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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. 12,245

APPLICATION OF CHI ENERGY, INC., FOR)
COMPULSORY POOLING, EDDY COUNTY,)
NEW MEXICO)

ORIGINAL

REPORTER'S TRANSCRIPT OF PROCEEDINGSEXAMINER HEARING

BEFORE: MICHAEL E. STOGNER, Hearing Examiner

October 7th, 1999

Santa Fe, New Mexico

This matter came on for hearing before the New Mexico Oil Conservation Division, MICHAEL E. STOGNER, Hearing Examiner, on Thursday, October 7th, 1999, 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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I N D E X

October 7th, 1999
 Examiner Hearing
 CASE NO. 12,245

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A P P E A R A N C E S

FOR THE DIVISION:

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FOR THE APPLICANT:

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* * *

1 WHEREUPON, the following proceedings were had at
2 10:33 a.m.:

3 EXAMINER STOGNER: At this time I'll call Case
4 Number 12,245.

5 EXAMINER STOGNER: Is that one continued?

6 EXAMINER STOGNER: Mr. Bruce, which one are we on
7 now?

8 MR. BRUCE: Chi Energy.

9 EXAMINER STOGNER: Well, I have --

10 MR. CARROLL: There's two here. We've got one
11 continued --

12 MR. BRUCE: Yeah, I don't have my docket in front
13 of me.

14 MR. CARROLL: I've got 12,245 continued.

15 MR. BRUCE: Yes, this is 12,245.

16 EXAMINER STOGNER: Okay, so it was 12,255 that
17 was continued?

18 MR. BRUCE: 12,255, yeah, is the one that should
19 have been continued.

20 MR. CARROLL: Oh, okay. Case 12,245, Application
21 of Chi Energy, Inc., for compulsory pooling, Eddy County,
22 New Mexico.

23 EXAMINER STOGNER: Call for appearances.

24 MR. BRUCE: Mr. Examiner, Jim Bruce of Santa Fe,
25 representing the Applicant. I have one witness to be

1 sworn.

2 EXAMINER STOGNER: Any other appearances?

3 Will the witness please stand to be sworn?

4 (Thereupon, the witness was sworn.)

5 JOHN W. QUALLS,

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

8 DIRECT EXAMINATION

9 BY MR. BRUCE:

10 Q. Would you please state your name for the record?

11 A. John Qualls, Midland, Texas.

12 Q. Who do you work for?

13 A. I work for Chi Energy, I'm a geologist and a
14 landman.

15 Q. Have you previously testified before the
16 Division?

17 A. Yes, sir.

18 Q. As both a landman and a geologist?

19 A. Yes, sir.

20 Q. And were your credentials as an expert petroleum
21 landman and an expert petroleum geologist accepted as a
22 matter of record?

23 A. Yes, sir.

24 Q. And are you familiar with the land and geologic
25 matters involved in this Application?

1 A. Yes, I am.

2 MR. BRUCE: Mr. Examiner, I'd tender Mr. Qualls
3 as an expert petroleum landman and as an expert geologist.

4 EXAMINER STOGNER: Let's go over his credentials
5 on the geological portion, Mr. Bruce.

6 MR. BRUCE: Okay, sure.

7 Q. (By Mr. Bruce) Mr. Qualls, could you describe
8 your educational and employment background with respect to
9 geology?

10 A. I've got a bachelor's of science degree in
11 geology from Eastern New Mexico University, and I've worked
12 as a geologist off and on for the past 20 years.

13 Q. What companies have you worked for? How long
14 have you been at Chi?

15 A. I've been at Chi about 12 years now.

16 Q. Okay, and before that who did you work for?

17 A. I worked for Amoco. I've been an independent
18 geologist, I've done consulting work for most of the majors
19 in the Permian Basin.

20 Q. And during that 20 years have you pretty much
21 been involved in the Permian Basin?

22 A. Yes, sir.

23 Q. And in both New Mexico -- southeast New Mexico
24 and west Texas?

25 A. Yes, sir.

1 MR. BRUCE: Mr. Examiner do you have any other
2 questions of the witness?

3 VOIR DIRE EXAMINATION

4 BY EXAMINER STOGNER:

5 Q. Yeah, would you consider yourself, Mr. Qualls,
6 primarily a landman or a geologist?

7 A. I do mostly land work right now. I do -- I am
8 involved with geology, though.

9 Q. Okay, and you've had quite a few years'
10 experience on the land end of it?

11 A. Yes, sir.

12 EXAMINER STOGNER: So qualified.

13 DIRECT EXAMINATION (Resumed)

14 BY MR. BRUCE:

15 Q. Mr. Qualls, would you identify Exhibit 1 for the
16 Examiner and describe what Chi seeks in this case?

17 A. Exhibit 1 is a land plat showing the proposed
18 south half of Section 10, the well unit, in Township 17
19 South, 28 East. Chi seeks an order pooling the south half
20 of Section 10 to the base of the Morrow formation.

