

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. 12,469

APPLICATION OF PALADIN ENERGY)
 CORPORATION FOR COMPULSORY POOLING,)
 LEA COUNTY, NEW MEXICO)

ORIGINAL

REPORTER'S TRANSCRIPT OF PROCEEDINGS

EXAMINER HEARING

BEFORE: MARK ASHLEY, Hearing Examiner

August 10th, 2000

Santa Fe, New Mexico

This matter came on for hearing before the New Mexico Oil Conservation Division, MARK ASHLEY, Hearing Examiner on Thursday, August 10th, 2000, 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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OIL CONSERVATION DIV.
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I N D E X

August 10th, 2000
Examiner Hearing
CASE NO. 12,469

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<u>RUSTY RICE</u> (Landman)	
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A P P E A R A N C E S

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 By: MICHAEL FELDEWERT

* * *

1 WHEREUPON, the following proceedings were had at

2 9:00 a.m.:

3 EXAMINER ASHLEY: The Division calls Case 12,469,
4 Application of Paladin Energy Corporation for compulsory
5 pooling, Lea County, New Mexico.

6 Call for appearances.

7 MR. FELDEWERT: Michael Feldewert, with the law
8 firm of Campbell, Carr, Berge and Sheridan, for the
9 Applicant. I have one witness today, Mr. Rusty Rice.

10 EXAMINER ASHLEY: Additional appearances?
11 Will the witness please stand to be sworn?

12 (Thereupon, the witness was sworn.)

13 RUSTY RICE,
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. FELDEWERT:

18 Q. Would you please state your full name for the
19 record?

20 A. Full name is Rusty Rice.

21 Q. Mr. Rice, where do you reside?

22 A. Dallas, Texas.

23 Q. And by whom are you employed?

24 A. I'm contractually employed by Paladin Energy
25 Corp.

1 Q. Have you previously testified before this
2 Division?

3 A. I have.

4 Q. As an expert witness in petroleum land matters?

5 A. Yes.

6 Q. At the time of your testimony, were your
7 credentials as an expert in petroleum land matters accepted
8 and made a matter of record?

9 A. They were.

10 Q. Are you familiar with the Application that has
11 been filed by Paladin in this case?

12 A. I am.

13 Q. And are you familiar with the status of the lands
14 in the subject area?

15 A. Yes.

16 MR. FELDEWERT: At this time I would tender Mr.
17 Rice as an expert witness in petroleum land matters.

18 EXAMINER ASHLEY: Mr. Rice is so qualified.

19 Q. (By Mr. Feldewert) Would you briefly state for
20 the Examiner what Paladin seeks with this Application?

21 A. Paladin is seeking an order pooling all minerals
22 from the surface to the base of the Devonian formation for
23 a rework operation on the Hamilton well, which is located
24 at a standard location in the northeast of the southeast of
25 Section 34.

1 Q. So this is a rework operation, you're not
2 drilling a new well?

3 A. That is correct.

4 Q. Okay, and so you're seeking to pool interests
5 here to rework an existing well for purposes of returning
6 it to economic production?

7 A. That is correct.

8 Q. Okay. Why don't you review for the Examiner
9 Paladin Exhibit Number 1?

10 A. It is a land plat which has designated the 40-
11 acre unit outlined in black, colored in yellow, in the
12 northeast of the southeast of Section 34, and the well is
13 highlighted in the center of the unit.

14 Q. There's an attachment to this exhibit. Can you
15 explain what that is?

16 A. Basically, it's a production history of wells in
17 the general area.

18 Q. For which -- For the Devonian formation?

19 A. For the Devonian formation, that's correct.

20 Q. Okay.

21 A. Knowles Pool.

22 Q. Of the wells that are listed on here, are any of
23 them active at this time?

24 A. There is one well listed on here, the Hamilton
25 2 Y, which is located in Section 35. That is the second

1 from the bottom, and that is another well that Paladin also
2 operates in the area.

