

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:)
APPLICATION OF CHESAPEAKE OPERATING,)
INC., FOR COMPULSORY POOLING, LEA)
COUNTY, NEW MEXICO)

CASE NO. 11,836

ORIGINAL

REPORTER'S TRANSCRIPT OF PROCEEDINGS

EXAMINER HEARING

RECEIVED

BEFORE: MICHAEL E. STOGNER, Hearing Examiner

SEP 11 1997

Oil Conservation Division

August 21st, 1997

Santa Fe, New Mexico

This matter came on for hearing before the New Mexico Oil Conservation Division, MICHAEL E. STOGNER, Hearing Examiner, on Thursday, August 21st, 1997, at the New Mexico Energy, Minerals and Natural Resources Department, Porter Hall, 2040 South Pacheco, Santa Fe, New Mexico, Steven T. Brenner, Certified Court Reporter No. 7 for the State of New Mexico.

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 Examiner Hearing
 CASE NO. 11,836

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A P P E A R A N C E S

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By: PAUL R. OWEN

* * *

1 WHEREUPON, the following proceedings were had at
2 9:58 a.m.:

3 EXAMINER STOGNER: At this time I'll call Case
4 Number 11,836.

5 MR. CARROLL: Application of Chesapeake
6 Operating, Inc., for compulsory pooling, Lea County, New
7 Mexico.

8 EXAMINER STOGNER: Call for appearances.

9 MR. KELLAHIN: Mr. Examiner, I'm Tom Kellahin of
10 the Santa Fe law firm of Kellahin and Kellahin, appearing
11 on behalf of the Applicant, and I have two witnesses to be
12 sworn.

13 EXAMINER STOGNER: Any other appearances?

14 MR. OWEN: Paul Owen of the Santa Fe law firm of
15 Campbell, Carr, Berge and Sheridan for Bristol Resources
16 Corporation.

17 EXAMINER STOGNER: Does Bristol have any
18 witnesses?

19 MR. OWEN: I have no witnesses in this matter,
20 Mr. Examiner.

21 EXAMINER STOGNER: Any other appearances?
22 How many witnesses do you have, Mr. Kellahin?

23 MR. KELLAHIN: Two, sir.

24 EXAMINER STOGNER: Will both witnesses please
25 stand to be sworn?

1 (Thereupon, the witnesses were sworn.)

2 MR. KELLAHIN: Mr. Examiner, I've distributed to
3 the court reporter and to you and Mr. Carroll copies of
4 Chesapeake's exhibits, and I've also handed a set to Mr.
5 Owen.

6 At this time we'd call Mr. Mike Hazlip. Mr.
7 Hazlip spells his last name H-a-z-l-i-p. He's a petroleum
8 landman with Chesapeake.

9 I gave you a set of marked exhibits, didn't I,
10 Mike?

11 MR. HAZLIP: Yes.

12 MR. KELLAHIN: Mr. Examiner, Mr. Hazlip.

13 MIKE HAZLIP,

14 the witness herein, after having been first duly sworn upon
15 his oath, was examined and testified as follows:

16 DIRECT EXAMINATION

17 BY MR. KELLAHIN:

18 Q. Mr. Hazlip, for the record, would you please
19 state your name and occupation?

20 A. Mike Hazlip, a landman for the Permian Basin for
21 Chesapeake Operating, Inc.

22 Q. And where do you reside, sir?

23 A. In Oklahoma City.

24 Q. On prior occasions, have you testified before the
25 Division and qualified as a petroleum landman?

1 A. Yes, sir.

2 Q. Pursuant to your employment, have you identified
3 a spacing unit in Lea County, New Mexico, that is subject
4 to the Northeast Lovington-Pennsylvanian Pool and have
5 proposed to locate and identify the interest owners in that
6 spacing unit?

7 A. Yes, sir.

8 Q. Having identified the interest owners, have you
9 attempted to negotiate with all the interest owners to form
10 on a voluntary basis a spacing unit for the drilling of
11 this well?

12 A. Yes, we have.

13 MR. KELLAHIN: We tender Mr. Hazlip as an expert
14 petroleum landman.

15 EXAMINER STOGNER: Mr. Hazlip is so qualified.

16 Q. (By Mr. Kellahin) Let's take a moment, Mr.
17 Hazlip, and turn your attention to Exhibit 1, orient the
18 Examiner to your proposal, and start off by identifying the
19 type of exhibit we're looking at.

20 A. Yes, this exhibit is the plat showing, in the
21 south half of the southeast quarter of Section 1 of 16-36,
22 the proposed proration unit.

23 Q. Locate us in relation to the community of
24 Lovington. Where are we?

25 A. We're about a mile and a half, two miles east of

1 Lovington, the city of Lovington.

2 Q. There are a number of Strawn well exploration
3 efforts going on in this general area. Have you identified
4 to your satisfaction what proposed Strawn pool you think
5 this well will be dedicated to?

6 A. Yes, sir --

7 Q. And what --

8 A. -- the Northeast Lovington-Penn.

9 Q. And what is the spacing provided in that pool?

10 A. Eighty acres.

11 Q. And what would a standard well location be?

12 A. It would be 330 from the boundaries and 150 feet
13 from the center of the offsetting quarter -- quarter-
14 quarter.

15 Q. The Kim 1-1 well, which is proposed to be in this
16 spacing unit, is located in an irregular-size section, is
17 it not? This section contains more than 640 acres?

18 A. Yes, sir, it does.

19 Q. When we get down to this portion of the section,
20 is this a standard size and shape for an 80-acre spacing
21 unit?

22 A. Yes, it is.

23 Q. All right. In a general chronological fashion,
24 describe when you first commenced efforts to acquire an
25 interest for your company and consolidate the other

1 interests for the drilling of this well.

2 A. It would have been late last year when I first
3 started. It was -- As far as this interest that we're
4 concerned about today, we started probably in January or
5 February.

6 Q. When you first started, how did you acquire
7 Chesapeake's interest, and from whom?

8 A. We went to the largest owner, which was Conoco,
9 and acquired a term assignment from them.

10 Q. In that spacing unit, how big an interest did
11 Conoco have?

12 A. They have a 65-percent working interest.

13 Q. Were you able to negotiate a term assignment with
14 Conoco by which they would assign to you their interest so
15 that you could drill this well?

16 A. Yes, we did.

17 Q. How long a period of time did you have under the
18 term assignment to commence operations for the drilling of
19 this well?

20 A. On this portion of the acreage contributed by
21 Conoco, we had 90 days.

22 Q. Let me direct your attention to Exhibit 2. Would
23 you identify and describe what Exhibit 2 is?

24 A. Yes, that's copy of the term assignment granted
25 from Conoco to Chesapeake.

1 Q. Under this term assignment, when would the 90
2 days have expired so that you could not have drilled the
3 well?

4 A. This term assignment was to expire August 29th,
5 1997.

6 Q. So unless it had been extended, it would expire
7 next week?

8 A. Yes.

9 Q. During this period of time in which you had the
10 term assignment from Conoco, were you negotiating with any
11 of the other working interest owners to acquire their
12 participation or their interest?

