Pride shall pay to Yates the amount of such actual costs incurred by Yates within 45 days after the later of (a) receipt of the schedule of such costs as required by ordering paragraph 9 or (b) the expiration of the time provided by ordering paragraph 8 within which Yates could elect to pay its share of well costs in advance, unless Pride files an objection to the reasonableness of such actual costs, in which event Pride shall pay to Yates the amount thereof that the Division determines to be reasonable within 60 days after such determination.

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 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:

(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) are hereby fixed at $5,000.00 per month while drilling and $600.00 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. 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.

18. The operator of the well and Unit shall notify the Division in writing of the subsequent voluntary agreement of all parties subject to the forced pooling provisions of this order.

19. Pride's APD for the State "X" Well No. 1 dated July 10, 2003 is hereby re-instated, and shall continue in effect for one year from the date of this order, unless this order sooner terminates.

20. Yates Petroleum Corporation's APD for the State "X" Well No. 1 dated August 25, 2003 is hereby cancelled *ab initio*.

21. 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 the day and year hereinabove designated.

STATE OF NEW MEXICO
OIL CONSERVATION COMMISSION

MARK E. FESMIRE, P.E., CHAIR

JAMI BAILEY, CPG, MEMBER

FRANK T. CHAVEZ, MEMBER

SEAL

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

IN THE MATTER OF THE HEARING CALLED BY THE OIL CONSERVATION COMMISSION FOR THE PURPOSE OF CONSIDERING:

CASE NO. 13153, *de novo*

APPLICATION OF PRIDE ENERGY COMPANY FOR CANCELLATION OF A DRILLING PERMIT AND REINSTATEMENT OF A DRILLING PERMIT, AN EMERGENCY ORDER HALTING OPERATIONS, AND COMPULSORY POOLING, LEA COUNTY, NEW MEXICO

ORDER NO. R-12108-B

ORDER OF THE OIL CONSERVATION COMMISSION

BY THE COMMISSION:

THIS MATTER came before the Oil Conservation Commission (the Commission) for hearing on October 14, 2004 at Santa Fe, New Mexico on the Application for Rehearing of Yates Petroleum Corporation and the Motion of Yates Petroleum Corporation for a Stay of Commission Order No. R-12108-A and for an Emergency Order, and the Commission, having carefully considered the same, now, on this 14th day of October, 2004,

FINDS:

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

2. This matter previously came before the Commission on August 12, 2004, on the application of Yates Petroleum Corporation (Yates) for *de novo* review, and, on September 9, 2004, the Commission issued Order No. R-12108-A granting the original Application of Pride Energy Company (Pride) for Cancellation of a Drilling Permit and Reinstatement of a Drilling Permit, and Compulsory Pooling.

3. On September 29, 2004, Yates filed a timely motion for rehearing.

4. On October 12, 2004, Yates filed a motion to stay Order R-12108-A "until such time as the Oil Conservation Commission process in this case has been completed."

5. Both parties had notice of the hearing held by the Commission in this case on August 12, 2004, and were present at that hearing through counsel and corporate representatives.

6. Both parties were given a full opportunity to present evidence and argument to the Commission at the September 9 hearing, and each party did, in fact, present extensive testimony.

7. The Motion for Rehearing does not allege that any evidence has been newly discovered, or that any party was precluded from offering evidence it sought to offer at the September 9 hearing.

8. The Commission accordingly concludes that a rehearing of the matters that were the subject of the evidentiary presentations at the September 9 hearing is not necessary.

9. However, the Motion for Rehearing raises an issue concerning the right of Yates to reimbursement for costs incurred in preparation to re-enter the State X Well No. 1 (API No. 30-025-07838) (the subject well) prior to the time that Yates ceased operations to abide the decision of the Oil Conservation Division.

10. Order No. R-12108-A provided that Yates should be allowed reimbursement for expenses it incurred in conducting re-entry operations on the subject well after August 25, 2003 and prior to the time when Yates received notice of the filing of the original application in this case.

11. No evidence was offered at the hearing on August 12, 2004, nor was evidence otherwise before the Commission, of the amount or nature of expenses incurred either within or subsequent to the time period for which reimbursement is allowed by Order R-12108-A.

12. The Commission accordingly concludes that a rehearing should be granted with respect to Order No. R-12108-A limited to the issues of the expenses for which Yates should be allowed reimbursement and the correction of clerical errors in Order R-12108-A.

13. Because these issues do not affect the right of Pride to operate the subject well, Yates' Motion for Stay should be denied.

IT IS THEREFORE ORDERED THAT:

1. Yates' Motion for Rehearing in this case is granted to the extent herein provided.

2. The issues for consideration upon rehearing shall be limited to the determination of costs for which Yates shall be allowed reimbursement.

3. This case will be set on the docket of the Commission for a new hearing, at which Yates may offer evidence concerning the expenses it incurred for which it seeks reimbursement that were not incurred within the time period provided in Order No. R-12108-A, and both parties may present evidence and argument concerning the propriety of allowing Yates reimbursement for such expenses.

4. The Motion of Yates Petroleum Corporation for a Stay of Commission Order No. R-12108-A and for an Emergency Order is denied.

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

STATE OF NEW MEXICO
OIL CONSERVATION COMMISSION

MARK E. FESMIRE, P.E., CHAIR

JAMI BAILEY, CPG, MEMBER

FRANK T. CHAVEZ, MEMBER

SEAL

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

IN THE MATTER OF THE HEARING CALLED BY THE OIL CONSERVATION COMMISSION FOR THE PURPOSE OF CONSIDERING:

CASE NO. 13153, Rehearing

APPLICATION OF PRIDE ENERGY COMPANY FOR CANCELLATION OF A DRILLING PERMIT AND REINSTATEMENT OF A DRILLING PERMIT, AN EMERGENCY ORDER HALTING OPERATIONS, AND COMPULSORY POOLING, LEA COUNTY, NEW MEXICO

ORDER NO. R-12108-C

ORDER OF THE OIL CONSERVATION COMMISSION

BY THE COMMISSION;

THIS MATTER originally came before the Oil Conservation Commission (the Commission) on August 12, 2004, and the Commission entered Order No. R12108-A disposing of this application on September 10, 2004. Pursuant to the application of Yates Petroleum Corporation for rehearing, and the order of the Commission granting same (Order No. R-12108-B, issued on October 14. 2004), this matter came again before the Commission for rehearing on November 10, 2004 at Santa Fe, New Mexico, and the Commission, having heard the evidence and arguments of counsel and carefully considered the same, now, on this 9th day of December, 2004,

FINDS:

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

2. In the original application in this case, Pride Energy Company (Pride) sought an order canceling a permit issued to Yates Petroleum Corporation (Yates) to re-enter the

abandoned State X Well No. 1 (API No. 30-025-01838) (the subject well), located 1980 feet from the North line and 660 feet from the West line (Unit E) of Section 12, Township 12 South, Range 34 East. NMPM, Lea County, New Mexico. Pride also sought reinstatement of a drilling permit previously issued to it to re-enter the same well, and an emergency order preventing Yates from conducting any operations on the well.