3 Q. What is the status of the acreage in the
4 northeast quarter of the southeast quarter of Section 34?

5 A. It is all fee ownership.

6 Q. Okay. And can you describe to the hearing
7 officer the primary objective of your reworking efforts in
8 the Hamilton A Number 2?

9 A. Primary objective is the Knowles-Devonian Pool.

10 Q. Do you have any secondary objectives?

11 A. We do not.

12 Q. Okay, why don't we move to Paladin Exhibit Number
13 2. Would you identify and review that for the Examiner,
14 please?

15 A. That is an exhibit that I prepared outlining all
16 of the owners of record in the northeast of the southeast.

17 Q. Okay. Now, the first page lists a number of
18 individuals. Where is Paladin's total interest shown?

19 A. Total interest is on page 2 at the top third
20 where it represents that they've got 88 percent under
21 lease, 88.153.

22 Q. Okay. So Paladin has leased all of the interests
23 of the individuals shown on all of page 1 and the top part
24 of page 2; is that right?

25 A. That is correct.

1 Q. At this time, Mr. Rice, what percentage of the
2 mineral interest is voluntarily committed to this well?

3 A. Ninety-two percent.

4 Q. Okay, and how do you derive that figure?

5 A. I derive that by the 88 percent owned by Paladin
6 under leasehold, along with the 4.6875 percent that is
7 currently under lease to a Charles Qualia.

8 Q. Has Mr. Qualia signed his lease yet?

9 A. I have been notified that the bank has executed a
10 lease to Mr. Qualia, yes.

11 Q. And has Mr. Qualia indicated whether he's willing
12 to participate in this operation?

13 A. Mr. Qualia has responded to telephone
14 conversations through written letters saying he will agree
15 to participate in the operation.

16 Q. Okay. Is there anyone on here, any other
17 individual listed on here who has recently indicated that
18 he or she is willing to participate in this operation?

19 A. No.

20 Q. Okay. How many interest owners are subject to
21 this pooling Application?

22 A. There are five.

23 Q. And where are they shown on this exhibit?

24 A. That is the section right above the lease to
25 Charles Qualia part, where it -- titled "Lessors who have

1 not been located or will not respond."

2 Q. Okay, there are six names listed. Is there one
3 individual on there who you have recently been contacted
4 by?

5 A. Yes, Ms. Winona Jones has contacted as of
6 yesterday and agreed to lease under the current terms.

7 Q. Of these five, are there any of these interest
8 owners in a proposed spacing unit who you have been unable
9 to locate?

10 A. There are three, yes.

11 Q. And who are they?

12 A. That is Lutishie Brewer, Jeanne Fuller and
13 Margaret Eversden.

14 Q. What efforts have you made to locate and find
15 these individuals?

16 A. We have sent out correspondence with their last
17 known address and attempted to reach them through phone
18 directory, on phones, have contacted other lessors that
19 appear to be relatives through title, with no success,
20 along with using the Internet to websites in attempting to
21 get addresses.

22 Q. Can you explain to the Hearing Examiner your
23 Paladin Exhibit Number 3?

24 A. Paladin Exhibit Number 3 are letters or
25 correspondence that have been sent out to those parties,

1 attempting to -- which have been sent certified mail,
2 attempting to notify them of our operation and our desire
3 to lease.

4 Q. These are the individuals you've been unable to
5 contact?

6 A. That is correct.

7 Q. Okay. In your opinion, Mr. Rice, have you made a
8 good faith effort to locate all individuals and obtain
9 their voluntary joinder?

10 A. We have.

11 Q. Okay. Now, we've gone through your effort to
12 locate individuals. What efforts have you made to obtain
13 voluntary joinder?

14 A. Voluntary joinder, we sent out AFEs prior to the
15 hearing and requested them either to lease or participate.

16 Q. Okay. When was your first contact with these
17 individuals?

18 A. The original contact was made back in January of
19 this year.

20 Q. Okay, and was that an effort to lease?

21 A. That was an effort to lease.

22 Q. And you said your AFEs went out in June?

23 A. Went out in June, that's correct.

24 Q. Okay. What is the current status of the
25 remaining individuals you've been unable to reach an

1 agreement with? I think there's a Lynda Pratt Rast and a
2 Keith Pratt Daniels; is that right?