13 A. Yes, we were.

14 Q. Who were the other parties that you were dealing
15 with?

16 A. We had previously negotiated a deal with Chapman,
17 who had an additional ten-percent interest. That was
18 another term assignment we gained. And the only other
19 outstanding interest at that time was owned by Bristol
20 Resources.

21 We initially started working with Apache on it.
22 They were of record, interest owner of record. And at some
23 point they finally realized it was not their interest, they
24 had conveyed it to Bristol Resources, so we began pursuing
25 Bristol.

1 Q. As of this morning, what company owns what
2 percentage of outstanding interest not yet committed?

3 A. Bristol Resources owns 25 percent that's
4 uncommitted.

5 Q. Let's turn to Exhibit Number 3. As a result of
6 the inabilities to get Bristol's voluntary cooperation,
7 were you compelled to obtain an extension from Conoco to
8 the farmout --

9 A. Yes.

10 Q. -- I mean to the term assignment?

11 A. Yes, we were.

12 Q. When we look at Exhibit 3, what now is the
13 expiration date for the term assignment by which you
14 control 65 percent?

15 A. We have until October 1st to drill our well.

16 Q. Let's turn to Exhibit 4. You referred to the
17 Chapman interest. That was a ten-percent interest that you
18 acquired?

19 A. Yes, sir.

20 Q. And it was acquired by another term assignment?

21 A. Yes.

22 Q. And what are we looking at here in Exhibit 4,
23 then?

24 A. Exhibit 4 is the term assignment from Chapman
25 covering a ten-percent interest over a good bit of acreage,

1 including their interest in the south half of the southeast
2 quarter of Section 1, where our proration unit --

3 Q. As to this spacing unit, when will this term
4 assignment expire?

5 A. This is a one-year term assignment, and with the
6 continuous development program and basically this being our
7 first well on the acreage that's covered by this term
8 assignment, we've got a lot of -- if this is -- if all the
9 acreage that's under this term assignment is prospective,
10 we've got to move on the initial well in order to complete
11 any other wells that might be prospective in here within
12 the term given.

13 Q. Let's turn to Exhibit 5, then, and describe for
14 the Examiner your efforts to obtain an agreement from
15 Bristol Resources, commencing -- and I -- Let's go back and
16 start with the Apache efforts.

17 Approximately when did that occur, and why were
18 you dealing with Apache?

19 A. That was late -- either late last year or January
20 of this year, we were working with Apache because they were
21 -- the indications that we had were that they were of
22 record, record owner for that 25 percent. We worked with
23 them for several months before determining that they had
24 sold their interest to Bristol Resources.

25 Q. All right, let's stop at that point, have you set

1 aside Exhibit 5, and we'll use that as a reference for your
2 subsequent testimony, and as we do that we'll go through
3 the correspondence and keep it chronological as well.

4 A. Okay.

5 Q. So if you'll refer to Exhibit 6, identify and
6 describe for us what we're looking at when we see this
7 exhibit.

8 A. After months of phone conversation and discussion
9 with Apache, Gary Carson with Apache Corporation, we
10 finally sent them a well proposal and AFE on April 23rd,
11 1997. That's Exhibit 6.

12 Q. And it has an attached AFE to it?

13 A. Yes, sir.

14 Q. Has this AFE changed since it was originally
15 submitted to Apache? It's an AFE dated April 18th, 1997.

16 A. No, sir, it hasn't.

17 Q. All right, so this continues to be the AFE that
18 you're utilizing in your discussions with Bristol and that
19 you're now proposing to the Division Examiner, adopted as a
20 reasonable AFE for purposes of a pooling order?

21 A. Yes, sir.

22 Q. All right. Following the Exhibit 6 letter of
23 April 23rd, what then is the next correspondence?

24 A. Well, as soon as we found out that Bristol had
25 the interest, we notified them immediately with a letter

1 and -- proposing this well and with an attached AFE. And I
2 was told by Apache to contact Mr. Charlie Sherwood of
3 Bristol Resources, and did so immediately.

4 Q. Identify for us, then, what Exhibit 7 is.

5 A. And that letter is Exhibit 7.

6 Q. It is dated April 24th?

7 A. Yes, sir.

8 Q. Now, if we turn to the chronology, Exhibit 5,
9 following your letter to Bristol, summarize for us the
10 sequence of telephone conversations between that point and
11 the next correspondence, which is June 25th.

12 A. Well, there were numerous phone conversations
13 between myself and Bristol Resources, and these are just
14 the ones that I had written in my notes.

15 But on -- After the letter was sent April 24th, I
16 made a phone call to Charlie Sherwood on May 13th, May
17 14th.

18 And then there are two dates that I don't have --
19 I don't have the dates written down, but I know they were
20 made before June 12th. And I was not given any assistance.
21 I could very seldom get hold of Charlie Sherwood. So I
22 went to Bristol, and I can't remember the name, but someone
23 in management with Bristol Resources. He gave me Ed Watts
24 to contact.

25 On June 12th I received a phone call from Ed

1 Watts at Bristol, explaining to me that they would be doing
2 something, they weren't going to hold us up, and so on and
3 so forth.

4 Q. On June 25th, did you have another phone
5 conversation with Mr. Watts?

6 A. Well, on June 23rd I did.

7 Q. I'm sorry, June 23rd?

8 A. Yes, sir.

9 Q. And summarize for us what that conversation was.

10 A. Well, he stated in that conversation that they
11 would farm out their interests to us, covering various bits
12 of acreage in Sections 1 and 6, under a farmout agreement
13 that would contain a 180-day continuous development, with a
14 simple override, they'd be delivering to us 75-percent net
15 revenue interest and retain -- I believe it was a 6.25-
16 percent override.

17 And he asked me to go ahead and send him a letter
18 so that they could sign off on it.

19 Q. Describe for us the kinds of farmout terms you're
20 accustomed to dealing with in this general vicinity in
21 terms of the percentage of net revenue interest that you
22 receive, what kind of back-in after payout are you
23 typically providing, and give us a general sense of what
24 these numbers mean.

25 A. Well, on the Conoco term assignment, we were

1 delivered a 75-percent net revenue, proportionately reduced
2 to their interest, with no back-in or -- just a simple
3 override.

4 On the Chapman interest, we were delivered a 76-
5 percent net revenue interest, no back-in, no escalation of
6 override.

