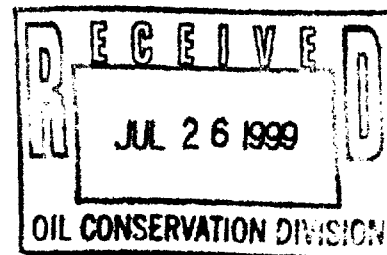


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July 26, 1999

Hand Delivered

Michael E. Stogner
Oil Conservation Division
2040 South Pacheco Street
Santa Fe, New Mexico 87505

Re: Case 12171 (West Lovington Strawn Unit expansion)

Dear Mr. Stogner:

Enclosed is a draft order in the above matter, on hard copy and disc (Wordperfect 5.1). This order sets forth the "technical committee" proposal.

Very truly yours,

A handwritten signature in cursive script, appearing to read "Jim Bruce".

James Bruce

Attorney for Gillespie Oil, Inc.

cc: Counsel of record (w/encl.)

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. 12171
ORDER NO. R-_____

APPLICATION OF GILLESPIE OIL, INC. FOR
UNIT EXPANSION, STATUTORY UNITIZATION,
AND QUALIFICATION OF THE EXPANDED UNIT
AREA FOR THE RECOVERED OIL TAX RATE AND
CERTIFICATION OF A POSITIVE PRODUCTION
RESPONSE PURSUANT TO THE "NEW MEXICO
ENHANCED OIL RECOVERY ACT," LEA COUNTY,
NEW MEXICO.

ORDER OF THE DIVISION

BY THE DIVISION:

This cause came on for hearing at 8:15 a.m. on May 27, 1999,
at Santa Fe, New Mexico, before Examiner Michael E. Stogner.

NOW, on this _____ day of _____, 1999, the Division
Director, having considered the testimony, the record, and the
recommendations of the Examiner,

FINDS THAT:

(1) Due public notice having been given as required by law,
the Division has jurisdiction of this cause and the subject matter
thereof.

(2) By Order No. 10449 entered in Case No. 11194 on August
29, 1995, the Division, upon the application of Gillespie-Crow,
Inc. (the predecessor to Gillespie Oil, Inc.), approved the
statutory unitization, pursuant to the Statutory Unitization Act,
NMSA 1978 Sections 70-7-1 through 70-7-21, of the following
described 1458.95 acres, more or less, of State, Federal, and Fee
lands in the West Lovington-Strawn Pool, Lea County, New Mexico:

WEST LOVINGTON STRAWN UNIT AREA

TOWNSHIP 15 SOUTH, RANGE 35 EAST, NMPM

Section 33: All
Section 34: W½

TOWNSHIP 16 SOUTH, RANGE 35 EAST, NMPM

Section 1: Lots 1 through 8

TOWNSHIP 16 SOUTH, RANGE 36 EAST, NMPM

Section 6: Lots 3 through 5

The unit became effective on October 1, 1995.

(3) By Order No. R-10448 entered in Case No. R-10448 on August 29, 1995, the Division authorized Gillespie-Crow, Inc. to institute a pressure maintenance project within the West Lovington Strawn Unit, hereinafter referred to as the WLSU, by the injection of gas into the Strawn formation, West Lovington-Strawn Pool, through the perforated interval from approximately 11,424 feet to 11,434 feet in its Speight Fee Well No. 1, located 660 feet from the North line and 2310 feet from the West line (Unit C) of Section 1, Township 16 South, Range 35 East, NMPM.

(4) By Order No. R-10864 entered in Case No. 11724 on August 27, 1997, the Division, upon the application of Gillespie-Crow, Inc., approved the expansion of the horizontal boundaries of the WLSU by statutorily unitizing, pursuant to the Statutory Unitization Act, an additional 160 acres, more or less, of State and Fee lands in the West Lovington-Strawn Pool, described as follows:

TOWNSHIP 15 SOUTH, RANGE 35 EAST, NMPM

Section 28: S½SE¼
Section 34: W½SE¼

The expanded unit area contains 1618.95 acres, more or less. The vertical limits of the expanded WLSU are defined in Decretory Paragraph No. (3) of Order No. R-10449, which was incorporated in Order No. R-10864 by reference. In addition, the secondary recovery project for the expanded unit area was approved. The unit expansion became effective on November 1, 1997.