3 A. That is correct. They have notified us a couple
4 of times of their desire to lease. We have prepared leases
5 in agreement with what they proposed, and they never will
6 send them back.

7 Q. Okay. Now, you have put together for the
8 Examiner the letters reflecting your attempts to obtain
9 voluntary joinder; is that right?

10 A. That is correct, along with the leases that were
11 sent out to the individuals.

12 Q. Is that Paladin Exhibit Number 4?

13 A. That is correct.

14 MR. FELDEWERT: Okay. And just for purposes of
15 the record and the Hearing Examiner, we'll note that these
16 are organized by interest owner, Exhibit Number 4.

17 EXAMINER ASHLEY: Excuse me?

18 MR. FELDEWERT: Exhibit Number 4 is organized by
19 interest owner.

20 EXAMINER ASHLEY: Okay.

21 Q. (By Mr. Feldewert) Why don't you now move to
22 Paladin Exhibit Number 5 and identify and explain that for
23 the Hearing Examiner, please?

24 A. That is an AFE which was prepared by an employee
25 of Paladin for the proposed operation.

1 Q. Is this the AFE that went out with your letters
2 in June?

3 A. That is correct.

4 Q. And what are the totals set forth in this
5 exhibit?

6 A. Totals set forth is \$88,174.

7 Q. Has Paladin Energy Corporation reworked any other
8 Devonian wells in the immediate area?

9 A. They have. They reworked the previously
10 referenced Y Number 2 well in Section 35.

11 Q. That's the one that was still producing?

12 A. Yes, sir.

13 Q. Are the costs on Paladin Exhibit Number 5 in line
14 with what has been charged by other operators in the area
15 for similar reworking efforts?

16 A. Yes, sir, I believe.

17 Q. Have you made an estimate of the overhead and
18 administrative costs for reworking this well and also while
19 producing this well if you are successful?

20 A. We have.

21 Q. And what is that figure?

22 A. \$400 a month, overhead.

23 Q. And where did that figure come from?

24 A. That came from a JOA that's been executed by
25 other partners of Paladin.

1 Q. How does that overhead amount compare with the
2 1999 Ernst and Young survey?

3 A. In my opinion, it's lower than the going rate.

4 Q. Do you recommend that this figure be incorporated
5 into any order that results from this hearing?

6 A. Yes, I do.

7 Q. Does Paladin Energy Corporation seek to be
8 designated as operator of this proposed rework project?

9 A. Yes, they do.

10 Q. Why don't you identify and review Paladin Exhibit
11 Number 6 for the Hearing Examiner?

12 A. Exhibit Number 6 is an AAPL Form 610, Version
13 1982, joint operating agreement dated April 1st of 1999.
14 It's been executed by Paladin Energy as operator and three
15 of the parties as nonoperator.

16 Q. Is this the joint operating agreement that's
17 going to govern the operations for the Hamilton A Number 2?

18 A. That is correct.

19 Q. And I think you indicated this has been executed
20 by other interest owners in the well; is that right?

21 A. Yes, two other nonoperators.

22 Q. Okay. Does this joint operating agreement set
23 the overhead rate and provide for the escalation of those
24 rates?

25 A. It does.

1 Q. And how is that done? Is that pursuant to the
2 COPAS form attached?

3 A. Pursuant to the COPAS, with no additional
4 addendums.

5 Q. Does Paladin request that the overhead rates
6 approved by this Division be subject to the increase in
7 accordance to the COPAS guidelines applicable to other
8 interest owners in the well?

9 A. They do.

10 Q. Would you identify for the Examiner Paladin
11 Exhibit Number 7?

12 A. It's an affidavit.

13 Q. Is this the affidavit with the attached letters
14 giving notice of the hearing?

15 A. That is correct.

16 Q. Okay. Why don't you briefly explain for the
17 Hearing Examiner what you propose to do with the Hamilton
18 A 2 well?