7 These are -- And these cover a good bit of
8 acreage and not just the proration unit itself. We
9 generally on a term assignment, if they grant us an acreage
10 position, pay a bonus consideration to them for something
11 of, generally, a longer term assignment.

12 Q. What kind of back-in after payout, if any, is
13 typical in this type of exploration?

14 A. Under a general farmout agreement, oftentimes
15 there is no back-in after payout; there is a simple
16 override. When there is a back-in it's generally a 25-
17 percent back-in, proportionately reduced to the owner's
18 interest.

19 Q. Okay. At this point what belief did you have
20 about the ability of you and Bristol to reach farmout terms
21 of their interest, to make a farmout to Chesapeake?

22 A. Well, at -- On our June 23rd date, when I had a
23 conversation with him, I thought we had worked out a deal.
24 And he told me to send a letter. I faxed it to him on the
25 25th, the same scenario we had discussed.

1 And again, we had gone through several scenarios
2 already over the phone, several possibilities. Ed had
3 expressed to me that the term assignment would probably not
4 work, term assignment with -- I had offered them a bonus
5 consideration for a term assignment covering a good bit of
6 acreage out there in Section 1 and 2. They had said that
7 that would probably not work for them, they would rather go
8 with a farmout agreement, some kind of a -- well, something
9 along the lines of what I sent him, a 90-day farmout
10 agreement with continuous development.

11 Q. And you did that by Exhibit 8, which is your
12 letter of June 25th?

13 A. Yes, sir.

14 Q. All right, and it sets forth in writing what
15 you've just summarized for us?

16 A. Yes, sir, it does.

17 Q. What then is the next event in this effort by you
18 to obtain agreement from Bristol?

19 A. Well, after sending the letter and not receiving
20 it back signed, I called Ed Watts of Bristol on June 26th,
21 June 30th and July 8th, July 21st, all the time hearing
22 that -- you know, being just simply put off, told that we
23 -- you know, it's just a matter of time, it's -- you know,
24 he just needed to get some management approval, needed to
25 get management to sign off on it, and it was just a matter

1 of him catching his management at the right time. They
2 seemed too preoccupied with other things, too busy, so on
3 and so forth, so...

4 Q. On August 13th -- Subsequent to August 13th, did
5 you receive a letter dated August 13th from Bristol?

6 A. Yes, I received a letter from Bristol -- Well, I
7 had received nothing until August 13th but on August 13th
8 received a fax from Bristol Resources telling us that they
9 would farm out under not exactly the terms we had discussed
10 before.

11 Q. Now, these terms are better for Bristol than what
12 you thought you and Mr. Watts had agreed to back in June?

13 A. Certainly.

14 Q. All right. What then happened?

15 A. Well, it gives them the option to increase their
16 override an additional five percent, and it drops us down
17 to a 70-percent net revenue. And again, it was unclear as
18 to how much authority we were -- Mr. Watts was given when
19 he wrote this letter. It says that it's subject to final
20 management approval.

21 And so it was nothing that we could feel like we
22 could depend on at this point, since we had been through
23 this process for such a long period of time with Bristol
24 already.

25 Q. Following that did you get another letter dated

1 the next day, August 14th from Bristol?

2 A. Yes, the very next day I get another letter from
3 Bristol indicating that they would -- they may participate
4 with some or all of their interest in Kim 1-1, which just
5 contradicts the letter I received the day before.

6 Q. The day following that, on August 15th, then, did
7 you respond to Mr. Watts?

8 A. Yes.

9 Q. That's set forth on Exhibit 11?

10 A. Yes, sir.

11 Q. Summarize for us what you're communicating to Mr.
12 Watts in Exhibit 11.

13 A. Basically just that we would be willing to accept
14 the terms that we had discussed before, and we would accept
15 the terms that he sent in his letter, with the exception of
16 the five-percent escalation of override after payout.

17 Q. And the reason that you could not accept that
18 counterproposal by Bristol was what, sir?

19 A. It just burdens -- It's too heavy a burden for us
20 to bear at 70 percent net revenue for our one well.

21 Q. Did you also transmit to Mr. Watts a suggested
22 form of operating agreement, which obviously still needed
23 to be edited by both companies, but did you communicate to
24 him a sample of an operating agreement?

25 A. Yes, at his request we sent a JOA that -- as we

1 generally use in that area.

2 Q. Okay. At this point where do we stand in terms
3 of Bristol and your ability to reach an agreement, Mr.
4 Hazlip?

5 A. I feel like we're at the same place we were when
6 we began this thing. We still don't have anything.

7 I have -- I called Ed Watts as late as Tuesday,
8 knowing that we had to leave Wednesday morning to come up
9 here and ask Ed for some agreement that was approved by
10 their management so that we didn't have to go through this
11 force-pooling process, and he assured me that he was still
12 trying to accomplish that, but that's what I've been
13 hearing for four or five months.

14 Q. At this point what, if any, concern do you have,
15 Mr. Hazlip, that in the absence of a pooling order issued
16 reasonably quickly, that you have a real expectation of not
17 being able to fulfill your term assignment from Conoco?

18 A. I don't -- There's no way we would be able to
19 drill this well with 100-percent working interest without
20 getting something accomplished here quickly.

21 Not to mention the problem that -- We have the
22 problem with the interest, and then we also have the
23 problem of our drilling rigs. Those are scarce, and we've
24 had to move our drilling schedule around considerably at a
25 great deal of expense and possible penalties to the company

1 if we don't utilize the drilling rigs in the manner we say
2 we're going to when we contract these.

3 Q. Let's talk about your experience concerning
4 operating agreements in which you have participated as the
5 nonoperator concerning the risk factor penalty for
6 subsequent well operations. What's the general current
7 agreement range for that penalty factor in southeastern New
8 Mexico?

9 A. I would say generally, the average I see is about
10 a 400-percent nonconsent penalty, and that's for subsequent
11 operations, that's for low-risk operations.

12 Q. How long have you been a landman?

13 A. Thirteen years.

14 Q. When you first started back in -- what, late
15 Seventies, early Eighties? -- what was the custom and
16 practice in the industry for a risk-factor penalty for
17 subsequent well operations?

18 A. Three hundred percent.

19 Q. Making sure of terminology, when you're using a
20 300-percent risk factor penalty and operating agreement,
21 does that equate to what the Division understands when it
22 gives you cost plus 200 percent?

23 A. Yes, sir.

24 Q. And the current fashion in southeastern New
25 Mexico is higher than 300 percent?

1 A. Absolutely. It's generally -- It used to be 100
2 percent for surface equipment and 300 percent for
3 operations, drilling and completion operations, any other
4 subsequent operation. It's now 200 percent on surface
5 equipment and 400 percent, and more.