(5) Order No. R-10862 established the following tract participations in the expanded unit area:

<u>TRACT NUMBER</u>	<u>PARTICIPATION</u>
1-11	95.2797924%
12	2.3161519%
13	2.1147842%
14	<u>0.2892715%</u>
	100.0000000%

(6) The tract participation formula used for the initial unit area and the first unit expansion is set forth in Section 13 of the Unit Agreement, and was based on hydrocarbon pore volume underlying a tract, less production through May 1, 1995.

(7) The applicant in the present case, Gillespie Oil, Inc., seeks to expand the horizontal boundaries of the WLSU by statutorily unitizing, pursuant to the Statutory Unitization Act, an additional 1123.95 acres, more or less, of State and Fee lands in the West Lovington-Strawn Pool, described as follows:

TOWNSHIP 15 SOUTH, RANGE 35 EAST, NMPM

Section 28: S $\frac{1}{2}$ SW $\frac{1}{4}$
 Section 32: E $\frac{1}{2}$ NE $\frac{1}{4}$
 Section 34: NE $\frac{1}{4}$ and E $\frac{1}{2}$ SE $\frac{1}{4}$
 Section 35: SW $\frac{1}{4}$

TOWNSHIP 16 SOUTH, RANGE 35 EAST, NMPM

Section 1: Lots 9-12

TOWNSHIP 16 SOUTH, RANGE 36 EAST, NMPM

Section 5: Lots 3-6
 Section 6: Lots 1, 2, 6, 7, and 8

(8) The applicant requested that Section 13 of the Unit Agreement, regarding tract participations, be revised for the expanded unit area as described in Exhibit A attached hereto. Hydrocarbon pore volume was calculated based on the map submitted at hearing as Gillespie Oil, Inc. Exhibit No. 3. The tract participations for the expanded unit area are described on Exhibit B attached hereto, which shall be contained in revised Exhibit "C" to the Unit Agreement.

(9) In addition, the applicant proposed that Section 16 of the Unit Agreement be revised to include a new paragraph, described in Exhibit C attached hereto. Such provision is necessary to ensure that the working interest owners who paid for injected gas recover their proportionate share of such gas ultimately produced, and should be approved. As of November 1, 1997, 3,646,566 mcf of gas had been injected into the Unitized Formation.

(10) The applicant further seeks to qualify the expanded unit area for the recovered oil tax rate pursuant to the "Enhanced Oil Recovery Act" (Laws 1992, Chapter 38, Sections 1 through 5), and that the following two wells, located on the tracts to be added to the WLSU, be certified as having a positive production response:

(a) The Snyder "EC" Com. Well No. 1, located in Lot 2 of Section 6, Township 16 South, Range 36 East, NMPM; and

(b) The Snyder "C" Well No. 4, located in Lot 1 of Section 6, Township 16 South, Range 36 East, NMPM.

(11) At the hearing in this matter, Energen Resources Corporation ("Energen"), Yates Petroleum Corporation ("Yates"), and Hanley Petroleum, Inc. ("Hanley") entered appearances in support of unit expansion. David H. Arrington Oil & Gas, Inc. entered an appearance in opposition to the inclusion of proposed Unit Tract 24 in the WLSU. Charles B. Gillespie entered an appearance in support of unit expansion, but proposing a smaller expansion, and also proposing an amendment to Article 10.4 of the Unit Operating Agreement. Snyder Ranches, Inc. ("Snyder Ranches"), a royalty owner, also entered an appearance in this matter.