19 A. Well, the Hamilton well has been shut in since
20 1998. Our proposal is to re-enter the well, acidize it and
21 rig up a pumping unit, rod pump.

22 Q. Why don't you explain for the Examiner what
23 Paladin Exhibit Number 8 is?

24 A. Paladin Exhibit Number 8 is basically an outline
25 of the operations to be conducted.

1 Q. On the Hamilton A Number 2?

2 A. On the Hamilton A Number 2 well, correct.

3 Q. Okay. Does Paladin request that the Examiner
4 impose a risk penalty against nonconsenting interest owners
5 in this recompletion effort?

6 A. They do.

7 Q. Are you prepared to make a recommendation to the
8 Examiner for that risk penalty?

9 A. I am.

10 Q. And what amount do you recommend?

11 A. The maximum allowed by statute, 200 percent.

12 Q. What does the joint operating agreement provide
13 by way of a risk penalty?

14 A. 400 percent for subsequent operations.

15 Q. Okay. Now, on what do you base this 200-percent
16 recommendation?

17 A. Basically the risk of the well -- of being able
18 to re-enter the well. From the history, when it was shut
19 in in 1998, it was very low volume, one barrel of oil and a
20 substantial amount of water. Due to low oil prices, the
21 well was shut in at that time.

22 There could be mechanical problems of reworking.
23 The well hasn't been tested in the last three years, so
24 there's a possibility of some collapse of casing or
25 whatnot.

1 The economic risk associated with the rework
2 would be the low production rates, which we are
3 anticipating to maintain some rate around ten barrels a
4 day, which is offset currently by the high oil prices.
5 Either one of those variables are reduced, the economic of
6 this well would be very less substantial.

7 Q. Have you been in contact with the petroleum
8 engineer for Paladin on this project?

9 A. I have.

10 Q. Would you explain to the Hearing Examiner Paladin
11 Exhibit Number 9?

12 A. Exhibit Number 9 is an affidavit of Rick Fuerman.
13 He is an employee of Paladin Energy, and he is a certified
14 engineer.

15 MR. FELDEWERT: I would note for the record, Mr.
16 Fuerman indicates he has previously testified before this
17 Division as a petroleum engineer.

18 Q. (By Mr. Feldewert) Mr. Rice, does Mr. Fuerman
19 indicate what he estimates to be the commercial rate of
20 production?

21 A. He does, and that is the ten barrels I referenced
22 earlier.

23 Q. And where is that shown in his affidavit? I
24 think it's shown in paragraph 7; is that right?

25 A. That is correct, paragraph 7.

1 Q. Does Mr. Fuerman consider this to be a very risky
2 venture?

3 A. He does.

4 Q. I think he states that in his affidavit as well;
5 is that correct?

6 A. That is correct.

7 Q. Okay. You mentioned the history of this well.
8 Have you prepared an exhibit that shows the history of the
9 Hamilton A Number 2 well?

10 A. We have, in Exhibit 10.

11 Q. Okay. I don't want to go through that in too
12 much detail, but when was that well first drilled?

13 A. First drilled in 1953 by Amerada Hess.

14 Q. Okay. And then at some point there was some
15 artificial lift production put on the well; is that
16 correct?

17 A. That is correct.

18 Q. And when was the well shut in?

19 A. The well was shut in in February of 1998.

20 Q. And why was that?

21 A. Due to low volumes and low oil prices.

22 Q. What was the last well test on that well?

23 A. Last well test was one barrel of oil and 350
24 barrels of water per day.

25 Q. When was that test conducted?

1 A. That was in February of 1998.

2 Q. About the time it was shut in?

3 A. Yes.

4 Q. Okay. Mr. Rice, do you believe that there's a
5 chance that Paladin's recompletion efforts here will not
6 succeed?

7 A. Yes.

8 Q. Does Mr. Fuerman, who submitted an affidavit in
9 this case, agree with that observation?

10 A. He does.

11 Q. Do you believe that even if your recompletion
12 efforts are successful that this venture may nevertheless
13 not be a commercial success?