6 As a matter of fact, I just received a JOA from
7 Nearburg Producing for a 500-percent nonconsent penalty.

8 Q. In addition to escalating risk factors, has there
9 been an escalation of overhead rates?

10 A. Yes.

11 Q. Are those overhead rates utilized by your company
12 higher than those set forth in the tabulation by Ernst and
13 Young?

14 A. Yes, they are.

15 Q. What does your company utilize in this area for
16 overhead rates for wells at this depth?

17 A. I'll have to look at that. I believe that's
18 \$7145 for a drilling well rate and \$714 for a producing
19 well rate.

20 Q. Are you requesting that level of overhead be
21 applied in this pooling Application?

22 A. Yes, we are.

23 Q. Okay. Do you have other interest owners that
24 have committed to operating agreements that include these
25 type of overhead rates?

1 A. Yes, we do.

2 Q. Give us a short list of who the companies are and
3 the kind of wells that have been applied already on a
4 voluntary basis that utilize this rate.

5 A. This rate is used in a global fashion with --
6 under a JOA with AnSon Corporation. They have agreed to
7 this rate. Vestige Energies is agreeable to that rate, and
8 Northport Production Company. We're utilizing the same
9 rate with all those?

10 Q. And these are rates utilized for the Strawn oil
11 wells that you're exploring for in southeastern New Mexico?

12 A. Yes, right here in this area, that's correct.

13 Q. And how many wells have been drilled under these
14 other operating agreements, approximately?

15 A. Four or five wells.

16 Q. In summary, then, Mr. Hazlip, do you believe
17 you've exhausted all good-faith opportunities to achieve
18 voluntary agreement with Bristol?

19 A. Yes, sir.

20 MR. KELLAHIN: That concludes my examination of
21 Mr. Hazlip, Mr. Examiner.

22 Exhibit 12 is my affidavit of mailing
23 notification to Bristol of the hearing in compliance with
24 the notice rules. That's marked as Exhibit 12.

25 And at this point we would seek your permission

1 to introduce Chesapeake's Exhibits 1 through 12.

2 EXAMINER STOGNER: Exhibits 1 through 12 will be
3 admitted into evidence at this time.

4 EXAMINER STOGNER: Somewhere I've got confused on
5 the actual percentage that Bristol owned -- Before I do
6 that, do you have any questions, Mr. Owen?

7 MR. OWEN: Just a few, Examiner Stogner.

8 EXAMINER STOGNER: Please, please.

9 EXAMINATION

10 BY MR. OWEN:

11 Q. Mr. Hazlip, is it your opinion that you're not
12 going to be able to get voluntary agreement on this project
13 from Bristol?

14 A. Yes.

15 Q. Are you going to attempt to -- Are you going to
16 make any more attempts to receive voluntary joinder from
17 Bristol?

18 A. I'm waiting to hear from Bristol. It's in their
19 court right now.

20 Q. Are you aware that a typical compulsory pooling
21 order gives the force-pooled party 30 days from the date of
22 the order to voluntarily join a well?

23 A. We would be happy to have them participate.

24 Q. Have you provided any geologic information that
25 you have developed to Bristol --

1 A. No.

2 Q. -- in the course of your negotiations?

3 A. No, we haven't.

4 Q. You gave several opinions about the custom and
5 practice in the industry regarding nonconsent penalties in
6 joint operating agreements. Joint operating agreements are
7 agreements that all the parties to those agreements agree
8 to, aren't they?

9 A. Yes.

10 Q. They agree to the penalty that's contained in
11 that JOA; is that right?

12 A. (Nods)

13 Q. Bristol has not executed a JOA on this project,
14 have they?

15 A. No, they haven't.

16 Q. They haven't agreed to any risk penalty on this
17 project, have they?

18 A. They haven't agreed to anything.

19 Q. Under a typical JOA, parties are allowed to
20 review the records of the operator, aren't they?

21 A. Review the records?

22 Q. Yes.

23 A. What records?

24 Q. Whatever records that the operator has generated
25 for the particular project that falls under the JOA.

1 A. Under a JOA, if they had signed the JOA, they
2 would have the ability to audit our accounting records,
3 that sort of thing, if that's what you mean.

4 Q. Would they have access to your geologic
5 interpretation of the project area?

6 A. No, not necessarily. Not under the terms of the
7 JOA.

8 Q. Under the JOAs that you discussed earlier, would
9 the parties to those JOAs have access to the geologic
10 interpretation of the project areas?

11 A. No.

12 Q. Were you present for the first case that was
13 presented today, dealing with Manzano, Manzano special pool
14 rules, on the Wolfcamp?

15 A. No, sir, I wasn't.

16 Q. Are you aware that Manzano has operations in
17 adjoining sections to the section at issue in this project?

18 A. Yes.

19 Q. Have you reviewed any of Manzano's geologic
20 interpretation of -- or has Chesapeake reviewed any of
21 Manzano's geologic interpretation of the project area?

22 A. No, we have not reviewed any of Manzano's
23 geological interpretation, to my knowledge, now.

24 Q. Have you discussed this matter with any
25 representatives of Manzano?

1 A. What matter?

2 Q. This project, this particular well. Have you
3 discussed this matter with any representatives of Manzano?

4 A. No.

5 Q. When was the term assignment from Conoco
6 executed?

7 A. June 17th, 1997.

8 Q. Did Chesapeake have an interest in the area
9 before June 17th?

10 A. Yes.

11 Q. What was Chesapeake's interest before that? I
12 just -- I missed that.

13 A. It was under a separate term assignment. We had
14 a -- where 40 acres of the 80 acres was already granted to
15 us under a term assignment by Conoco two years ago. So
16 that was an existing interest we had.

17 The other 40 acres that is to go into this
18 proration unit was not assigned at that time. So this
19 covers the other 40 acres in the 80-acre proration unit.
20 And we had agreed with Conoco long before June 17th, the
21 day it was signed, that they would grant us a term
22 assignment.

23 Q. You proposed a well on April 23rd, you proposed a
24 well to Bristol on April 23rd, 1997; is that right?

25 A. April 24th to --

1 Q. 24th?

2 A. -- Bristol. Yes, sir.

3 Q. But you didn't have the term assignment from
4 Conoco until June 17th, right?

5 A. That's correct. We had a verbal with them.

6 Long before that I had told Conoco that we still
7 had to work up the Bristol interest and not to worry
8 about -- We knew that the term assignment would only give
9 us 90 days. I asked them to take their time on granting us
10 that term assignment in writing, and they did as I had
11 asked so that we would -- knowing that I had to work out
12 something with Bristol Resources, give me more time to work
13 out something with Bristol.

14 I was given every indication from Bristol that we
15 were going to be able to work something out.

16 Q. And on April 24th you sent a letter to Bristol
17 proposing terms that you thought you had agreed to in a
18 conversation with Ed Watts; is that right?