(12) The evidence presented at hearing shows that:

(a) Order No. R-10864 was the subject of a *de novo* appeal to the Oil Conservation Commission, held on August 12, 1999, and the record in that case is incorporated herein by reference. The record shows that:

(i) Hanley has requested that Unit Tract 15 be brought into the unit effective November 1, 1997.

(ii) Tract 15 has hydrocarbon pore volume underlying it, and should have been brought into the unit in 1997.

(iii) In order to protect correlative rights and prevent waste, Tract 15 shall be incorporated into the unit area effective November 1, 1997, and Tracts 14 and 15 shall have jointly allocated to them a 0.2892715% tract participation for the period from November 1, 1997 to April 1, 1999.

(b) After the unit was expanded, the Snyder "C" Well No. 4 was drilled and completed in the West Lovington-Strawn Pool.

(c) At a November 1998 working interest owner's meeting, additional pressure testing of the reservoir was authorized, and a technical committee was formed to consider new reservoir data and unit expansion.

(d) The technical committee met five times during the next several months. The committee determined that the Snyder "C" Well No. 4 was in pressure communication with the unit's reservoir, and also reconsidered the status of the Snyder "EC" Com. Well No. 1. The committee subsequently proposed unit expansion as proposed on Gillespie Oil, Inc. Exhibit No. 3.

(e) The Strawn formation underlying the expanded unit area, as proposed by the applicant, has been reasonably defined by development, as required by the Statutory Unitization Act.

(f) As of May 1, 1999 the unit had produced 3.85 million barrels of oil and had injected 6.51 BCF of gas, and pressure decline in the reservoir had been substantially arrested. The WLSU has instituted a highly successful pressure maintenance project which has benefitted the West Lovington-Strawn Pool and the interest owners therein.

(13) The unitized management, operation, and further development of the Strawn formation underlying the expanded unit area is reasonably necessary in order to effectively carry on pressure maintenance operations and to substantially increase the ultimate recovery of oil and gas therefrom.

(14) The existing pressure maintenance operation, as applied to the Strawn formation underlying the expanded unit area, is feasible, will prevent waste, and will result with reasonable probability in the increased recovery of substantially more oil from the Strawn formation than would otherwise be recovered.

(15) The estimated additional costs, if any, of conducting unitized operations will not exceed the estimated value of the additional oil recovered thereby, plus a reasonable profit.

(16) A good faith effort has been made to secure voluntary unitization of the Strawn formation underlying the expanded unit area.

(17) The tract participation formula in the Unit Agreement for the WLSU allocates produced and saved unitized hydrocarbons to the separate tracts in the expanded unit on a fair, reasonable, and equitable basis.

(18) Unitization and adoption of the current unitized methods of operation will benefit the working, royalty, and overriding royalty interest owners of the oil and gas rights within the expanded WLSU.

(19) The plan of unitization for the expanded unit area, embodied in the Unit Agreement approved by the Division in Case No. 11195 (Order No. R-10449), as modified by revised Section 13, Section 16, and Exhibits "A", "B", and "C" thereto, which agreement

is incorporated herein by reference, is fair, reasonable, and equitable.

(20) The operating plan for the expanded unit area, covering the manner in which the expanded unit area will be supervised and managed, and costs allocated and paid, is embodied in the Unit Operating Agreement approved by the Division in Case No. 11195 (Order No. R-10449), which agreement is incorporated herein by reference.

(21) The West Lovington Strawn Unit Agreement, as amended, as applied to the expanded unit area, provides for unitization of the West Lovington Strawn Unit Area upon terms and conditions that are fair, reasonable, and equitable, and which include:

(a) an allocation as to the separately owned tracts in the expanded unit area of all oil and gas that is produced from the expanded unit area and which is saved, being the production that is not used in the conduct of unit operations or not unavoidably lost;

(b) a provision for the credits and charges to be made and the adjustments among the owners in the expanded unit area for their respective investments in wells, tanks, pumps, machinery, materials, and equipment contributed to unit operations;