3. Pride additionally sought an order pooling all uncommitted mineral interests underlying the W/2 of Section 12, Township 12 South, Range 34 East, NMPM, Lea County, New Mexico, from the surface to the base of the Mississippian formation, forming a standard 320-acre gas spacing and proration unit (the Unit) for all formations or pools spaced on 320 acres within this vertical extent, which presently include, but are not necessarily limited to, the undesignated Four Lakes-Mississippian Gas Pool and the undesignated Four Lakes-Morrow Gas Pool, such unit to be dedicated to the well.

4. Both Yates and Pride appeared at the original Commission hearing on August 12, 2004 through counsel and presented land and technical testimony. Pride presented the testimony of John W. Pride, a petroleum landman and one of the principals of Pride, and Jeff Ellard, a geologist employed by Pride. Yates presented the testimony of Charles E. Moran, a landman employed by Yates, John Amiet, a geologist employed by Yates, and David F. Boneau, a petroleum engineer employed by Yates.

Undisputed Facts

5. Based on the statements of counsel and testimony offered by the parties, the Commission concludes that the following facts pertinent to this case are undisputed:

(a) Yates is the owner of the entire working interest in the north half and southeast quarter of Section 12, Township 12 South, Range 34 East.

(b) Pride is the owner of the entire working interest in the southwest quarter of Section 12.

(c) The subject well is located in the northwest quarter of Section 12 on land leased exclusively to Yates.

(d) Pride is the operator of the State M Well No. 1 (API No. 30-025-20689) (the State M), located 660 feet from the south and west lines of Section 1, Township 12 South, Range 34 East, which well is completed in, and producing from, the Mississippian formation. That well is dedicated to a spacing unit comprising the west half of Section 1, pursuant to a voluntary unit agreement to which Pride and Yates are both parties.

(e) On May 24, 2001 Yates filed an Application for Permit to Drill (APD) to re-enter the subject well, which it designated the "Limbaugh AYO State Well No. 1", and to which it proposed to dedicate a spacing unit comprising the north half of Section 12. The Division approved that APD on May 25, 2001.

(f) On April 15, 2002, in anticipation of the forthcoming expiration of its APD, Yates filed a sundry notice to extend its APD for an additional year, until May 25, 2003. The Division approved the requested extension on April 18, 2002.

(g) On May 25, 2003, Yates' APD to re-enter the subject well expired.

(h) On July 10, 2003, Pride filed an APD to re-enter the subject well under the name "State X Well No. 1," to which it proposed to dedicate a. spacing unit comprising the west half of Section 12, including the southwest quarter, which is leased to Pride.

(i) Pride's APD was approved by the Division on July 16, 2003.

(j) On August 25, 2003, Yates filed a new APD to re-enter the subject well, again designating the well as the "Limbaugh AYO State No. 1" and again proposing to dedicate to the well a spacing unit comprising the north half of Section 12.

(k) On August 26, 2003, the district supervisor of OCD District 1, approved Yates' APD for the subject well, and prepared a letter to Pride canceling Pride's APD.

(l) Yates has stipulated that it will undertake no operations with respect to the subject well pending the Commission's decision, thereby mooting Pride's request for an emergency order prohibiting such operations.

Technical Evidence

6. Although the history and land ownership are undisputed, as indicated in the foregoing findings, there exists controversy concerning the technical aspects of the case.

7. At the August 12, 2004 Commission hearing, the parties presented the following technical evidence:

(a) Mr. Ellard, Pride's geologist, testified that the objective in re-entering the subject well would be the Austin cycle of the upper Mississippian (the target reservoir), in which production was encountered in the State M, to the north of the subject well.

(b) Mr. Ellard further testified that the target reservoir was formed by shedding of fragmented rock from a raised fault block produced by faults lying to the west of these two wells. In wells farther to the south and east, away from the faulting, where the rock was not fragmented, the formation is present, but with insufficient porosity to be productive.

(c) Mr. Ellard opined that producible hydrocarbons would most likely be located closest to the fault because, of the material shed from the upthrown side of the fault, that material composed of larger particles, and therefore characterized by greater porosity and permeability, would be deposited in close proximity to the fault.

(d) Mr. Ellard placed the fault that created the target reservoir on a bearing more or less north to south and located a short distance to the west of the State M and the subject well, generally along and close to the section line between Section 12 and the adjacent Section 11. On this basis, he opined that the subject well would more likely drain producible hydrocarbons from the quarter section lying south of the subject well (the southwest quarter of Section 12), than from the quarter section lying east of the subject well (the northeast quarter of Section 12).

(e) Mr. Ellard testified that it is not possible to determine with any degree of accuracy the extent of the target reservoir with the information presently available. However, he opined, based on comparison of the old log of the subject well with the old log of the State M, that the subject well would likely encounter a comparable thickness of pay in the target reservoir (25 feet as compared to 30 feet in the State M).

(f) Mr. Amiet, Yates' geologist, agreed generally with Mr. Ellard's interpretation of the nature of the target reservoir and the mechanism of deposition, including the assessment that the extent of the target reservoir could not be determined with available information, but disagreed with Mr. Ellard's placement of the fault that produced the up-thrown block from which the reservoir material was presumably eroded.

(g) Mr. Amiet testified that 3D seismic run along a west-to-east bearing close to the location of the subject well, and which was admitted in evidence, demonstrated that no significant fault down-thrown to the east existed in the westward proximity of the subject well. He opined that the fault that controls the location of the target reservoir runs to the north of the State M and trends northeast to southwest. Accordingly, he concluded that the subject well is more distant from the fault than is the State M, and the Pride acreage in the southwest quarter of Section 12 is yet more distant.