19 A. Yes.

20 Q. So you thought you had an agreement on April
21 24th?

22 A. No, I thought you were talking about the June
23 23rd letter, or the June 25th letter.

24 No, the April 24th letter was simply a drilling
25 well proposal and AFE.

1 Q. Oh, that was just the AFE?

2 A. Right.

3 Q. You thought you had an agreement on June 23rd,
4 right --

5 A. Yes.

6 Q. -- with Bristol?

7 And you received the term assignment from Conoco
8 on June 17th, right?

9 A. Yes, for the additional 40 acres. We had, two
10 years prior to that, already had 40 acres of the 80 tied up
11 from Conoco. This was on the additional 40 that makes up
12 the rest of the 80-acre proration unit.

13 MR. OWEN: That's all I have, thank you.

14 MR. KELLAHIN: Follow-up question, Mr. Examiner.

15 EXAMINER STOGNER: Mr. Kellahin?

16 FURTHER EXAMINATION

17 BY MR. KELLAHIN:

18 Q. Mr. Owen has talked to you about sharing
19 information. In fact, this prospect and other prospects by
20 Chesapeake in this area are being drilled by 3-D seismic
21 data, are they not?

22 A. Yes, sir.

23 Q. What is the practice of Chesapeake in relation to
24 sharing 3-D seismic data with an interest owner in a
25 spacing unit who has not voluntarily agreed in some fashion

1 to participate in the well?

2 A. We don't share our 3-D seismic.

3 Q. How do you go about advising people that you're
4 trying to attract into an area of exploration with the 3-D
5 seismic data? What's the process?

6 A. If we are -- the only way we have shown to date -
7 - The only way we've shown this data to those that are
8 participating with us is if they grant us an acreage
9 contribution with 50 to 75 percent of their interest. Then
10 we're generally willing to share our 3-D data with them,
11 knowing that they would -- are either granting us their
12 acreage or granting us a good portion of their acreage with
13 the right -- retaining the right to participate with a
14 portion of their interest. And we've done that in many
15 cases.

16 And we offered that to Bristol, and they
17 declined.

18 Q. The 3-D, then, is shown to interest owners only
19 after some commitment on participation in some fashion?

20 A. Yes, sir.

21 Q. You don't just show it to somebody that's not yet
22 committed?

23 A. That's correct.

24 Q. All right.

25 A. And on top of that, we don't necessarily show the

1 3-D data, even to those that participate in the well,
2 without getting some kind of an acreage contribution or
3 interest contribution from that company.

4 Q. All right, sir. And the Bristol interest that's
5 outstanding at this point in this spacing unit is a 25-
6 percent interest?

7 A. Yes, sir.

8 MR. KELLAHIN: All right, sir. No further
9 questions.

10 MR. OWEN: I have a couple follow-up questions,
11 Mr. Examiner.

12 EXAMINER STOGNER: Mr. Owen?

13 FURTHER EXAMINATION

14 BY MR. OWEN:

15 Q. You testified about a potentially appropriate
16 risk penalty. You're not basing that risk penalty on any
17 agreement that you have with Bristol, are you?

18 A. No.

19 Q. You're basing that on what Chesapeake appears --
20 or Chesapeake perceives to be the risk involved with this
21 project, right?

22 A. The risk penalty -- Are you talking about the
23 risk penalty in the JOA, or are you talking about the risk
24 penalty that the OCD allows for in their --

25 Q. You're requesting that the OCD impose a risk

1 penalty upon Bristol, because Chesapeake is taking a risk
2 in drilling this well, and Bristol hasn't voluntarily
3 agreed; isn't that right?

4 A. Yes, sir.

5 Q. And you base your assessment of risk upon that
6 3-D seismic; is that right?

7 A. On many things. 3-D seismic is just one factor
8 involved, and if I were asking for a reasonable amount of
9 risk, I would ask for more than the OCD allows.

10 Q. But you've asked for risk, based in part --
11 You're asked for a risk penalty based in part upon the 3-D
12 seismic and your interpretation of that 3-D seismic; isn't
13 that right?

14 A. I guess I would be asking for the same risk,
15 whether or not we had the 3-D seismic. If we didn't have
16 3-D seismic, I would certainly be asking for the maximum
17 amount of risk that the OCD would allow us.

18 And even with the 3-D seismic -- and our
19 geologist will get more into this -- there is an enormous
20 amount of risk even with the 3-D seismic, yes, sir. So
21 either way, I would be asking for 300-percent risk penalty.

22 MR. OWEN: Okay, thank you. That's all I have.

23 EXAMINER STOGNER: Mr. Kellahin --

24 MR. KELLAHIN: No, sir.

25 EXAMINER STOGNER: -- redirect?

1 Mr. Carroll?

2 EXAMINATION

3 BY MR. CARROLL:

4 Q. Mr. Hazlip, this issue is interesting. It's the
5 second time the Division has been presented with the same
6 issue in the last month.

7 In your experience in the industry, is it common
8 practice not to share such geologic information without
9 some commitment by the other party when you're trying to
10 get voluntary joinder in drilling a well?

11 A. Yes, it's standard not to. But we don't -- It's
12 industry standard practice not to share your 3-D seismic
13 with anybody without some --

14 Q. Without an agreement to participate or farm out,
15 one of the two, or some type of acreage contribution?

16 A. With that -- Well, I would say, I would limit
17 that more to without some kind of an acreage contribution.
18 As a matter of fact, I can't even recall a situation where
19 I have shown on -- from -- whatever company I was working
20 for at the time, I have not shown 3-D or shared 3-D seismic
21 with any company without them granting us a portion of
22 their interest.

23 Oftentimes what we do is -- and this with several
24 companies I've worked for -- give them the 3-D data
25 contingent upon them granting us a good portion of their

1 interest, and if they still want to have the right to
2 participate with a portion, then we grant -- then they're
3 allowed that right.

4 Sometimes it's -- they'll give us the -- all
5 their interest. They can view the 3-D data. That's fine
6 as long as we have the interest.

7 Sometimes we grant -- we give them the data for
8 50 to 75 percent of their interest, with their right to
9 participate after their viewing of the data and all that
10 with the additional.

11 If they don't participate, then they have the
12 commitment to farm out the rest of it to us on the same
13 basis as we got the first part of it.

14 Q. And I take it you develop or purchase such
15 information at substantial cost --

16 A. Yes.

17 Q. -- to your company?

18 A. Yes, it is substantial.

19 MR. CARROLL: That's all I have.

20 EXAMINER STOGNER: Thank you. Any other
21 questions?

22 MR. KELLAHIN: No, sir.

23 EXAMINATION

24 BY EXAMINER STOGNER:

25 Q. Do you want to repeat those overhead charges

1 again?