(c) a provision governing how the costs of unit operations, including capital investments, shall be determined and charged to the separately owned tracts and how said costs shall be paid, including a provision providing when, how, and by whom the unit production allocated to an owner who does not pay his share of the costs of unit operation shall be credited to such owner, or the interests of such owner, and how his interest may be sold and the proceeds applied to the payment of his costs;

(d) a provision for carrying any working interest owner on a limited, carried, or net-profits basis, payable out of production, upon terms and conditions which are just and reasonable, and which allow an appropriate charge for interest for such service payable out of production, upon such terms and conditions determined by the Division to be just and reasonable, and providing that any non-consenting working interest owner being so carried shall be deemed to have relinquished to the unit operator all of his operating rights and working interest in and to the unit until his share of the costs, service charge, and interest are repaid to the unit operator;

(e) a provision designating the unit operator and providing for the supervision and conduct of unit operations, including

the selection, removal, or substitution of an operator from among the working interest owners to conduct unit operations;

(f) a provision for a voting procedure for the decision of matters to be decided by the working interest owners in respect to which each working interest owner shall have a voting interest equal to his unit participation; and

(g) the time when unit operations shall commence and the manner in which, and the circumstances under which, unit operations shall terminate and for the settlement of accounts upon such termination.

(22) The applicant requested that a 200% penalty be assessed against those working interest owners who do not voluntarily agree to join the proposed unit.

(23) Section 70-7-7.F of the Statutory Unitization Act provides that the unit plan of operation shall include a provision for carrying any working interest owner subject to limitations set forth in the statute, and any non-consenting working interest owner so carried shall be deemed to have relinquished to the unit operator all of his operating rights and working interest in and to the unit until his share of the costs has been repaid plus an amount not to exceed 200 percent thereof as a non-consent penalty.

(24) Applicant's Unit Operating Agreement contains a provision whereby any working interest owner who elects not to pay his share of unit expense shall be liable for his share of such unit expense plus an additional 200 percent thereof as a non-consent penalty, and that such costs and non-consent penalty may be recovered from each non-consenting working interest owner's share of unit production.

(25) A non-consent penalty of 200 percent should be adopted in this case. The applicant should be authorized to recover from unit production each non-consenting working interest owner's share of unit expense plus 200 percent thereof.

(26) The statutory unitization of the expanded WLSU is in conformity with the above findings, and will prevent waste and protect the correlative rights of all interest owners within the proposed unit, as expanded, and should be approved.

(27) The additional wells within the proposed expanded unit area are entitled to be qualified for the recovered oil tax rate and certified for a positive production response. These wells, and the acreage dedicated thereto, are as follows:

WELL NAME

WELL UNIT

Snyder "EC" Com. Well No. 1
(WLSU Well No. ____)

WLSU Tracts 16A and
16B

Snyder "C" Well No. 4
(WLSU Well No. ____)

WLSU Tract 17

IT IS THEREFORE ORDERED THAT:

(1) The expanded West Lovington Strawn Unit Area, comprising 2742.90 acres, more or less, of State, Federal, and Fee lands in the West Lovington-Strawn Pool, Lea County, New Mexico, is hereby approved for statutory unitization pursuant to the Statutory Unitization Act, NMSA 1978 Sections 70-7-1 through 70-7-21.

(2) The lands included within the expanded West Lovington Strawn Unit Area shall comprise:

EXPANDED WEST LOVINGTON STRAWN UNIT AREA

TOWNSHIP 15 SOUTH, RANGE 35 EAST, NMPM

Section 28: S $\frac{1}{2}$ S $\frac{1}{2}$
Section 32: E $\frac{1}{2}$ NE $\frac{1}{4}$
Section 33: All
Section 34: All
Section 35: SW $\frac{1}{4}$

TOWNSHIP 16 SOUTH, RANGE 35 EAST, NMPM

Section 1: Lots 1-12

TOWNSHIP 16 SOUTH, RANGE 36 EAST, NMPM

Section 5: Lots 3-6
Section 6: Lots 1-8

(3) Tract 15 shall be included in the unit effective November 1, 1997, and unit expansion shall otherwise be effective as of April 1, 1999.