(h) Mr. Amiet interpreted the logs from the subject well to show no more than 10 feet of reservoir in the target formation (as compared to 30 feet in the Ml), confirming his conclusion that the subject well is more distant from the fault.

(i) Mr. Amiet testified that Yates had other 3-D seismic runs that tended to confirm his placement of the controlling fault, but Yates did not offer this other seismic information in evidence.

(j) Mr. Amiet further testified that the prevailing contours on the down-thrown side of the controlling fault favored the flow of eroded material to the east, rather than to the south. On this basis, he opined that the Yates acreage in the east

half of Section 12 is more likely to contain reservoir rock that might be drained by the subject well than is the Pride acreage in the southwest quarter.

(k) Dr. Boneau, Yates' engineering witness, calculated the probable drainage area of the State M based on production data and log analysis, to be 145 acres. Assuming that the drainage characteristics of the subject well would be otherwise similar to those of the State M, he calculated that 97% of production in the target reservoir from the subject well would be drawn from Yates acreage if Yates assumptions were correct, and 65% if Pride's assumptions were correct.

Analysis of Legal Issues

8. Based on the evidence and arguments at the August 12, 2004 hearing, the Commission finds and concludes concerning the legal issues presented as follows:

(a) This case requires an analysis of the effect of the Division's action in approving an APD.

(b) Pride filed an APD proposing a well at an orthodox location, and attached thereto a Dedication Plat (C-102) proposing to dedicate thereto a standard unit which was not then dedicated to any other well in the pool. Accordingly, Pride's APD was *prima facie* valid, and the Division properly approved it.

(c) The Division, through its district supervisor, subsequently purported to revoke its approval of Pride's APD on the ground that Pride did not own an interest in the drill-site tract.

(d) As this Commission observed in Order No. R-11700-B, entered in Cases No. 12731 and 12744, the Division has neither the responsibility nor jurisdiction to determine whether an applicant for a permit to drill has the requisite title to the land in question. Order No. R-11700-B, Finding 27.

(e) The Commission further stated in Order No. R-11700-B that an applicant for a permit to drill must have a good faith claim of title. Order R-11700-B, finding 28.

(f) Although the Division can and should cancel an APD when it properly determines that no such good faith claim exists (as the Commission determined, based on a District Court judgment, in Order No. R-11700-B), it should not make that determination, which necessarily cannot be made on the face of the APD or from Division records, without first giving the applicant notice and an opportunity for a hearing. Although the Commission doubts that the right conferred by approval of an APD is properly characterized as "property," it nevertheless concludes that such approval confers rights that should not be revoked arbitrarily.

(g) In any event, a determination that Pride did not have a good faith claim could not have been made in this case. Here, unlike Cases No. 12731 and 12744, there is

no title dispute. It is undisputed that Pride owns a working interest in the unit proposed in its APD, *i.e.*, the west half of Section 12, and that the west half of Section 12 is a standard unit permitted by applicable spacing rules. It is likewise undisputed that, at the time Pride filed its APD, Yates' previously approved APD calling for a north half spacing unit had expired.

(h) Again, the Commission said in Order No. R-11700-B:

> An operator may first apply for a permit to drill a well and may thereafter pool (on a voluntary or compulsory basis) separately owned tracts to the well. Alternatively, the operator may first pool and later seek a permit to drill. The two are not mutually exclusive, and there is no preferred methodology.
>
> Order R-11700-B, finding 35.

(i) The Commission accordingly concludes that an owner who would have a right to drill at its proposed location in the event of a voluntary or compulsory pooling of the unit it proposes to dedicate to the well has the necessary good faith claim of title to permit it to file an APD even though it has not yet filed a pooling application. If an owner uses this right to "tie-up" acreage without proceeding diligently to seek voluntary or compulsory pooling, or if the acreage can more properly be developed by inclusion in a different unit, an aggrieved owner can file an application with the Division to cancel its approval of the APD, which the Division can do after notice and hearing.

(j) It follows that Pride's approved APD in this case was improperly revoked, and Yates' subsequent APD was improperly approved. It does not necessarily follow, however, that Pride is entitled to the relief it seeks in this case.

(k) As the Commission stated in Order No. R-11700-B:

> An application for a permit to drill serves different objectives than an application for compulsory pooling and the two proceedings should not be confused.
>
> Order No. R-11700-B, finding 33.

(l) In Order No. R-11700-B, the Commission ordered cancellation of an APD based on a judicial determination that the party who filed the APD had no title to the subject unit and therefore could not be an operator of a well within that unit. The Commission further ordered approval of an APD subsequently filed by a party whose title the court had approved. However, the Commission deferred the issue of the proper configuration of the unit to be dedicated to the proposed well for determination in a pending compulsory pooling proceeding.

(m) Thus the existence of a properly approved APD should not be a basis for prejudging the issues in a compulsory pooling application. If the applicant prevails on its compulsory pooling application and is appointed operator in a compulsory pooling order, it is entitled to approval of an APD in any case. If the compulsory pooling application is denied, the applicant having in this case no other basis for a claim of title to the drill-site tract, cancellation of the APD would be a necessary consequence.

(n) Ordinarily, Division precedent would require an owner opposing a compulsory pooling application on the ground that prudent development would counsel the formation of a different unit to file a competing application. However, in this case, compulsory pooling would be unnecessary to form a north half unit, as Yates proposes. Accordingly, Yates should be permitted to offer evidence in support of its proposal as a defense to Pride's compulsory pooling application.

(o) The Commission accordingly concludes that its decision in this case must be based on its evaluation of the technical testimony presented in support of, and against, Pride's compulsory pooling application, irrespective of the circumstances with regard to the approval of the respective APDs.

Analysis of Technical Issues

9. Based on the evidence and arguments at the August 12, 2004 hearing, the Commission finds and concludes concerning the technical issues presented as follows:

(a) Expert witnesses for both parties concurred that, on the basis of the information presently available, the total quantity of reserves in the Mississippian formation underlying Section 12, or particular quarter sections thereof, cannot practicably be determined.