2 A. Those were seven thousand -- for a drilling well
3 rate, \$7145. And a producing well rate of \$714.50.

4 Q. Is this in line with the standard charges,
5 pursuant to the Ernst and Young publication?

6 A. I haven't looked at the Ernst and Young, but I'm
7 aware that they are higher than the Ernst and Young rates.

8 Q. Has Chesapeake participated with anybody else
9 that has charged these overhead charges in this area of Lea
10 County?

11 A. No, sir, we've -- and most of our drilling out
12 here, most of our participation, has been with us as
13 operator. And the reason we're submitting this number is
14 because this is the number that we have in the JOA with all
15 the other co-owners that are participating in this
16 particular well.

17 Q. And where did you come up with that number?

18 A. That number was established by our management
19 under an agreement with AnSon before I ever entered the
20 picture. They were under an exploration agreement with
21 AnSon in the area, and it was a number that AnSon had
22 agreed to.

23 EXAMINER STOGNER: Any other questions?

24 MR. KELLAHIN: No, sir.

25 EXAMINER STOGNER: You may be excused. Thank

1 you, Mr. Hazlip?

2 THE WITNESS: Thank you.

3 EXAMINER STOGNER: Mr. Kellahin?

4 MR. KELLAHIN: Mr. Examiner, we'll call Robert
5 Hefner. Mr. Hefner is a petroleum geologist.

6 MR. HEFNER: Good morning.

7 EXAMINER STOGNER: Hi.

8 MR. CARROLL: Good morning.

9 ROBERT A. HEFNER, IV,

10 the witness herein, after having been first duly sworn upon
11 his oath, was examined and testified as follows:

12 DIRECT EXAMINATION

13 BY MR. KELLAHIN:

14 Q. Mr. Hefner, on prior occasions have you testified
15 before the Division?

16 A. Yes, I have.

17 Q. And you testified in one of these hearings we had
18 to develop an 80-acre oil pool for Strawn exploration in
19 southeastern New Mexico?

20 A. I have.

21 Q. As part of your duties for Chesapeake, have you
22 been involved in exploration geology for these Strawn wells
23 in Lea County, New Mexico?

24 A. I have.

25 Q. Have you focused for your presentation today on

1 the question of the geologic risk involved concerning the
2 drilling of the Kim 1-1 well?

3 A. Yes, sir, I have.

4 MR. KELLAHIN: We tender Mr. Hefner as an expert
5 geologist.

6 EXAMINER STOGNER: Mr. Hefner is so qualified.

7 Q. (By Mr. Kellahin) Let's use for illustration
8 purposes of your testimony, Mr. Hefner, Exhibit Number 13.
9 Do you have a copy of that?

10 A. Yes, I do.

11 Q. Within the spacing unit in Section 1, there is an
12 area that's colored, and it has a certain size and a shape
13 to it. What's the significance of that size and shape?

14 A. That's our current interpretation of the algal
15 buildup representing a possible productive reservoir in the
16 proration unit that we're requesting under the Kim 1-1.

17 Q. When we're looking for Strawn oil production in
18 this portion of southeastern New Mexico, describe for us
19 what kind of critter this is. What's the deposition of the
20 Strawn, how was it formed, and how did we get these
21 accumulations of trapped hydrocarbons in the Strawn?

22 A. The Strawn reservoir is -- the present school of
23 thought is that these are algal buildups that nucleate on
24 some kind of existing topography and grow up against some
25 of the regional thicknesses and through that is then

1 subsequently exposed and which secondary processes occur to
2 provide a void space for porosity and permeability, and
3 they're often very small and isolated. As I've got
4 rendered here, it would be just a one-well field if it
5 does, indeed, exist.

6 It's far different from some of the other Strawn
7 that has been developed, say, by what you're most familiar
8 with recently, by Gillespie in the West Lovington, which
9 has a much greater areal extent.

10 Q. Gillespie-Crow's unit in West Lovington would be
11 highly unusual?

12 A. Yes, it is.

13 Q. In this portion of the exploration for Strawn,
14 they tend to be one- and maybe, at most, two-well pods?

15 A. Yes, sir. If you look at the historical
16 statistics on the Strawn to the southeast of where this
17 proposed location is, the average drainage area for
18 productive Strawn is 80 acres.

19 Q. Give us a sense of how the 3-D seismic data is
20 being utilized by you and other companies in this area to
21 explore for Strawn oil production.

22 A. Well, on this particular map that we're using as
23 Exhibit 13, we've got all the wells that have penetrated
24 the Strawn. And you can see on this map that we've had 18
25 wells that have tested the Strawn formation. And the bulk

1 of that activity was during the Eighties, although there
2 was an early well in 1959, drilled in Section 1 that was
3 actual Devonian test that penetrated the Strawn, but the
4 Strawn in that well was tight.

5 The second phase of drilling for Strawn
6 reservoirs in this area depicted by the map was
7 predominantly during the mid-Eighties. The success rates
8 for finding productive Strawn was only 40 percent. So 60
9 percent of the time they were dry holes.

10 Q. Now, in the Eighties we're using conventional
11 exploration techniques that don't include the 3-D seismic
12 efforts?

13 A. That's correct. If at all, they were probably
14 using 2-D seismic to try to delineate these mounds.

15 Q. In the Nineties, then, were other operators in
16 this area utilizing 3-D seismic data in trying to find
17 Strawn production?

18 A. Yes, sir, the most recent activity has been by a
19 company called Manzano who has shot a 3-D in this area, and
20 they've been attempting to develop Strawn reservoirs
21 utilizing their 3-D seismic. During 1996 and the early
22 part of this year, they've drilled a total of five wells
23 trying to find the Strawn, and out of those five wells,
24 only one has been productive.

25 So the success rate has not changed since the

1 mid-Eighties, utilizing the 3-D seismic.

2 Q. Let's find the five wells Manzano is using 3-D
3 seismic on, and then we'll find the one of the five that
4 was successful.

5 A. Okay, most of the wells are located in Section
6 11. They have the names Chipshot 1-11, the Chipshot 2-11,
7 and then the Double Eagle 1-11, as you go to the northeast
8 there.

9 Then in Section 2 would be their most recent
10 attempt, called the Killer Bee. And then a well that was
11 drilled just prior to that was in Section 12, called the
12 Kim Harris Number 3. That was a productive Strawn test
13 that had an IP of 135 barrels of oil from the Strawn, which
14 is located in between two dry holes in the Strawn, even on
15 that 180. You had a well that was drilled in 1990 by
16 Bridge called the Kim Harris 1-12 that found tight Strawn.
17 And then Manzano tried in 1995 to drill another one on that
18 80, called the Kim Harris Number 2. It again found tight
19 Strawn.

20 Later, a company by the name of Middle Bay
21 attempted a re-entry into that well, drilled about 400 --
22 sidetracked 400 feet north. Still dry.

