

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

APPLICATION OF THE NEW MEXICO OIL CONSERVATION DIVISION, THROUGH THE ENFORCEMENT AND COMPLIANCE MANAGER, FOR A COMPLIANCE ORDER AGAINST XERIC OIL & GAS CORPORATION, FINDING THAT THE OPERATOR IS IN VIOLATION OF 19.15.3.101.B NMAC AS TO 69 WELLS & 19.15.4.201 NMAC &/OR 19.15.13.1115 NMAC AS TO 80 WELLS; DETERMINING THAT THE REFERENCED VIOLATIONS ARE KNOWING & WILLFUL AND IMPOSING PENALTIES; REQUIRING OPERATOR TO POST THE REQUIRED SINGLE-WELL FINANCIAL ASSURANCES FOR THE 69 NON-COMPLIANT WELLS BY A DATE CERTAIN; REQUIRING OPERATOR TO BRING THE 80 INACTIVE WELLS BACK INTO COMPLIANCE WITH RULE 201 &/OR RULE 1115 BY A DATE CERTAIN; AND IN THE EVENT OF NON-COMPLIANCE WITH ANY ASPECT OF THE ORDER, DECLARING THE WELLS ABANDONED, AUTHORIZING THE DIVISION TO PLUG THE WELLS AND FORFEITING ANY APPLICABLE FINANCIAL ASSURANCE - LEA COUNTY, NEW MEXICO.

CASE NO. 14106 De Novo

PRE-HEARING STATEMENT

The Oil Conservation Division submits this pre-hearing statement pursuant to OCD Rule 19.15.4.13.B NMAC.

APPEARANCES

APPLICANT

OIL CONSERVATION DIVISION

APPLICANT'S ATTORNEY

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RESPONDENT (De Novo Applicant)

XERIC OIL & GAS CORP.

RESPONDENT'S ATTORNEY

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STATEMENT OF THE CASE

The Oil Conservation Division (OCD) seeks a compliance order and penalties against Xeric Oil & Gas Corporation ("Xeric"). Xeric is the Operator of Record for the 88 wells originally identified and referenced by the Application. The Division Rule designated as

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19.15.4.201 NMAC at the time of filing of the application, but now identified as 19.15.5.9 NMAC, requires an operator to plug and abandon or temporarily abandon a well in accordance with Division rules within 90 days after a period of one year of continuous inactivity. The Division Rule designated as 19.15.3.101.B NMAC at the time of filing of the application, but now designated as 19.15.8.9.C NMAC, requires that Operators post additional financial assurance/one-well financial assurance for all state or fee wells that have been inactive/in temporary abandonment for more than two years. For the sake of clarity, the current rule designations will be used from this point forward.

Based upon production reports and data submitted by Xeric to the OCD, at the time of the filing of this Application for Hearing, Xeric had 69 wells in violation of 19.15.8.9.C NMAC and 80 wells in violation of 19.15.5.9 NMAC, with some wells falling into both categories [for a total of 88 wells]. If, however, it is Xeric's contention that any of the specified wells are, indeed, active and thus not in violation of one or both of these two Rules, then Xeric has violated 19.5.7.24 NMAC, which requires Operators to accurately report production on a monthly basis to the OCD.

Significant effort was expended on the part of the OCD both prior and subsequent to the filing of this application to advise Xeric of the ongoing violations and to work with Xeric to remedy the situation. Despite these efforts, the violations not only persisted, but have actually worsened. The following timeline may assist the Commission in understanding the facts and issues before it, and the OCD's rationale for filing an application in this case:

- **2000-2008** General pattern by Xeric Oil and Gas of increasing number of idle, inactive and shut-in wells; increasing noncompliance with OCD Rules; numerous letters issued by District as well as informal notification made by District Office to Xeric of continued occurrences of violations.
- **March 5, 2008** Tim Collier, Ron St. John and Adam Hirschfeld acquired Xeric Oil and Gas ("Xeric") on this date. They reviewed Xeric's well files prior to acquisition and were aware that "there were problems" and that there were "several" noncompliant wells that would need to be addressed. They did not contact NMOCDC prior to acquisition, however, either to inquire regarding the obligations of NM operators or to inquire regarding the company, Xeric. Hirschfeld did utilize the OCD online system prior to the acquisition to obtain list of Xeric wells reporting production. *EXHIBIT 3 - pp. 47, 48, 57, 58, 73.*
- **March 5, 2008** OCD coincidentally filed the Application for hearing the same day that the acquisition took effect, although the OCD had no knowledge of any planned change in management. The OCD was not informed of the change in

management until the April 15, 2008 telephone conference. Hearing was scheduled for April 17, 2008.