(4) The vertical limits of the expanded West Lovington Strawn Unit Area are described in Decretory Paragraph No. (3) of Order No. R-10449, which is incorporated herein by reference.

(5) The secondary recovery project for the expanded unit is hereby approved. The transfer of allowables between wells in the expanded project area should be permitted.

(6) The West Lovington Strawn Unit Agreement and the West Lovington Strawn Unit Operating Agreement, approved by Division Order No. R-10449, as modified by the revised Section 13, Section 16, and Exhibits "A", "B", and "C" thereto, are incorporated by reference into this order.

(7) The tract participations for the expanded West Lovington Strawn Unit Area are hereby established as described on Exhibit C attached hereto.

(8) The Unit Agreement approved by Order No. R-10449, as amended by revised Section 13, Section 16, and Exhibits "A", "B", and "C" thereto, and the Unit Operating Agreement for the West Lovington Strawn Unit provide for unitization and unit operation of the expanded Unit Area upon terms and conditions that are fair, reasonable, and equitable, and which include the provisions described in Finding Paragraph No. (21) above.

(9) This order shall not become effective unless and until the owners of seventy-five (75) percent of the working interest and seventy-five percent (75) of the royalty interest in the expanded West Lovington Strawn Unit have approved the plan for unit operations as required by NMSA 1978 Section 70-7-8.

(10) If the persons owning the required percentage of interest in the expanded West Lovington Strawn Unit Area as set out in NMSA 1978 Section 70-7-8 do not approve the plan for unit operations within 6 months from the date of entry of this order, this order shall cease to be of any further force and effect and shall be revoked by the Division, unless the Division shall extend the time for good cause shown. Any failure to obtain the required percentage approval shall not affect the validity of Order Nos. R-10448, R-10449, and R-10864 as they are in effect prior to the date of this order.

(11) When persons owning the required percentage of interest in the expanded West Lovington Strawn Unit Area have approved the plan for unit operations, the interests of all persons in the expanded unit area are unitized whether or not such persons have approved the plan of unitization in writing.

(12) The applicant as Unit Operator shall notify the Division Director of any removal or substitution of said Unit Operator by any working interest owner within the expanded Unit Area.

(13) A non-consent penalty of 200 percent is hereby adopted in this case. The applicant shall be authorized to recover from unit production each non-consenting working interest owner's share of unit expense plus 200 percent thereof.

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

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

STATE OF NEW MEXICO
OIL CONSERVATION DIVISION

LORI WROTENBERY
Director

EXHIBIT A

Case No. 12171
Order No. R-_____

SECTION 13. TRACT PARTICIPATION (EXPANDED UNIT). The percentages of Tract Participation for each Tract within the Unit Area have been calculated and determined in accordance with the following formulas:

1. October 1, 1995 - October 31, 1997 (Original Unit).

Tract Participations for Tracts 1-11 (the original Unit Area) are those calculated under the Unit Agreement, as approved and amended by Division Order No. R-10449.

2. November 1, 1997 - March 31, 1999 (First Expansion).

Tract Participations for this period are those approved by Division Order No. R-10864, as follows:

Tracts 1-11:	95.2797924%
Tract 12:	2.3161519%
Tract 13:	2.1147842%
Tract 14:	0.2892715%

Production allocated to Tracts 1-11 was apportioned among said Tracts in the proportions set forth in Division Order No. R-10449.

There shall be no retroactive changes in Tract Participations or in allocation of production of Unitized Substances for any period prior to April 1, 1999.

3. Effective April 1, 1999 (Second Expansion).

(a) Tract Participation Percentage = $(80\% \times \text{HPV}) + (20\% \times \text{WF})$, where:

HPV = Hydrocarbon Pore Volume: Determined by volumetric original oil in place in the Unitized Formation under each Tract divided by volumetric original oil in place in the Unitized Formation under the expanded Unit Area.

