

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

**APPLICATION OF CHI ENERGY, INC. FOR APPROVAL OF A SECONDARY
RECOVERY PROJECT AND TO QUALIFY THE PROJECT FOR THE RECOVERED
OIL TAX RATE, EDDY COUNTY, NEW MEXICO.**

CASE NO. 14353

**REVISED
ENTRY OF APPEARANCE AND
PRE-HEARING STATEMENT OF THE OIL CONSERVATION DIVISION**

The Oil Conservation Division (OCD) submits this revised pre-hearing statement pursuant to 19.15.4.13(B) NMAC to address issues that have arisen since the OCD filed its original pre-hearing statement, and add a witness.

RECEIVED
OCD
2009 OCT 22
P 2:55

APPEARANCES

APPLICANT
Oil Conservation Division

APPLICANT'S ATTORNEY
Gail MacQuesten
Oil Conservation Division
Energy, Minerals and Natural
Resources Department
1220 S. St. Francis Drive
Santa Fe, NM 87505
(505) 476-3451
FAX: 476-3462
E-mail: gail.macquesten@state.nm.us

RESPONDENT
Chi Operating, Inc.

RESPONDENT'S ATTORNEY
James Bruce
Post Office Box 1056
Santa Fe, NM 87504
(505) 982-2043

STATEMENT OF CASE

Chi Energy, Inc. (Chi) has applied for a waterflood project.

Rule 19.15.26.8 NMAC provides that the Oil Conservation Division may grant a permit for injection only to an operator who is in compliance with Subsection A of 19.15.5.9 NMAC (Part 5.9). The OCD entered its appearance in this case to alert the hearing examiners to the fact that Chi was out of compliance with Part 5.9.

At the time the OCD filed its original entry of appearance, it identified a particular Part 5.9 issue: Chi's failure to post a single well financial assurance for one of its wells. Chi has since addressed that particular issue. However, the OCD has reviewed Chi's compliance with Part 5.9 and identified additional issues. Those issues are set out in the attached letter, which was sent to Chi's attorney on October 15, 2009.

The Oil Conservation Division objects to the grant of an injection permit to Chi while it is out of compliance with Part 5.9.

OCD'S PROPOSED EVIDENCE

WITNESS: Jane Prouty, OCD Bureau Chief for Automation and Records
ESTIMATED TIME: 30 minutes

WITNESS: Dorothy Phillips, Financial Assurance Administrator
ESTIMATED TIME: by affidavit

Witness: Daniel Sanchez, OCD Compliance and Enforcement Manager
ESTIMATED TIME: 10 minutes

PROCEDURAL MATTERS

By separate document, the OCD will be requesting that this matter be continued.

Respectfully submitted
this 21st day of October 2009 by

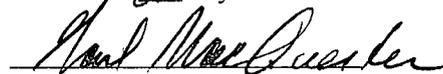


Gail MacQuesten
Oil Conservation Division
Energy, Minerals and Natural
Resources Department
1220 S. St. Francis Drive
Santa Fe, NM 87505
(505) 476-3451

Attorney for the Oil Conservation Division

Certificate of Service

I certify that I mailed and e-mailed a copy of this pleading to Mr. James Bruce at the addresses shown above this 21st day of October 2009.


Gail MacQuesten

New Mexico Energy, Minerals and Natural Resources Department

Bill Richardson
Governor

Joanna Prukop
Cabinet Secretary

Mark Fesmire
Division Director
Oil Conservation Division



October 15, 2009

James Bruce
P.O. Box 1056
Santa Fe NM 87504-1056

e-mail: jamesbruc@aol.com

Re: Chi Operating, Inc., OGRID 4378
Case No. 14353

Dear Mr. Bruce:

In Case No. 14353 Chi Operating, Inc. (Chi) seeks approval of a waterflood project. 19.15.26.8 NMAC provides, in relevant part, that the division may only grant injection permits to operators in compliance with 19.15.5.9 NMAC, commonly known as "Part 5.9." The Oil Conservation Division (OCD) entered its appearance in Case No. 14353 to alert the hearing examiners to the fact that Chi was out of compliance with Part 5.9, and therefore could not obtain approval of the waterflood project. At the time the OCD filed its entry of appearance, the financial assurance report on OCD's website showed that Chi was out of compliance with Part 5.9 because it had not posted the required single well financial assurance for one of its inactive wells. Chi has since resolved that issue. However, the OCD has found additional Part 5.9 issues.

Part 5.9 requires, in part, that operators be in compliance with financial assurance requirements of 19.15.8.9 NMAC, and not have too many wells in violation of the inactive well rule, 19.15.25.8 NMAC. The number of non-compliant inactive wells allowed depends on the size of the operator. As the operator of record of 115 wells, Chi can have no more than 5 wells in violation of the inactive well rule and still be in compliance with Part 5.9.

The financial assurance requirements include the requirement that all state or fee wells that have been inactive for more than two years and are not plugged and released be covered by a single-well financial assurance. A single-well financial assurance is required even if the well is also covered by a blanket financial assurance, even if the well is on approved temporary abandonment status, and even if the wellbore has been plugged.