- **April 15, 2008**

Two days prior to the scheduled hearing date, new Xeric president Tim Collier and prior principal Joe Cook, contacted OCD by telephone to discuss the filing of application and the scheduled hearing. St. John and Hirschfeld were not in attendance. The hearing was continued by the OCD based on representations made by Mr. Collier during that telephone conference. Mr. Collier relayed information to Hirschfeld following the telephone conference, including that there were wells that they needed to get back on production, that they needed to retain counsel, and that they needed to set up a meeting in person with the OCD. *EXHIBIT 3- pp.22-23.*

- **June 13, 2008**

Conference held at OCD, Santa Fe, and attended by Hirschfeld, Collier, St. John, Xeric counsel and OCD counsel. Numerous issues were discussed at this conference including the inactive well violations and Xeric's continued financial assurance noncompliance. Collier made numerous representations and assurances to OCD on behalf of Xeric regarding plans and intentions of Xeric, and agreed to provide OCD with written plan and timeline and to keep OCD informed of progress and any plan changes. Written submission was to be provided to the OCD so that the OCD would have sufficient time to review it prior to the next scheduled hearing date of July 10, 2008. *EXHIBIT 3 - p.51.*

- **July 1, 2008**

Xeric counsel contacted OCD counsel via email to request a continuance of the upcoming hearing scheduled for July 10th, indicating that Xeric was in the process of coordinating with the District OCD office and was actively preparing the requested written submission. Based on this representation, a final continuance to September 4, 2008 was agreed to by the OCD.

- **July 30, 2008**

Having still not received the promised written submission from Xeric, OCD counsel once again contacted counsel for Xeric to make a status inquiry.

- **August 15, 2008**

The OCD receives a "Status Update and Plan of Action" from Xeric. *EXHIBIT 11.* Upon review, it was determined that the submission was grossly insufficient for numerous

reasons. Most significantly, not only did the "Update" lack any specification of dates or even a general timeframe for completion of work or attainment of goals, but it wholly failed to address the specific violations relating to inactivity and financial assurance noncompliance that were identified in the application for this case.

- August 21, 2008

OCD counsel sent a letter to Xeric counsel outlining findings of insufficiency with regard to Status Update and inviting submission of additional information and documents prior to upcoming hearing date, September 4, 2008. *EXHIBIT 4.*

- September 4, 2008

DIVISION HEARING CONDUCTED. At the time the application was filed, operator had 69 wells (of 110 total) for which additional bonding was owed, totaling \$734,814 in additional bonding owed, and 80 wells that were inactive for one year plus 90 days in violation of OCD Rules. At the time of the hearing, these figures had increased to **74 wells with outstanding bonding owed, totaling \$781,982 owed, and 82 total "inactive" wells.**

TESTIMONY was presented by Xeric principals St. John and Hirschfeld that Collier was no longer a partner, but that at all times prior he had been authorized to act on behalf of Xeric and St. John and Hirschfeld were aware of the fact that Collier had made certain representations and assurances to the OCD on behalf of Xeric. Both acknowledged that the promises made by Collier had not been fulfilled. St. John and Hirschfeld testified that the focus of Xeric's efforts for getting into compliance was to start with the "Gregory" and "Crosby Deep" leases first, and that they had been in communication with a rig company already and anticipated moving quickly with regard to the first ten sites they had begun work on. Xeric presented as exhibits, ten sundries for wells located on these identified leases, and indicated that it was Xeric's intention to either return each to production or plug them, and that they planned to formally file each sundry within the week. Hirschfeld stated that he did not begin to familiarize himself with the New Mexico OCD rules until after the June 13, 2008 conference with the OCD, and that as of the date of the September hearing, he had not yet contacted the OCD financial assurance administrator to obtain information regarding financial assurance

requirements, process, etc. *Exhibit 3- pp.34, 42, 48, 70-71, 80-81, 83.* (Sundry Exhibit from Division Hearing: *EXHIBIT 2*).