23 Manzano just here recently in 1997 drilled the
24 Kim Harris Number 3 and found some Strawn tucked in between
25 those two wells.

1 Q. Which of the five Manzano efforts was the
2 successful effort?

3 A. It was that Kim Harris Number 3.

4 Q. Okay. Let's look in that vicinity. In 1990, the
5 Kim Harris 1-12 was unsuccessful. Describe for us this
6 area of attempts to find the Strawn in the close proximity
7 of these wells and still the continuation of failure.

8 A. The wells that have been successful do not number
9 very many. Besides that Kim Harris Number 3, there's
10 another well in Section 12, called the State 12, drilled by
11 Matador in 1989. That well found productive Strawn, had a
12 cumulative production of 126,537 barrels, some gas and also
13 some water. It's been inactive since December of 1996.

14 The other successful wells, there's one in
15 Section 6 called the Anderson 6 that cum'd 58,675 barrels
16 of oil and 10,000 barrels of water and some gas. It's been
17 inactive since November of 1996.

18 The other successful attempt is a well in Section
19 1 called the Anderson. It has cum'd since 1987 only 87,000
20 barrels.

21 So those that have been successful have not been
22 even -- real successful, averaging around 90,000 barrels
23 per well, which is not too much more than just paying out
24 for the activity.

25 Q. All right. So in terms of costs and price for

1 oil, you need about 90,000-plus, just to get your money
2 back?

3 A. That's correct.

4 Q. Ninety-thousand-plus barrels?

5 A. Uh-huh.

6 Q. Okay. Summarize for us, then, your opinion as to
7 an appropriate risk-factor penalty. What is that, sir?

8 A. It would be the maximum allowed by New Mexico.

9 Q. And the reasons that support that would be -- ?

10 A. That we have seen even less -- utilizing 3-D,
11 that it has not increased the success rate, so it has not
12 improved your risk profile. And even on the spacing that
13 some of these have been drilled, even that has not improved
14 the success rate in the area.

15 MR. KELLAHIN: That concludes my examination of
16 Mr. Hefner.

17 We move the introduction of his Exhibit 13.

18 EXAMINER STOGNER: Exhibit Number 13 will be
19 admitted into evidence.

20 Thank you, Mr. Kellahin.

21 Mr. Owen, your witness.

22 MR. OWEN: Thank you, Mr. Examiner.

23 EXAMINATION

24 BY MR. OWEN:

25 Q. You say that your 3-D seismic has not improved

1 your risk profile. Have you utilized your 3-D seismic data
2 in your diagram or in your chart, which is Chesapeake
3 Exhibit Number 13?

4 A. Yes, it has been utilized, and it's helped us
5 with the bias of that geometry that you see on that map.

6 Q. But it hasn't improved the risk profile at all;
7 is that right?

8 A. In this area the only activity by anyone
9 utilizing 3-D has been Manzano, and I'm basing it on their
10 activity. We have drilled elsewhere; we have not drilled
11 in this area utilizing 3-D.

12 And even in the areas where we have drilled
13 wells, we have drilled several that have not found
14 productive Strawn. The two of them missed, and one had a
15 high water cut to them.

16 So there's still risk, 3-D does not remove the
17 risk. There's still interpretation risk utilizing these
18 tools.

19 Q. Have you seen Manzano's 3-D data?

20 A. No, sir, I have not.

21 Q. What other data did you use besides the 3-D to
22 compile Exhibit Number 13?

23 A. It's based predominantly on the 3-D.

24 Q. On the 3-D seismic?

25 A. Yes, sir.

1 Q. You haven't made that 3-D seismic data available
2 to Bristol, have you?

3 A. No, we have not. Generally, we spend quite a lot
4 of money on these 3-Ds, we risk a lot of money even before
5 we even know whether we're going to be able to drill a
6 well. And so in order to do that, we'd like other
7 companies to share in that risk.

8 Q. So you're basing your assessment of the risk
9 involved in this project upon your 3-D seismic results, on
10 one hand, and the lack of success in the Strawn production
11 on the other hand; is that right?

12 A. Ask the question again. I'm not sure if I
13 understood --

14 Q. You're basing your assessment of the risk
15 involved in this particular well upon your 3-D seismic
16 interpretation on the one hand, and the lack of success in
17 other Strawn exploration on the other hand; is that right?

18 A. We have not drilled a well in this area, and so
19 until we drill this well I'm not sure how well my
20 interpretation will hold up, so...

21 Q. But other companies haven't been all that
22 successful in the Strawn?

23 A. No, they have not. It's a very difficult
24 reservoir to explore for, even with 3-D.

25 Q. Even with the benefit of Strawn -- of 3-D

1 seismic, it's still --

2 A. That's correct.

3 Q. -- pretty risky?

4 A. That's -- As you can see, this is around 11,500
5 feet in depth. You're averaging a lot of rock with
6 seismic. There's a lot of interpretation risk.

7 Q. Have you prepared any cross-sections of this
8 area?

9 A. No, I have not.

10 Q. Have you prepared any other diagrams of this area
11 based on a 3-D seismic, for your own -- for your internal
12 purposes?

13 A. What you see here is what I've prepared.

14 Q. This is the only geologic interpretation that
15 Chesapeake has used to base their decision to drill their
16 well?

17 A. It's based on our interpretation, so there's
18 backup to where that interpretation came from. But this is
19 the end result of that interpretation.

20 Q. Are there other charts, diagrams, anything else
21 that's been produced from the raw 3-D data?

22 A. It's all -- It's on the workstation, if that's
23 what you're trying to get to.

24 Q. It's all --

25 A. We do -- we do --

1 Q. It's all on your computer?

2 A. That's correct.

3 Q. You have --

4 A. The 3-D seismic does cover this area.

5 Q. But you do have interpretations of the 3-D
6 seismic on your computer that are --

7 A. Sure.

8 Q. -- that are not the raw 3-D data; is that right?

9 A. I'm not sure if I understand the question.

10 Q. I mean, you've got the raw -- And I'm not
11 completely clear on this 3-D anyway, but you've got the raw
12 3-D data after you shoot the seismic; is that right?

13 A. Correct.

14 Q. And you produce interpretations of that data --

15 A. It's been --

16 Q. -- that you present to your management?

17 A. It's been loaded on the workstation, and I have
18 interpreted that data volume, and it is on the workstation,
19 and this is a result of that interpretation that's on this
20 map.