(b) None of Yates' witnesses offered any convincing reason for supposing that the east half of Section 12 would be productive in the Mississippian. Dr. Boneau testified that the State M well would have a drainage area of 145 acres, and that the subject well is likely to be only half as good a well, suggesting a drainage radius for the subject well of less than 160 acres. Although Mr. Amiet projected the target reservoir into the northeast quarter of the section, he also testified that porosity would fall off rapidly as the distance from the fault increased, and he conceded that his projection of the alluvial fan that produced the target reservoir to the east depended upon the unproven assumption that the observed contours of the formation corresponded to the contours existing at the time of deposition.

(c) If Pride's placement of the controlling fault as bearing north to south, and in close proximity to the subject well, is correct, then its conclusion that the southwest quarter of Section 12 will likely be productive in the Mississippian, and the east half of the section will not be productive, accords with the understanding of both geologists of the nature of this reservoir.

(d) Although no good logs of the subject well are available, the Commission concludes that Mr. Pride's interpretation that there is likely a comparable amount of reservoir footage in the subject well to that encountered in the State M well is more convincing, and that interpretation is consistent with the north-south alignment of the controlling fault, and with the conclusion that the southwest quarter of Section 12 is likely to be productive.

(e) Both geologists predicted that the east half of the section is less likely to be productive from the target reservoir than the west half. The southwest quarter, however, is quite likely productive if the controlling fault actually exists in the north-south orientation as **Pride's** evidence suggests that it does.

(f) If the southwest quarter proves to be productive, and the east half of the section does not, then the establishment of lay down units in this section would violate **Pride's** correlative rights. If Pride drilled a well in the southwest quarter, such well would have to be included in a south-half unit, and Yates would be entitled to one-half of the production therefrom based on its ownership of the unproductive southeast quarter. If, on the other hand stand up units are established, and the east half proves to be productive, Yates can recover for itself all of the east half production by drilling on the east-half unit.

(g) Yates relies principally on its 3-D seismic to demonstrate that the critical fault is oriented northeast-southwest, and not north-south. Though Mr. Amiet testified that Yates has seismic data that confirms his suggested location of the fault, Yates did not offer any such seismic data in evidence.

(h) Though Mr. Amiet testified that he interpreted the seismic data offered in evidence as disproving the existence of a north-south fault in the location suggested by Pride, he conceded that a small fault with a throw of as much as 100 feet might exist that might not be apparent from the seismic data. The existence of a fault with much reduced throw compared to that farther to the north would be consistent with Mr. Pride's testimony that the fault "dies" to the south.

(i) The Commission concludes that Pride's geologic interpretation is, on the whole, more convincing that **Yates'** interpretation.

10. The Commission accordingly concludes that:

(a) A compulsory-pooled unit should be established consisting of the west half of Section 12, Township 12 South, Range 34 East. NMPM, Lea County, New Mexico, and that such unit should be dedicated to the subject well;

(b) Pride should be designated operator of the subject well and of the unit.

(c) Yates APD for re-entry of the subject well should be cancelled.

(d) The order should provide that any pooled working interest owner in the proposed unit 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 re-entering and re-completing the well.

(e) Reasonable charges for supervision of unit operations (combined fixed rates) should be fixed at $5,000.00 per month while drilling and $600.00 per month while producing, provided that these rates should be adjusted annually pursuant to Section III.1.A.3. of the COP AS form titled *"Accounting Procedure-Joint Operations."*

(f) Yates commenced operations to re-enter the subject well prior to the filing of this application, based on an APD reflecting Division approval.

(g) Pride should reimburse Yates for reasonable costs incurred by Yates in connection with such operation.

11. The Commission entered Order No. R-12108-A on September 9, 2004 granting the application of Pride Energy Company but authorizing Yates to recover the actual well costs incurred by Yates in conducting re-entry operations on the subject well after August 25, 2003 and "prior to the time when Yates received notice of the filing of the original application in this case".

12. Yates filed its Application for Rehearing in this case on September 29, 2004 in which it requested a new hearing on, among other issues, the portion of Order No. R-12108-A that limited Yates' recovery of costs to those costs incurred prior to the time it received notice of Pride's original application in this case.

13. On October 14, 2004, the Commission entered Order No. R-12108-B that granted Yates' Application for Rehearing but limited the issues for consideration on rehearing to the determination of costs for which Yates shall be allowed reimbursement.

14. On NovemberlO, 2004, this case came on for re-hearing before the Commission on the issue of costs for which Yates shall be allowed reimbursement.

15. Yates appeared at the hearing through counsel and presented the testimony of Charles E. Moran, a landman employed by Yates and Tom Wier, an accountant employed by Yates. Pride appeared through counsel but did not present testimony.

16. Mr. Moran testified that Yates had commenced operations on the subject well in August 2003, and that these operations had continued until Yates voluntarily stopped operations pending a decision of the Division in this case. Mr. Moran further testified that, although Pride had filed an application seeking an emergency order directing Yates to cease operations on this well, the Division had deferred action on Pride's application and found, on September 12, 2003, that "Yates should not be required to cease all re-entry operations of the State "X" Well No. 1." Mr. Moran requested that Yates be authorized to recover the actual

costs it incurred in the re-entry of the subject well prior to the time it voluntarily ceased operations on the well or October 7, 2003.

17. Mr. Moran also testified that Yates had complied with the provisions of ordering Paragraph 9 of Order No. R-12108-A by providing a schedule of all actual well costs it had incurred in conducting re-entry operations on the well by letter dated October 8, 2004, that it had received an AFE for the well from Pride by letter dated September 14, 2004; and, to be certain that it was not in a non-consent position under Commission Order No. R-12108-A, on October 13, 2004, Yates had paid to Pride its share of these AFE costs.

18. Mr. Wier reviewed the schedule of well costs submitted to Pride and the Commission on October 8, 2004, identified items that had occurred after October 7, 2003 and provided supporting information for the costs incurred prior to that date.

19. Pride requested that it be allowed time to review and object to the costs on the schedule provided by Yates and the supporting information submitted at the hearing.

20. Yates should be reimbursed for all reasonable costs incurred through October 7, 2003 in furtherance of the re-entry of the subject well, and the time for objections to those costs should be extended through December 31, 2004.