21 Q. And do you seek that for 40- and 160-acre pools
22 or formations, as well as the 320 acres?

23 A. Yes, sir.

24 Q. Okay. Based on that well location, the 40-acre
25 unit would be the southwest of the southwest?

1 A. Yes, sir.

2 Q. Okay. What is the well's location?

3 A. The well is located 990 feet from the south and
4 990 feet from the West, Section 10.

5 Q. And referring to Exhibit 2, could you identify
6 that for the Examiner and briefly describe the working
7 interest ownership in this well?

8 A. Yes. Exhibit 2 is a working interest ownership
9 of the Coal Train Fed Com Number 1, which is the proposed
10 well, listing all the working interest owners and their
11 percentages.

12 Q. Which of these parties have you not come to terms
13 with at this point?

14 A. Mobil Exploration and Producing.

15 Q. That's the only one?

16 A. Yes, sir.

17 Q. Okay. Let's discuss your efforts to obtain the
18 voluntary joinder of Mobil in the well, and I refer you to
19 Exhibit 3.

20 A. Exhibit 3 contains copies of the correspondence
21 with the interest owners. We first sent a written offer to
22 the interest owners on July the 2nd, 1999. That letter
23 enclosed an AFE and requested the interest owners to
24 participate in the well.

25 Q. Okay. Before we go on here, Mr. Qualls, your

1 letter here is not only to Mobil, but it was to Enron as
2 well. Since this date, have you come to terms with Enron?

3 A. Yes, sir.

4 Q. Okay, so you don't seek to pool Enron?

5 A. No, sir.

6 Q. Okay. Go on with your contacts with Mobil,
7 please.

8 A. In addition to this, two times during the month
9 of August we talked with Dave Collins, who's a land manger
10 for Mobil out of Houston. We requested a farmout or
11 requested a term assignment. His response was, go ahead
12 with the force pooling and then they might make a decision.

13 Q. What is the reason for Mobil's indecision?

14 A. I really couldn't answer that. They just were
15 not really that interested in this area, is the information
16 that I received, and they pretty much want you to go ahead
17 with compulsory pooling in order for them to make a
18 decision.

19 Q. Okay. In your opinion has Chi made a good-faith
20 effort to obtain the voluntary joinder of Mobil in this
21 well?

22 A. Yes, sir.

23 Q. Referring to Exhibit 4, please discuss the cost
24 of the proposed well.

25 A. Exhibit 4 is a copy of the AFE for the well.

1 It's a proposed 10,400-foot Morrow test with an estimated
2 dryhole cost of \$445,650 and a completed well cost of
3 \$699,150.

4 Q. Are these well costs in line with the costs of
5 other wells drilled to this depth in this area of Eddy
6 County?

7 A. Yes, sir.

8 Q. Does Chi Energy request that it be designated
9 operator of the well?

10 A. Yes, we do request that Chi be designated
11 operator.

12 Q. Or do you request -- No, excuse me. Do you
13 request that Chi Operating, Inc., be designated operator?

14 A. Yes, sir, Chi Operating, Inc.

15 Q. Okay, that's the operating arm of Chi Energy?

16 A. Yes, sir.

17 Q. Do you have a recommendation on the amounts which
18 should be paid for supervision and administrative expenses?

19 A. We request that \$6000 a month be allowed for a
20 drilling well and \$759 a month be allowed for a producing
21 well.

22 Q. And what are these rates based on?

23 A. It's based on Ernst and Young's 1998 survey
24 median rates.

25 Q. Are these amounts equivalent to those normally

1 charged by Chi Operating and other operators in this area
2 for wells of this depth?

3 A. Yes, sir.

4 Q. Do you request that these rates be adjusted
5 according to the COPAS accounting procedure?

6 A. Yes, sir.

7 Q. And were the interest owners being pooled
8 notified of this hearing?

9 A. Yes, sir.

10 Q. Is Exhibit 5 my affidavit of notice containing
11 the notice, this time, the notice letter and the certified
12 return receipts?

13 A. (Nods)

14 Q. Let's move on to the geology, Mr. Qualls.

15 A. All right.

16 Q. Would you identify your Exhibit 6 and would you
17 discuss the primary zones of interest in this area?

18 A. Exhibit 6 is a structure map of the area with the
19 proposed well and the well unit identified in Section 10.
20 The primary zone of interest for this well is the Morrow
21 "B" sand. Secondary objectives are the Morrow "A" sand and
22 possibly the Cisco.