21 Q. Is this the only interpretation of that that
22 you've presented to your management?

23 A. I don't even know if they've even had this. We
24 don't have a formal structure -- that's where you're --

25 Q. Yeah, that's where I'm going.

1 A. -- presentation, no, it's very informal, and...

2 MR. OWEN: Okay. All right, that's all I have.

3 EXAMINER STOGNER: Mr. Kellahin, any redirect?

4 MR. KELLAHIN: No, sir.

5 EXAMINER STOGNER: Mr. Carroll?

6 EXAMINATION

7 BY EXAMINER STOGNER:

8 Q. Referring to that Butler Anderson well --

9 A. In Section 1?

10 Q. Yes, up to the north of your proposed well.

11 A. Yes, sir.

12 Q. Now, is that well presently producing?

13 A. I show it as inactive. If it is, it's
14 subeconomic. I don't know if it's -- It may still be
15 holding. I have not dug into its current status, whether
16 it's holding that spacing unit still or not, but --

17 MR. HAZLIP: My understanding --

18 MR. KELLAHIN: Wait --

19 MR. HAZLIP: -- it's still holding --

20 MR. KELLAHIN: One testifier at once.

21 Q. (By Examiner Stogner) And whose well was it?

22 A. It was originally drilled by a company called
23 Esteril. It is now operated by a company called Butler.

24 Q. I'm sorry, what?

25 A. Butler.

1 Q. Butler.

2 A. As you can see by the initial potential that's on
3 that map, it wasn't real good potential to begin with and
4 has only cum'd 87,000 barrels.

5 Q. And your interpretation would be that that
6 production would not be part of the algal mound in which
7 you have interpreted as under your property?

8 A. No, it would not be.

9 EXAMINER STOGNER: Any other questions of this
10 witness?

11 MR. KELLAHIN: No, sir.

12 EXAMINER STOGNER: Anything further, Mr.
13 Kellahin?

14 MR. KELLAHIN: I have nothing further, Mr.
15 Examiner.

16 EXAMINER STOGNER: Mr. Owen, do you have anything
17 further in this matter?

18 MR. OWEN: I don't have any witnesses. I would
19 like to make a statement.

20 EXAMINER STOGNER: Okay. Mr. Owen, you may go
21 ahead and make a statement.

22 MR. OWEN: Mr. Examiner, Chesapeake comes before
23 you today and requests that you enter a 200-percent
24 penalty, based on two factors. First, on the fact that, in
25 Chesapeake's experience, joint operating agreements

1 typically have at least a 200-percent -- cost-plus-200-
2 percent penalty provision. And second, based on their
3 geologic interpretation of the area.

4 As to the first basis for Chesapeake's request
5 for a 200-percent penalty, as you know, a joint operating
6 agreement is just that. It's an agreement between the
7 parties to develop a certain area. If the parties, after
8 agreeing to that development, refuse to consent to a
9 particular project, they agree to a penalty against
10 themselves. Bristol has not agreed to that penalty.

11 What Chesapeake is requesting is that you invoke
12 the police power of the State to impose that penalty upon
13 Bristol.

14 And the factors that you've been shown to support
15 that is a single geological interpretation of 3-D seismic.

16 What Bristol has been asked to do is to join a
17 project without knowing the risks that are involved.
18 They've been asked to trust Chesapeake.

19 As you know, 3-D seismic is a relatively recent
20 innovation in this area, and all the companies are still
21 trying to figure out how to use it in conjunction with each
22 other and in trying to get other companies to join with
23 them in projects.

24 Bristol hasn't seen the 3-D seismic. Chesapeake
25 won't show them the 3-D seismic. Bristol has no idea how

1 to assess the risk involved with this particular project.
2 They've just been asked to trust Chesapeake on this one.

3 Chesapeake has made a calculated decision to
4 drill this well, and they have made the conclusion that is
5 a very risky well, even with the benefit of 3-D seismic.

6 From Bristol's perspective, they don't know
7 whether to join. It's even more of a risk, from their
8 perspective, without the benefit of reviewing the 3-D
9 seismic.

10 Bristol's being asked to commit significant
11 resources to a project without having the education
12 necessary to make an educated guess, an educated decision
13 about whether this is an appropriate project.

14 While Bristol does not challenge Chesapeake's
15 land or geologic interpretation, Bristol does request that
16 if you see it appropriate to impose -- to force-pool
17 Bristol's interest into this project, that you not impose a
18 risk penalty upon Bristol.

19 That's all I have.

20 EXAMINER STOGNER: Thank you, Mr. Owen.

21 Mr. Kellahin?

22 MR. KELLAHIN: Mr. Examiner, back in 1977 when we
23 were putting on pooling cases to your predecessor, the risk
24 factor penalty in the statute was 50 percent.

25 At that time, I and others appearing before the

1 agency persuaded the Division to recognize that the
2 industry standard of common practice of agreement was
3 substantially higher than the statutory limit. And at that
4 point in time the custom and practice in the industry was
5 to utilize 200 percent, cost plus 200 percent, the 300-
6 percent number.

7 That has been some 20 years ago.

8 The point here to be made is that the current
9 maximum you're allowed to utilize is substantially less
10 than what operators and interest owners in these areas of
11 development are utilizing for themselves. Simply a point
12 of perspective about the maximum you are allowed to
13 authorize.

14 For some five months now, Mr. Hazlip has been
15 negotiating with Bristol, and they continue to drag their
16 feet. If Bristol wants to share the risk of the seismic
17 play, they have been afforded opportunities to participate
18 by paying, acquiring or committing in order to share that
19 data. They can develop their own seismic data. They can
20 make their own interpretation.

21 Be that as it may, you can see that Manzano, a
22 competitor in the area utilizing 3-D seismic work,
23 demonstrates a one-out-of-five success ratio. It's
24 incredibly risky.

25 Therefore, we think the maximum is justified.

1 We've afforded Bristol the opportunity to
 2 participate, to farm out, and to come join us in this risky
 3 effort. If they choose not to do so, then their 25 percent
 4 comes out of Chesapeake's pocket. It comes out of
 5 Chesapeake's funds. And we pay their share. And as a
 6 consequence for that risk we ought to be entitled to
 7 receive out of production, if we're successful, not only
 8 their share of the costs but a penalty factor as well.

9 I suspect that the penalty probably will never
 10 pay out. You can see how small these pods are. They're
 11 one-well pools. And the risk is appropriate for the
 12 maximum that you're allowed. And even then, we are at
 13 risk.

14 We ask that you enter an order as requested with
 15 the maximum penalty and let us go on our business before
 16 our term assignment from Conoco expires in October and,
 17 through Bristol's delay, we are precluded from this
 18 exploration.

19 Thank you.

20 EXAMINER STOGNER: Thank you, Mr. Kellahin.

21 Case Number 11,836 will be taken under
 22 advisement.

23 (Thereupon, these proceedings were concluded at
 24 11:01 a.m.)

I do hereby certify that the foregoing is
 a complete record of the proceedings in
 the Examiner hearing of Case No. 11836.
 * * * heard by me on 21 August 1997.

STEVEN T. BRENNER, COB, Examiner
 Oil Conservation Division
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