Original oil in place is calculated from hydrocarbon pore volume using 100% of the density porosity electric log response with a 3% porosity cutoff, with an $R_w = 0.48$.

WF = Wellbore Factor: Determined by (i) the number of wells on a Tract, (ii) multiplied by the maximum average daily producing rate during a consecutive six (6) month producing period divided by the allowable for the West Lovington-Strawn Pool (250 BOPD/well), (iii) divided by the cumulative sum of all Well Factors in the Unit Area.

Tracts 1-11 shall have a cumulative Wellbore Factor of 11 assigned thereto.

(b) Tract Participations for Tracts 12-14 shall be calculated under the subparagraph (a) formula for the period commencing April 1, 1999.

The participations for each Tract in the expanded Unit Area are set forth in Exhibit "C" (Second Revision) to the Unit Agreement.

The Tract Participation percentages have been calculated upon the basis of all Tracts within the Unit Area, as expanded, being committed to this Agreement as of the effective date of unit expansion (being April 1, 1999), and such Tract Participations shall govern the allocation of Unitized Substances produced from the Unit Area after April 1, 1999; subject, however, to any revisions of the Unit Area and Exhibit "C" (Second Revision) in accordance with the provisions hereof.

If, subsequent to the effective date of unit expansion, any additional tract becomes committed hereto under the provisions of Section 4 (Expansion), Unit Operator shall revise Exhibits "B" and "C," or the latest revisions thereof, to show the new percentage participations of the then committed tracts, which revised exhibits shall, upon their approval by the Commissioner, Authorized Officer, and Division, supersede, as of their effective date, the last previously effective Exhibits "B" and "C." In any revision of Exhibit "C," the revised percentage participations of the respective tracts listed in the previously effective Exhibit "C" shall remain in the same ratio one to the other.

EXHIBIT B

Case No. 12171
Order No. R-_____

<u>TRACT NUMBER</u>	<u>PARTICIPATION</u>
Tracts 1-11:	82.32717578%
Tract 12:	1.94876739%
Tract 13:	2.20668140%
Tract 14:	1.59651829%
Tract 15:	1.38011413%
Tract 16A:	0.93524424%
Tract 16B:	0.00318158%
Tract 17:	2.92221146%
Tract 18A:	0.68203761%
Tract 18B:	2.19884747%
Tract 19:	0.50798636%
Tract 20:	0.28117699%
Tract 21A:	0.22480684%
Tract 21B:	0.37490265%
Tract 21C:	0.58041413%
Tract 22A:	0.99302789%
Tract 22B:	0.10845452%
Tract 23A:	0.13516109%
Tract 23B:	0.00467880%
Tract 24:	0.22141939%
Tract 25A:	0.00772937%
Tract 25B:	0.14139325%
Tract 26:	0.19235471%
Tract 27:	<u>0.02571467%</u>
	100.00000000%

EXHIBIT C

Case No. 12171
Order No. R-_____

SECTION 16. OUTSIDE SUBSTANCES.

Paragraph 2 (New): Consistent with Article 11.1 of the Unit Operating Agreement (Basis of Charge to Working interest Owners), Unit Operator shall allocate and pay the proceeds from the production, recovery, and sale of all volumes of gas purchased or acquired and injected into the Unitized Formation for pressure maintenance operations before the effective date of the first expansion of the Unit (the "Initial Injection Volumes") to the Working Interest Owners in the Unit as then constituted, and according to the Unit Participations in effect at the time the costs of acquisition of the Initial Injection Volumes were incurred (per Exhibit "D" attached to the Unit Operating Agreement in effect before November 1, 1997). At such time as 100% of the Initial Injection Volumes have been produced, recovered, and sold, proceeds from the production, recovery, and sale of subsequently acquired and injected gas volumes shall be allocated and paid to the Working Interest Owners in proportion to their Unit Participations (per Exhibit "D" to the Unit Operating Agreement in effect during the pertinent time period) at the time the costs of acquisition of subsequently injected gas volumes were incurred.