23 Q. Is the structure important in the Morrow in this
24 area?

25 A. Yes, sir. We mapped this on the top of the

1 Morrow -- I mean, excuse me, on the top of the Atoka. The
2 way we interpret it, it reflects the Morrow on the top of
3 the Atoka.

4 Q. Okay.

5 A. That's what why we call it the top of the
6 Atoka/Morrow structure map.

7 Q. Let's move on to your Exhibit 7. Could you
8 identify that, discuss the geology a little bit further and
9 the production from the wells in this area?

10 A. Exhibit 7 is an isopach from the top of the gross
11 Morrow clastics to the top of the Mississippian. Generally
12 in this area it trends north to south. The proposed
13 location will give us approximately 225 feet of Morrow
14 clastics, which we believe is necessary in order to pick up
15 the pay sands.

16 Q. Now, is the production in this area fairly new?

17 A. Yes, sir, it is. We drilled -- Chi Operating
18 drilled a well, which is -- I have a type log on it, which
19 is Exhibit 8. It's Section 9. That well has been
20 producing about five months now. I think we completed it
21 at the end of May. It's made 227 million cubic feet of gas
22 and about 2545 barrels of condensate.

23 If you'll look on the map in Section 8, Chi
24 Operating drilled what we called the Silver Streak in the
25 northeast quarter. That is a marginal well making about 50

1 MCF a day.

2 Going southwest from our proposed Coal Train, in
3 Section 16, Yates Petroleum has drilled a well in the
4 southeast quarter called the Spurck, and it is making 4.8
5 million cubic feet of gas a day.

6 Just south of that in Section 21 is an OXY well
7 which is making 1.7 million cubic feet of gas per day.

8 Q. Now, based on this map, as you said, the Chi well
9 in Section 8 isn't a very good well, is it?

10 A. No, sir.

11 Q. So you do have the potential of stepping out
12 another well location and having a poor well?

13 A. Exactly.

14 Q. And you mentioned the type log. Why don't you
15 move on to that Exhibit 8 and maybe move on to the primary
16 zones you're looking at for the Examiner?

17 A. All right. Exhibit 8 is a type log, which is the
18 well in Section 9 called the Cannonball. It shows the top
19 of the Atoka around 9400 feet. Come on down to about 9600
20 feet, you see the top -- or excuse me, 9700, you see the
21 top of the Morrow clastics. Right below that is the "A"
22 sand, which is the secondary objective in our well, and
23 below that is the "B" sand, which is now producing in this
24 Cannonball well.

25 It also shows the top of the Mississippi at

1 around 9900.

2 Q. In your opinion, what penalty should be assessed
3 against Mobil if it goes nonconsent in this well?

4 A. Cost plus 200 percent.

5 Q. Mr. Qualls, as far as the exhibits, were Exhibits
6 1 through 5 prepared by you or under your direction or
7 compiled from company business records?

8 A. Yes, sir.

9 Q. Now, on Exhibits 6 and 7, down at the bottom they
10 say that they were prepared by Curt Anderson. Have you
11 reviewed the data that went into the preparation of these
12 exhibits?

13 A. Yes, sir.

14 Q. And do you agree with their interpretation?

15 A. Yes.

16 Q. And Exhibit 8 is simply from the company files?

17 A. Right, it's just a type log. It's a copy of the
18 log of the Cannonball, Section 9.

19 MR. BRUCE: Mr. Examiner, at this time I'd move
20 the admission of Chi Energy Exhibits 1 through 8.

21 EXAMINER STOGNER: Exhibits 1 through 8 will be
22 admitted into evidence at this time.

23 Q. (By Mr. Bruce) And Mr. Qualls, in your opinion
24 is the granting of this Application in the interests of
25 conservation and the prevention of waste?

1 A. Yes, sir.

2 EXAMINATION

3 BY EXAMINER STOGNER:

4 Q. Mr. Qualls, let's talk about Mobil's interest.
5 You show on Exhibit Number 2 a 37.5 percent. That's for
6 the south half, 320-acre dedication?

7 A. Yes, sir.

8 Q. Where is their acreage?

9 A. It is in the -- If you look on the land map,
10 which is Exhibit 1, they own the northeast of the southeast
11 quarter and the south half of the southeast quarter.

12 Q. Okay, northeast of the southeast -- Repeat that
13 again?

14 A. The northeast quarter of the southeast quarter
15 and the south half of the southeast quarter.

16 MR. BRUCE: Mr. Examiner, I guess there's no need
17 to pool 40 and 160-acre units here.

18 EXAMINER STOGNER: Okay.

19 MR. BRUCE: Just noticed that.

20 Q. (By Examiner Stogner) Okay, looking at one of
21 your maps --

22 A. Yes, sir.

23 Q. -- either Exhibit 6 or 7 --

24 A. Uh-huh.

25 Q. -- within that south half there shows to be a gas

1 well emblem up there in the northwest quarter of the
2 southwest quarter.