IT IS THEREFORE ORDERED THAT:

1. Pursuant to the application of Pride, all uncommitted interests, whatever they may be, in the oil and gas from the surface to the base of the Mississippian formation underlying the W/2 of Section 12, Township 12 South, Range 34 East, NMPM, Lea County, New Mexico, are hereby pooled to form a standard 320-acre gas spacing and proration unit (the Unit) for all formations or pools spaced on 320 acres within this vertical extent, which presently include, but are not necessarily limited to, the Undesignated Four Lakes-Mississippian Gas Pool and the Undesignated Four Lakes-Morrow Gas Pool. The Unit shall be dedicated to the subject well, located 1980 feet from the North line and 660 feet from the West line (Unit E) of Section 12.

2. The operator of the Unit shall commence re-entry operations on the subject well within 90 days after issuance of this order, and shall thereafter continue such operations with due diligence to test the Mississippian formation. If this order is suspended pending any further appeals, the ninety-day period provided in this paragraph shall be tolled during the time of such suspension.

3. In the event the operator does not commence re-entry operations within the time provided in ordering paragraph 2, this order shall be of no further effect, unless the operator obtains a time extension from the Division Director for good cause.

4. Should the subject well not be completed within 120 days after resumption of re-entry operations pursuant to this order, then this order shall be of no further effect, and the

unit created by this order shall terminate, unless the operator obtains a time extension from the Division Director following notice and hearing.

5. Upon final plugging and abandonment of the subject well, the pooled unit created by this Order shall terminate unless this order has been amended to authorize further operations.

6. Pride is hereby designated the operator of the subject well and of the Unit.

7. 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 re-entering, completing and equipping the subject well ("well costs").

8. 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 and charges for supervision but shall not be liable for risk charges authorized by paragraph 14 of this order. 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."

9. Within 5 days after the issuance of this order, Yates shall furnish the Division and Pride an itemized schedule of actual well costs incurred by Yates in conducting re-entry operations on the subject well after August 25, 2003 and prior to October 7, 2004, the time when Yates voluntarily ceased operations on the subject well. If no objection to such actual costs is received by the Division, and the Division has not objected on or before December 31, 2004, such costs shall be deemed to be the reasonable well costs. If there is an objection to the reasonableness of such costs within the time allowed by this order, the Division will determine the amount thereof that constitutes reasonable well costs after notice and hearing.

10. If Yates elects to pay in advance its share of costs of the re-entry of the subject well pursuant to this order, Yates may deduct the amount of such actual costs from its share of estimated well costs to be paid pursuant to ordering paragraph 8. If the amount to be paid by Yates pursuant to this provision is less than the amount paid by Yates to Pride at the time of its election pursuant to Order No. R-12108-A, Pride shall refund such excess to Yates within 45 days after receiving notice of Yates' election pursuant to this Order No. R-12108-C. If the Division subsequently determines that any amount of actual costs for which Yates claims reimbursement does not constitute reasonable well costs, Yates shall, within 60 days after such determination, pay to Pride the amount that such actual costs previously reimbursed to Yates exceed the amount thereof that the Division determines to be reasonable.

11. If Yates elects not to pay in advance its share of costs of the re-entry of the subject well pursuant to this order, Pride shall refund all amounts paid by Yates at the time of its election pursuant to Order No. **R-12108-A**, and shall pay to Yates the amount of actual costs incurred by Yates, within 45 days after the later of (a) receipt of the schedule of such costs as required by ordering paragraph 9 or (b) the expiration of the time provided by ordering paragraph 8 within which Yates could elect to pay its share of well costs in advance. If, however, Pride files an objection to the reasonableness of such actual costs, Pride shall, in lieu of paying actual costs claimed by Yates at the time provided in the preceding sentence, pay to Yates the amount thereof that the Division determines to be reasonable within 60 days after such determination.

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 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:

(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) are hereby fixed at $5,000.00 per month while drilling and $600.00 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. 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.

18. The operator of the well and Unit shall notify the Division in writing of the subsequent voluntary agreement of all parties subject to the forced pooling provisions of this order.

19. Pride's APD for the State "X" Well No. 1 dated July 10, 2003 is hereby re-instated, and shall continue in effect for one year from the date of this order, unless this order sooner terminates.

20. Yates Petroleum Corporation's APD for the State "X" Well No. 1 dated August 25, 2003 is hereby cancelled *ab initio*.

21. Order No. R-12108-A is hereby rescinded in its entirety, and this Order No. R-12108-C is substituted therefor.

22. 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 the day and year hereinabove designated.

STATE OF NEW MEXICO
OIL CONSERVATION COMMISSION

MARK E. FESMIRE, P.E., CHAIR

JAMI BAILEY, CPG, MEMBER

FRANK T. CHAVEZ, MEMBER

SEAL

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

IN THE MATTER OF THE HEARING CALLED BY THE OIL CONSERVATION COMMISSION FOR THE PURPOSE OF CONSIDERING:

CASE NO. 13153, Rehearing

APPLICATION OF PRIDE ENERGY COMPANY FOR CANCELLATION OF A DRILLING PERMIT AND REINSTATEMENT OF A DRILLING PERMIT, AN EMERGENCY ORDER HALTING OPERATIONS, AND COMPULSORY POOLING, LEA COUNTY, NEW MEXICO

ORDER NO. R-12108-D

ORDER OF THE OIL CONSERVATION COMMISSION

BY THE COMMISSION:

THIS MATTER came before the Oil Conservation Commission (the Commission) on this 10th day of February, 2005, at Santa Fe, New Mexico, on Pride Energy Company's Motion for Stay of Commission Order (the motion), and the Commission, having heard arguments of counsel and carefully considered the same, now

FINDS:

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

2. In the original application in this case, Pride Energy Company (Pride) sought an order canceling a permit issued to Yates Petroleum Corporation (Yates) to re-enter the abandoned State X Well No. 1 (API No. 30-025-01838) (the subject well), located 1980 feet from the North line and 660 feet from the West line (Unit E) of Section 12, Township 12 South, Range 34 East, NMPM, Lea County, New Mexico. Pride also sought reinstatement of

a drilling permit previously issued to it to re-enter the same well, and an emergency order preventing Yates from conducting any operations on the well.

3. Pride additionally sought an order pooling all uncommitted mineral interests underlying the W/2 of Section 12, Township 12 South, Range 34 East, NMPM, Lea County, New Mexico, from the surface to the base of the Mississippian formation, forming a standard 320-acre gas spacing and proration unit (the Unit) for all formations or pools spaced on 320 acres within this vertical extent, which presently include, but are not necessarily limited to, the undesignated Four Lakes-Mississippian Gas Pool and the undesignated Four Lakes-Morrow Gas Pool, such unit to be dedicated to the well.