- October 10, 2008

Order R-13005 - Issued by the Division, finding that Xeric knowingly and willfully violated the OCD Rules previously-designated as Rules 101.B and 201. The Order required that the single-well financial assurances owed on the 69 wells specified in the Application be paid by November 28, 2008, that all delinquent production reports be filed by December 31, 2008, that the 80 inactive wells be plugged or otherwise returned to compliance by January 30, 2008 and that Xeric pay a penalty assessment of \$88,000 by January 30, 2008. *EXHIBIT 5*.

- February 5, 2009

COMPLIANCE STATUS: 74 wells with outstanding bonding owed totaling \$781,982, and 82 inactive wells. Penalty assessment has not been paid; all deadlines set by Division Order disregarded. *EXHIBITS 7-10*.

Although De Novo request filed, NO STAY requested or granted, and therefore underlying Division Order stands; Xeric now in full violation of all ordering paragraphs of Order No. R-13005.

INSPECTIONS conducted and photos taken of the 10 Gregory and Crosby Deep wells reference d at Division Hearing: 0/10 wells appear active; 0/10 wells are plugged; 8/10 wells have no flowlines to wellhead; 1/10 wells has stained soil and oil around wellhead; 2/10 with sub-pump still in the hole and the cable cut off at surface. *EXHIBIT 6*.

- February 13, 2008

OCD discovered that an incorrect depth had previously been reported/recorded for one of Xeric's inactive wells, and that therefore the single well financial assurance based on depth for that well was incorrectly noted on the system. Therefore, the actual, total outstanding single-well financial assurance owed is actually \$667,130 for 74 wells. *EXHIBIT 1*.

Xeric has a longstanding history in this state as a company with no regard for the laws or rules of New Mexico, and present management has perpetuated the well-established bad practices of this company since becoming involved in March of last year. Xeric thus has been and continues to be grossly out of compliance with OCD rules, and does so in a knowing and willful manner. It has now been nearly a year since the filing of this

action, and, coincidentally since the acquisition of Xeric by the new principals, during which time the number of wells out of compliance has actually increased. Xeric has yet to post a single one of the individual bonds that came due as of January 1, 2008, which it owes on its many inactive wells and which St. John and Hirschfeld unequivocally acknowledged they have been aware of since at least June of last year. St. John and Hirschfeld failed to make even the most basic inquiry regarding their duties and obligations as New Mexico operators and to plan accordingly with regard to acquiring this company, and upon being informed of their obligations, have subsequently failed to take steps to remedy their mistakes.

Xeric has been given repeated opportunities by the OCD to work with the OCD to try to find a solution to the longstanding, ongoing and worsening noncompliance issues, and has repeatedly chosen not to take advantage of those opportunities. Ultimately, after having heard evidence regarding Xeric's refusal to honor its obligations and after learning of its insistence on remaining in a state of continued noncompliance, the Division ordered Xeric to bring these wells into compliance by dates certain assessed Xeric a penalty. Without seeking or being granted a stay of the Order, Xeric simply chose to disregard that Order, much like it has chosen to disregard OCD rules, and has persisted in its failure and refusal to comply with New Mexico rules.

Xeric's persistent disregard for New Mexico law and rules is apparent from its longstanding pattern and practice as a New Mexico operator. The sheer numbers of wells involved in this case, together with the clear knowing and willful nature of the violations, justify the imposition of significant penalties. The OCD originally sought only the assessment of the amount of \$1,000 per well for a total of \$88,000, which the Division Order imposed, and Xeric has since disregarded. At this time, given the disregard for the Division Order and the continued noncompliance, the OCD feels a more significant penalty assessment is appropriate and therefore seeks a penalty assessment in the amount of at least double that imposed by the Division order: \$176,000.

The OCD seeks an Order stating the following in this case:

1. Requiring that by a date certain, Xeric be required to post each and every single-well financial assurance required pursuant to 19.15.8.9.C NMAC (currently a total of \$667,130 for 74 wells). ¹
2. Requiring that as to each of the 80 wells specified in the Application as inactive (in violation of 19.15.5.9 NMAC, formerly referred to as Rule 201) by a date certain, Xeric properly plug and abandon those wells, and file all required reports and paperwork.
3. Requiring that Xeric pay a monetary penalty assessment the amount of \$176,000 (twice that which was imposed at the Division Hearing due to the severity (88 wells in violation of one or both of the identified Rules at

¹ Once bonds are posted, and then upon plugging and abandoning **and full release of the site** of each of these inactive wells, Xeric may seek release of the posted bonds.

the time of filing) and duration (over ten years in some instances with regard to violations of Rule 201/19.15.5.9 NMAC, and continuing in nature even after issuance of a Division Order) of Xeric's willful violations, pursuant to NMSA 1978, Section 70-2-31(A), specifically for its knowing and willful violations of Rules 101/19.15.5.9 NMAC, 201/19.15.5.9 NMAC and/or Rule 1115/19.5.7.24 NMAC (independent of and in addition to any other penalty assessment(s) Ordered in this matter for other violations of the OCD Rules and/or the New Mexico Oil and Gas Act).