3 A. Uh-huh.

4 Q. What's the story on that well?

5 A. The northwest quarter of the southwest quarter?

6 Q. Yes, sir.

7 A. I believe that's a well that was drilled and it's
8 either depleted -- It's not producing any longer. We
9 looked. We've looked at re-entering that well and possibly
10 going into the Cisco. It looks like there's a Cisco reef
11 in that well. I don't believe it's got the potential to
12 produce in the Morrow.

13 Q. Do you know how deep that well was drilled?

14 A. Not offhand, I don't know exactly the depth.

15 Q. Now, when you say it's no longer producing, is it
16 plugged and abandoned?

17 A. I believe so, yes, sir.

18 Q. And you said Chi -- Who drilled it?

19 A. I'm not sure who drilled that well. We now own
20 the acreage that that well is on --

21 Q. All right.

22 A. -- and we're looking at re-entering it and
23 possibly trying to complete the Cisco.

24 Q. Now, what is Chi Operating, Inc.'s, relationship
25 with Chi Energy, Inc.?

1 A. Chi Operating, Inc., is the entity that -- which
2 we operate oil and gas wells in New Mexico.

3 Q. It's a wholly owned subsidiary?

4 A. Yes.

5 Q. And once the well was drilled and completed, then
6 if it is a producer, who would be the operator? Chi
7 Operating or --

8 A. Chi Operating.

9 Q. Chi Operating. Okay. At the time you made this
10 Application, I'm assuming that Enron was not a party or had
11 not agreed?

12 A. Yes, sir, they had not at the time.

13 Q. Okay, so that's the reason Energen's
14 documentation appears in this; is that right?

15 A. Yes, sir.

16 EXAMINER STOGNER: Okay. Anything further in
17 this matter?

18 MR. BRUCE: One thing, Mr. Examiner, I forgot to
19 give you the original affidavit of notice.

20 EXAMINER STOGNER: Would you like the copy back?

21 MR. BRUCE: Sure, thank you.

22 EXAMINATION

23 BY MR. CARROLL:

24 Q. Is the well named Freight Train or Coal Train?

25 A. Coal Train. The prospect is the Freight Train

1 Prospect. The well will be the Coal Train Fed Number 1.

2 FURTHER EXAMINATION

3 BY EXAMINER STOGNER:

4 Q. Has that well been staked?

5 A. Yes, sir.

6 Q. Do you know if an API number has been assigned to
7 it?

8 A. I'm not certain if it has. I know it's been
9 approved.

10 EXAMINER STOGNER: Since it's been approved, I'm
11 sure an API number has been -- Mr. Bruce, would you get
12 back with me on that information and API number on this
13 particular well?

14 MR. BRUCE: Yes.

15 THE WITNESS: I'm sure I have it at the office.
16 I can look on the APD.

17 EXAMINER STOGNER: Also, if you have a copy of
18 the APD, if you can furnish it to Mr. Bruce, we can make
19 that a part of the record. It won't necessarily need to be
20 an exhibit, but that information would be --

21 MR. BRUCE: Will do, Mr. Examiner.

22 EXAMINER STOGNER: I'm going to leave the record
23 open in this particular matter, pending receipt of that
24 particular information.

25 If there's nothing further in Case Number 12,245,

1 it will be taken under advisement at that time.

2 THE WITNESS: Thank you.

3 EXAMINER STOGNER: Thank you.

4 (Thereupon, these proceedings were concluded at
5 10:50 a.m.)

6 * * *

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9
10
11 I do hereby certify that the foregoing is
12 a complete record of the proceedings in
13 the Examiner hearing of Case No. 12245,
14 heard by me on 7 October 1999.
15 Michael E. Stogner, Examiner
16 Oil Conservation Division
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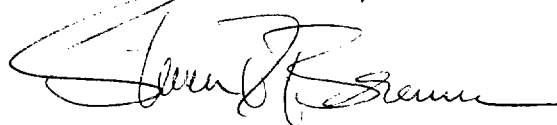
CERTIFICATE OF REPORTER

STATE OF NEW MEXICO)
) ss.
COUNTY OF SANTA FE)

I, Steven T. Brenner, Certified Court Reporter and Notary Public, HEREBY CERTIFY that the foregoing transcript of proceedings before the Oil Conservation Division was reported by me; that I transcribed my notes; and that the foregoing is a true and accurate record of the proceedings.

I FURTHER CERTIFY that I am not a relative or employee of any of the parties or attorneys involved in this matter and that I have no personal interest in the final disposition of this matter.

WITNESS MY HAND AND SEAL October 27th, 1999.



STEVEN T. BRENNER
CCR No. 7

My commission expires: October 14, 2002