4. On December 9, 2004, the Commission entered Order No. R-12108-C, *inter alia*, granting Pride's application for compulsory pooling, providing that the pooled unit formed by the order be dedicated to the subject well, appointing Pride as operator of the unit and the subject well and directing Pride to commence re-entry operations on the subject well within ninety (90) days after issuance of the order.

5. On December 27, 2004, respondent, Yates Petroleum Corporation (Yates) filed an application for rehearing. The Commission took no action on the application for rehearing, and the same was deemed overruled on January 10, 2005. Yates filed notice of appeal of the Commission's Order in the District Court of Santa Fe County.

6. On February 4, 2005, Pride filed the motion with the Commission seeking a stay of the requirement of Order No. R-12108-C that it commence re-entry operations on the subject well no later than March 9, 2005.

7. Yates filed a written response to the motion and appeared at the hearing through counsel. Yates argued that, in view of its filing of a notice of appeal in District Court, the Commission has no jurisdiction to consider a motion to stay its order so long as the appeal of that order is pending in the courts.

8. The jurisdiction of an administrative agency to consider a request to stay its order during the pendency of an appeal therefrom was recognized by the New Mexico Court of Appeals in *Tenneco Oil Company v. New Mexico Water Quality Control Commission,* 105 N.M. 708, 736 P.2d 986 (1986). Although the New Mexico Supreme Court has subsequently enacted Rule 1-074 expressly conferring jurisdiction upon the District Courts to entertain motions to stay administrative orders, Rule 1-074 does not provide that the jurisdiction of the district court over such motions is exclusive. In view of the fact that the Court of Appeals, in *Tenneco, supra,* opined that it had inherent authority to grant such stays, but that its power was not exclusive, the Commission concludes that the jurisdiction of the District Court over such matters is not exclusive, and the Commission has jurisdiction to consider the motion.

9. Pride did not offer any evidence in support of the motion. In the motion and at the hearing Pride argued that the order would require it to incur substantial expense in

operation of a well in which it would own no interest if the District Court were to reverse the Commission's order.

10. Pride did not offer any evidence that Yates or any of the other respondents would be unable to respond in damages should Pride incur monetary injury as it claimed.

11. The Commission accordingly concludes that:

a. Pride has made no showing of good cause under the terms of Order No. R-12108-C why the time provided in said order for the commencement of re-entry operations should be extended;

b. Pride has not shown that it will incur any irreparable harm if a stay is not granted.

12. Counsel for Yates stated that Yates' lease will expire on June 30, 2005. Pride did not dispute this assertion.

13. The Commission accordingly concludes that:

a. Substantial harm would probably result to Yates if a stay were granted, and

b. A balancing of the parties respective interests requires denial of a stay, since Pride would have a remedy for harm it may incur if a stay is not granted; whereas Yates would not have a remedy for harm it may incur if a stay is granted.

14. There is not evidence that granting of the motion is necessary for the prevention of waste or protection of correlative rights.

IT IS THEREFORE ORDERED THAT:

1. Pride's Motion for Stay of Commission Order No. R-12108-C is hereby denied.

2. 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 the day and year hereinabove designated.

STATE OF NEW MEXICO
OIL CONSERVATION COMMISSION

MARK E. FESMIRE, P.E., CHAIR

JAMI BAILEY, CPG, MEMBER

FRANK T. CHAVEZ, MEMBER

SEAL

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. 13531
ORDER NO. R-12547

APPLICATION OF YATES PETROLEUM CORPORATION FOR AN ORDER (1) DIRECTING PRIDE ENERGY COMPANY TO REIMBURSE YATES FOR THE WELL COSTS INCURRED BY YATES IN ITS ATTEMPT TO RE-ENTER THE STATE "X" WELL NO. 1 (API NO. 30-025-01838) LOCATED IN SECTION 12, TOWNSHIP 12 SOUTH, RANGE 34 EAST, NMPM, PRIOR TO THE TIME PRIDE ENERGY COMPANY ASSUMED OPERATIONS OF THE WELL; (2) DIRECTING PRIDE ENERGY COMPANY TO ACCOUNT FOR AND PAY ALL SUMS IT IS NOW IMPROPERLY HOLDING PURSUANT TO EXPIRED ORDERS OF THE DIVISION AND COMMISSION; AND, (3) REQUIRING PRIDE ENERGY COMPANY TO PLUG AND ABANDON THE STATE "X" WELL NO. 1, LEA COUNTY, NEW MEXICO.

ORDER OF THE DIVISION

BY THE DIVISION:

This case came on for hearing at 8:15 a.m. on January 5, 2006, at Santa Fe, New Mexico, before Examiner David R. Catanach.

NOW, on this 8th day of May, 2006, the Division Director, having considered the testimony, the record, and the recommendations of the Examiner,

FINDS THAT:

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

(2) The applicant, Yates Petroleum Corporation ("Yates"), seeks: (1) an order directing Pride Energy Company ("Pride") to reimburse Yates for the well costs Yates incurred while conducting re-entry operations on the State "X" Well No. 1 (API No. 30-025-01838) located 1980 feet from the North line and 660 feet from the West line (Unit E) of Section 12, Township 12 South, Range 34 East, NMPM, Lea County, New Mexico, prior to the time Pride assumed operations of the well; (2) an order directing Pride to

account and refund to Yates all of the portion of the estimated share of well costs for the State "X" Well No. 1 now improperly held by Pride pursuant to an order of the Oil Conservation Commission ("Commission"); and (3) an order directing Pride to plug and abandon the State "X" Well No. 1.

(3) Pride appeared at the hearing through legal counsel in opposition to the application.

(4) At the hearing, Yates requested that the portion of its application seeking an order directing Pride to plug and abandon the State "X" Well No. 1 be dismissed.