14 A. We do.

15 Q. Is that again confirmed by the affidavit filed by
16 Mr. Fuerman?

17 A. Yes.

18 Q. How soon does Paladin Energy plan to re-enter
19 this well?

20 A. As soon as possible.

21 Q. In your opinion, will granting this Application
22 be in the best interests of conservation, the prevention of
23 waste and the protection of correlative rights?

24 A. Yes, I believe so.

25 Q. Were Exhibits 1 through 10 prepared by you or

1 under your direction?

2 A. They were.

3 MR. FELDEWERT: Mr. Examiner, that's all I have
4 at this time.

5 EXAMINER ASHLEY: Would you like to enter these
6 exhibits for the record?

7 MR. FELDEWERT: I would like to enter them into
8 the record, thank you.

9 EXAMINER ASHLEY: Exhibits 1 through 10 will be
10 admitted into evidence at this time.

11 EXAMINATION

12 BY EXAMINER ASHLEY:

13 Q. Mr. Rice, could you go over the overhead rates
14 again for drilling and production? I didn't catch that.

15 A. The overhead rates which is provided for in our
16 operating agreements are \$400 a month.

17 Q. Is that for re-entry and for producing?

18 A. Yes.

19 Q. Both?

20 A. Yes, sir.

21 Q. Okay.

22 A. That's the monthly overhead rates, not the
23 drilling rates.

24 Q. And the risk penalty you want, cost plus 200
25 percent?

1 A. Yes, sir.

2 Q. And that's what's reflected in the JOA?

3 A. Actually, the JOA provides for 400 percent,
4 subsequent operations.

5 Q. Mr. Rice, the JOA is cost plus 400 percent?

6 A. No, it's just 400 percent --

7 Q. Okay.

8 A. -- recoupment of 400 percent --

9 Q. Okay.

10 A. -- so cost plus 300 percent.

11 Q. Okay.

12 A. And that was a negotiated figure between the
13 parties who executed the agreement.

14 Q. So you're going in to re-enter this well, to
15 recomplete it in the same zone that it was completed in
16 prior to being shut in?

17 A. Yes, sir.

18 EXAMINER ASHLEY: Mr. Feldewert, I have a couple
19 of questions that I want to check on before we take this
20 under advisement. So at this time I would like to go ahead
21 and take a recess --

22 MR. FELDEWERT: Okay.

23 EXAMINER ASHLEY: -- for about 20 minutes, and
24 then we'll come back and finish up with this one.

25 MR. FELDEWERT: Sure.

1 EXAMINER ASHLEY: So at this time, let's recess
2 until -- 20 minutes, that would be 9:45 that we'll
3 reconvene.

4 (Thereupon, a recess was taken at 9:25 a.m.)

5 (The following proceedings had at 9:45 a.m.)

6 EXAMINER ASHLEY: This hearing will now come back
7 to order.

8 I just had some questions about the risk penalty,
9 the percent risk penalty. I've worked that out, I've
10 gotten the answers I need. I don't have anything further.

11 THE WITNESS: Okay.

12 EXAMINER ASHLEY: So thank you.

13 THE WITNESS: All right, thank you.

14 EXAMINER ASHLEY: And there being nothing further
15 in this case, Case 12,469 will be taken under advisement.

16 (Thereupon, these proceedings were concluded at
17 9:46 a.m.)

18 * * *

19
20
21 I do hereby certify that the foregoing is
22 a complete record of the proceedings in
the Examiner hearing of Case No. 12469,
23 heard by me on 8-10-00 49.

24 Mark Ashley Examiner
25 Of Conservation Division

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 August 11th, 2000.



STEVEN T. BRENNER
CCR No. 7

My commission expires: October 14, 2002