4. Requiring Xeric to submit any and all delinquent C115s reflecting any as-yet unreported production, if any, for the subject wells by a date certain.
5. Requiring that Xeric reappear before the Commission at the Commission Meeting to be conducted in April, 2009 (currently scheduled for April 9, 2009) for purposes of a Status Hearing to advise the Division and the Commission as to the Status of actions taken toward fulfillment of obligations imposed by the Commission's Order.
6. Requiring that Xeric reappear before the Commission at the next Commission Meeting scheduled to be held following the last deadline set by the Commission's Order in this matter for purposes of Xeric providing confirmation that all deadlines set by the Order have been met.
7. Further, if Xeric fails to meet the deadlines set by the Order:
 - (1) Assessing a penalty against Xeric of not less than \$1,000.00 for each full week of non-compliance with the Order;
 - (2) Authorizing the Division to plug the subject wells in accordance with a Division-approved plugging program, pursuant to NMSA 2008 §70-2-14(B);
 - (3) Authorizing the Division to forfeit any applicable financial assurances posted in relation to the subject wells; and
 - (4) For such other and further relief as the Director deems just and proper under the circumstances.

APPLICANT'S PROPOSED EVIDENCE

WITNESS:

Daniel Sanchez, Enforcement & Compliance Manager
Dorothy Phillips, Financial Assurance Administrator

ESTIMATED TIME:

60 minutes
Affidavit

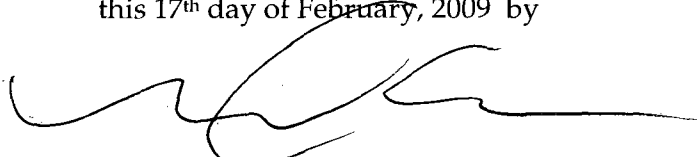
EXHIBITS (submitted simultaneously herewith):

1. Affidavit of Dorothy Phillips, Financial Assurance Administrator for the OCD.²
2. Xeric "Exhibit C" from September 4, 2008 Division Hearing, consisting of 10 Notice of intent sundry forms completed but never filed by Xeric.
3. Transcript Portions from OCD Division Hearing conducted September 4, 2008: testimony of Xeric Representatives Ronald St. John and Adam Hirschfeld.
4. Letter dated August 21, 2008 from OCD counsel to counsel for Xeric.
5. Division Order dated October 10, 2008 arising out of Hearing conducted on September 4, 2008.
6. Photographs and Inspection records for inspections of ten "Crosby Deep" and "Gregory" lease wells for inspections performed on February 6, 2009.
- 10 ~~X~~ 7. Inactive Well List for Xeric from OCD Online dated September 3, 2008.
8. Inactive Well List for Xeric from OCD Online dated February 16, 2009.
9. Inactive Well Additional Financial Assurance Report from OCD Online dated February 16, 2009.
- 7 ~~X~~ 10. Inactive Well Additional Financial Assurance Report from OCD Online dated September 3, 2008.
11. August 15, 2008 Status Update and Plan of Action Received from Xeric.

PROCEDURAL MATTERS

None.

Respectfully submitted
this 17th day of February, 2009 by

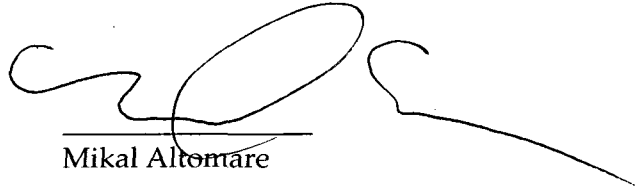


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² Please note that due to Ms. Phillips being unexpectedly out of the office due to illness, the attached version of Exhibit 1, Affidavit of Dorothy Phillips, has not yet been fully executed. The fully executed version will be submitted as soon as Ms. Phillips is available to execute it.

CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing pleading was emailed to counsel for Xeric, Ms. Ocean Munds-Dry, Esq. at OMundsDry@HollandHart.com, this 17th day of February, 2009.



Mikal Altomare