(5) A brief chronological summary of the events leading up to this case is described as follows:

On September 5, 2003, Yates moved a rig onto and commenced re-entry operations on the plugged and abandoned State "X" Well No. 1 in order to test the Mississippian formation. The N/2 of Section 12 was to be dedicated to the well forming a standard 320-acre spacing and proration unit;

On September 10, 2003, Pride filed an application with the Division to: i) re-instate its drilling permit to re-enter the State "X" Well No. 1; ii) cancel Yates' drilling permit to re-enter the State "X" Well No. 1; iii) halt Yates' re-entry operations on the State "X" Well No. 1; and iv) compulsory pool all mineral interests in the W/2 of Section 12, this 320-acre spacing and proration unit to be dedicated to the State "X" Well No. 1. This application was assigned Case No. 13153;

Prior to the hearing in Case No. 13153, which was heard by the Division on October 23, 2003, Yates voluntarily moved off the State "X" Well No. 1;

On March 2, 2004, Order No. R-12108 was issued in Case No. 13153. This order approved the application of Pride, thereby effectively awarding Pride the operatorship of the State "X" Well No. 1. Pursuant to the provisions of the order, Pride was required to commence re-entry operations on the State "X" Well No. 1 by June 1, 2004;

On September 9, 2004, Order No. R-12108-A was issued by the Commission in *de novo* Case No. 13153. This order awarded Pride the operatorship of the State "X" Well No. 1 and required Pride to commence re-entry operations on the State "X" Well No. 1 by December 31, 2004. The order also required that Yates, within 30 days from the date of the order, provide Pride an itemized schedule of actual well costs incurred by Yates in conducting re-entry operations on the State "X" Well No. 1 after August 25, 2003 and prior to the time Yates received notice of the filing of the original application in this case;

On October 14, 2004, Order No. R-12108-B was issued by the Commission upon the application of Yates for rehearing *de novo* Case No. 13153. This order granted Yates' request for rehearing to the extent that the issues for consideration upon rehearing shall

be limited to the determination of costs for which Yates shall be allowed reimbursement from Pride;

On December 9, 2004, Order No. R-12108-C was issued in the rehearing of *denovo* Case No. 13153. This order again awarded Pride operatorship of the State "X" Well No. 1 and; i) required Pride to commence re-entry operations on the State "X" Well No. 1 within 90 days from the date of the order; ii) required Yates, within 5 days from the date of the order, to provide Pride and the Division an itemized schedule of actual well costs incurred by Yates in conducting re-entry operations on the State "X" Well No. 1 during the period after August 25, 2003 and prior to October 7, 2004; and iii) rescinded Division Order No. 12108-A;

On February 10, 2005, Order No. R-12108-D was issued upon Pride's Motion for Stay of Order No. R-12108-C. This order denied Pride's Motion to Stay Order No. R-12108-C;

On February 15, 2005, Pride commenced re-entry operations on the State "X" Well No. 1; and

On March 27, 2005, Pride ceased re-entry operations on the State "X" Well No. 1.

(6) The evidence presented demonstrates that Pride complied with Order No. R-12108-C by commencing re-entry operations on the State "X" Well No. 1 in a timely manner. The evidence further shows that Pride ceased re-entry operations on March 27, 2005, and that the State "X" Well No, 1 has not yet been completed. Order No. R-12108-C provides that:

"(4) Should the subject well not be completed within 120 days after resumption of re-entry operations pursuant to this order, then this order shall be of no further effect, and the unit created by this order shall terminate, unless the operator obtains a time extension from the Division Director following notice and hearing."

Issue No. 1: **Well Costs Incurred by Yates in Its Attempt to Re-enter the State "X" Well No, 1 and Its Request for Reimbursement from Pride.**

(7) Order No. R-12108-C provided that:

"(9) Within 5 days after the issuance of this order, Yates shall furnish the Division and Pride an itemized schedule of actual well costs incurred by Yates in conducting re-entry operations on the subject well after August 25, 2003 and prior to October 7, 2004, the time when Yates voluntarily ceased operations on the subject well. If no objection to such actual costs is received by the Division, and the Division has not objected on or before December 31, 2004, such costs shall be deemed to be the reasonable well costs. If there is objection to the reasonableness of such costs within the time allowed by this order, the Division will determine the amount thereof that constitutes reasonable well costs after notice and hearing."

(8) The evidence and testimony presented at the hearing relating to the well costs incurred by Yates in its re-entry attempt on the State "X" Well No. 1 is summarized as follows:

a. Yates first provided Pride its schedule of well costs to re-enter the State "X" Well No. 1 on October 13, 2004. There is no evidence to demonstrate whether or not Yates provided Pride any other well cost schedule subsequent to that time;

b. Yates' well costs to re-enter the State "X" Well No. 1 after August 25, 2003 and prior to October 7, 2004 are $84,391.58; and

c, By letter dated September 30, 2005, Pride notified Yates that it objected to certain of Yates' well costs in the amount of $25,442.21.

(9) It is Yates' position that since Pride did not object to the "reasonableness" of its well costs on or before December 31, 2004, as provided by Order No. R-12108-C, then the provisions of Order No. R-12108-C should be final and binding upon Pride, and Pride should not be given the opportunity to object to the well costs at this time.

(10) It is Pride's position that:

a. it should be given the opportunity to object to Yates' well costs;

b. certain of Yates' well costs had to be duplicated by Pride once it commenced re-entry operations on the State "X" Well No. 1, and therefore these duplicative costs should not be allowed; and

c. Pride should only have to pay 50% of the well costs incurred by Yates in its re-entry attempt on the State "X" Well No. 1 because Yates owns a 50% interest in the well unit.

(11) Pride did not object to the "reasonableness" of Yates' well costs until September 30, 2005, nearly nine months after the deadline to object imposed by Order No. R-12108-C had passed.

(12) Pride failed to utilize the opportunity to object to Yates' well costs afforded by Order No. R-12108-C.

(13) Because Pride did not object to Yates' itemized schedule of actual well costs on or before December 31, 2004, under the terms of Order No. R-12108-C, such costs were deemed at that time to be the reasonable well costs. The Division does not have the authority to re-determine that issue, which was decided by the Commission.

(14) The Commission also determined that Pride shall pay to Yates the full amount of the actual well costs identified in Yates' schedule. Ordering paragraphs 10 and 11 of Order No. R-12108-C set out two possible scenarios for payment of Yates' actual well costs, and in each scenario Pride is required to pay the full amount of Yates' actual well costs. Each scenario also takes into account that Pride had previously submitted an AFE for the well by letter dated September 14, 2004 and that Yates, in order to be certain that it was not in a non-consent position under Commission Order No. R-12108-A, had paid to Pride its share of those AFE costs. Each scenario also assumes that Pride will submit a new AFE for the well as required by Ordering Paragraph 8 of Order No. R-12108-C, and that Yates will have a second opportunity to decide whether to participate.