The OCD website includes a financial assurance report and an inactive well list to help operators track their compliance with those requirements. Those lists do not show all violations, however, because the computer only looks at the compliance of wells that have reported production or injection at some point in time. (Including wells that never reported production or injection would result in including wells for which an APD was issued, even if that well was never drilled, or was just recently completed.)



Chi's well list includes a large number of wells that have never reported production or injection. I have researched the well files for those wells, and found the following violations of the inactive well rule and the single well financial assurance requirements:

Elkan #002, 30-025-38525. The well file indicates that the wellbore of this well was plugged in 2006. The well is not considered "plugged" for purposes of the inactive well rule because the well site has not been cleaned up and released as required by 19.15.25.10 NMAC. The site should have been cleaned no later than one year after the plugging of the wellbore. The OCD issued Chi a letter of violation, dated 3-18-08, regarding the need to clean the well site. This well is a fee well that has been inactive for more than two years. This well is in violation of both the inactive well rule and the single well financial assurance requirements. If Chi completes the cleanup of the site and the district office approves the release of the well, the well will not be in violation of the inactive well rule and will not require a single-well financial assurance.

Elkan #002Y, 30-025-38186. The well file indicates this well was drilled, and the wellbore plugged, in January 2007. Again, the well is not considered plugged because the site has not been cleaned and released. The OCD issued Chi a letter of violation, dated 3-18-08, regarding the need to clean the well site. This well is a fee well that has been inactive for more than two years. This well is in violation of both the inactive well rule and the single well financial assurance requirements.

Footjoy 14 State #001, 30-015-33721. According to the well file, this well was drilled in 2005. Chi filed a notice of intent to plug the well dated January 8, 2009, but nothing appears in the well file to show that the well has been plugged. This is a state well that has been inactive for more than two years. This well is in violation of both the inactive well rule and the single well financial assurance requirements.

In Bounds Com #001, 30-015-31600. From the documents in the well file, it appears that the wellbore of this well was plugged in 2002, but the well is not considered plugged because of unresolved pit closure issues. This is a fee well that has been inactive for more than two years. The well is in violation of both the inactive well rule and the single well financial assurance requirements.

Munchkin Fed #007, 30-015-33933. According to the well file, this well was drilled in November 2006. The well file includes a notice of intent to plug back, but there is no further documentation to indicate whether that was done. The OCD issued Chi a letter of violation dated 8-6-09 regarding the inactive well violation. Because this well is federal, there is no requirement for a single well financial assurance.

Nicols 30 State Com #002, 30-015-36788. According to the well file, this well was drilled in December of 2008 and January of 2009. Chi filed a notice of intent to plug, which was approved with the condition that the work be completed by 9-26-09. No further information appears in the well file. The inactive well rule requires a well to be plugged within 90 days after a 60-day period following suspension of drilling operations or a determination that the well is no longer usable for beneficial purposes. The well is in violation of the inactive well rule. Because this state well has not been inactive for more than two years, it is not yet in violation of the single-well financial assurance requirements.

Oxy Marsh Hawk State #002, 30-025-38309. From the well file, it appears that this well was drilled in October 2007, and the wellbore was plugged in January of 2008. The well is not considered plugged because the site has not been cleaned and released. It is in violation of the

inactive well rule because site cleanup was not completed within one year of the plugging of the wellbore. The state well has been or soon will be inactive for more than two years, and that will put it in violation of the single-well financial assurance requirements.

Salado Fed. #001, 30-025-38402. The well file indicates that the wellbore of this well was plugged 8-6-07. It has not been released. It appears that there may be unresolved issues involving a pit closure. Because this well is federal, it is not in violation of the single-well financial assurance requirements.

Silver Bullet #001, 30-015-21789. It appears from the documents in the well file that the wellbore of this well was plugged after a re-entry in 2005. The well is not considered plugged because the site has not been cleaned and released. This state well has been inactive for more than two years and is in violation of the single-well financial assurance requirements in addition to the inactive well rule.

WC 4 #001, 30-015-31773. The status of this well is unclear from the well file. There is an extension on an APD until a date in 2003. There are no documents in the file indicating the well was drilled. However, there is an approved application for closure of a drilling pit, dated 7-16-07. If this fee well was drilled in 2003, it is in violation of the inactive well rule and the single-well financial assurance requirements.

Please encourage Chi to review the well files for these wells. If Chi disagrees with the OCD's analysis of the information in the well files, please let us know. If the information in the well files is incorrect or out of date, please work with the relevant district office to correct those errors.

The OCD performed this record review for Chi in an effort to move forward with Case 14353. However, it is Chi's responsibility to be aware of the compliance status of its wells and take the appropriate actions to stay in compliance. It is disturbing to learn that the OCD issued letters of violation putting Chi on notice of three of the issues identified above, yet it appears that Chi did nothing to return those wells to compliance.

If Chi is still out of compliance with Part 5.9 when Case 14353 is heard, the OCD will be prepared to present evidence of the Part 5.9 violations.

Sincerely,



Daniel Sanchez
Compliance and Enforcement Manager

Ec: Gail MacQuesten, OCD Attorney
Larry "Buddy" Hill, District 1
Randy Dade, District 2