(a) Ordering Paragraph 10 of Order No. R-12108-C applies if Yates elects to pay in advance its share of costs of the re-entry of the well. Under this scenario, Order No. R-12108-C provides that "Yates may deduct the amount of such actual costs from its share of estimated well costs to be paid pursuant to ordering paragraph 8." If the amount is less than the amount already paid by Yates pursuant to Order No. R-12108-A, Pride is to refund the excess to Yates;

(b) Ordering paragraph 11 of Order No. R-12108-C applies if Yates elects not to pay in advance its share of costs of the re-entry. Under this scenario, Order No. R-12108-C provides that "Pride shall refund all amounts paid by Yates at the time of its election pursuant to Order No. R-12108-A, and shall pay to Yates the amount of actual costs included by Yates."

(15) Nothing in Order No. R-12108-C precludes Pride, once it has paid to Yates its actual well costs, from including those costs in Pride's schedule of actual well costs. Inclusion of all of Pride's actual well costs, including payments made to Yates to reimburse Yates for its costs in conducting re-entry operations after August 25, 2003 and prior to October 7, 2004, is contemplated by NMSA 1978, Section 70-2-17, which provides that each owner should pay his proportionate share of actual expenditures required for development and operation of the well. Order No. R-12108-C echoes this language in its provisions regarding owners paying "their share" or a proportionate share, of well costs. See ordering paragraphs 8, 10, 11, 13, 14(a), 15 and 16.

(16) Order No. R-12108-C determined that Pride shall reimburse Yates for actual well costs incurred in its re-entry attempt on the State "X" Well No, 1 during the period after August 25, 2003 and prior to October 7, 2004. Consequently, Pride should be required to pay Yates the amount of $84,391.58.

Issue No. 2: **Pride's Actual Well Costs for Re-entry of the State "X" Well No. 1 and Overpayments Made by Yates to Pride**

(17) The evidence and testimony presented at the hearing relating to the well costs incurred by Pride in its re-entry attempt on the State "X" Well No. 1 is summarized as follows:

a. Yates and its affiliated companies, Yates Drilling Company, Abo Petroleum Corporation, and Myco Industries, Inc. (hereinafter collectively referred to as "Yates") own 50% of the interest in the W/2 of Section 12. On October 13, 2004, Yates paid to Pride a total of $376,647.43 for its share of the estimated well costs to re-enter the State "X" Well No. 1. Yates' 50% share of estimated well costs was based upon Pride's Authority for Expenditure (AFE) dated September 14, 2004 which showed total completed well costs to be $753,294.85;

b. Pride's actual well costs for the State "X" Well No. 1 as shown in Exhibit No. 7, and not including the $84,391.58 Pride is required to pay Yates, is $708,402.78. Included in these actual wells costs are the following charges to which Yates is objecting:

Legal Fees:	$15,215.11
NuTech Energy Alliance:	$ 3,163.60
Heartland Equipment Co.:	$ 888.46
Phillips Casing & Tubing, LP:	$ 248.97
Title Opinion:	$ 1,363.71
Total:	$20,879.85

c. at the hearing, legal counsel for Pride withdrew the charges for NuTech Energy Alliance ($3,163.60), Heartland Equipment Company ($888.46) and Phillips Casing & Tubing, LP ($248.97). Legal counsel for Pride further stated that subsequent to the hearing, Pride will provide a copy of the title opinion to Yates;

d. in its closing statement submitted subsequent to the hearing, Yates stated that they have not yet received a copy of the title opinion from Pride, and therefore requested that this cost be included in its objected charges;

e. subsequent to the time Yates filed its closing statement, Pride stated to the Division that it has provided a copy of the title opinion to Yates. Consequently, this cost should not be considered in dispute at this time;

f. taking into consideration the charges withdrawn by Pride at the hearing, the total charges currently in dispute are $15,215.11 for legal fees.

(18) Yates' position with regards to the legal fees is that these fees may be charged against another party only where authorized by contract or by statute, and further contends that neither of these facts is present in this dispute.

(19) Pride stated that these legal fees are costs relating to the various Division and Commission pooling hearings in this matter, and contends that these costs would not have been incurred if the Division had not cancelled Pride's APD for the State "X" Well No. 1 in August 2003.

(20) Legal fees for compulsory pooling hearings are not customarily included as well costs. Furthermore, there is no evidence to demonstrate that these costs were authorized by contract or statute, therefore these costs are deemed by the Division to be "non-reasonable" well costs and should not be included in the actual well costs.

(21) Pride's actual total well costs for the State "X" Well No. 1 should be established as follows:

$708,402.78 (Actual Well Costs, Exhibit No. 7)
- $ 3,163.60 (NuTech Energy Alliance)
- $ 888.46 (Heartland Equipment Company)
- $ 248.97 (Phillips Casing & Tubing, LP)
- $ 15,215.11 (Legal Fees)

= $688,886.64 (Actual Total Well Costs)

(22) Yates's share of the total well costs are: $344,443.32 determined as follows: (0.5) x $688,886.64.

(23) Pride should be required to reimburse Yates the amount of $32,204.11. This amount was determined by subtracting from the amount Yates has already paid to Pride ($376,647.43), Yates' share of actual total well costs ($344,443.32).

IT IS THEREFORE ORDERED THAT:

(1) The application of Yates Petroleum Corporation is hereby approved.

(2) Pride Energy Company shall reimburse Yates Petroleum Corporation for actual well costs incurred in Yates' re-entry attempt on the State "X" Well No. 1 during the period after August 25, 2003 and prior to October 7, 2004, as required by Order No. R-12108-C.

(3) Within 14 days from the date of this order, Pride Energy Company shall reimburse Yates the following well costs and overpayments:

$84,391.58—The actual well costs incurred by Yates in its re-entry attempt on the State "X" Well No. 1 after August 25, 2003 and prior to October 7, 2004; and

$32,204.11—The amount that Yates' actual payments to Pride exceeded its share of actual well costs.

(4) The portion of Yates' application seeking an order directing Pride Energy Company to plug and abandon the State "X" Well No. 1 is hereby dismissed.

(5) Jurisdiction is hereby 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

MARK E. FESMIRE, P.E.
Director

SEAL