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June 11, 2002

VIA OVERNIGHT MAIL
UPS TRACKING NO. 1Z F70 735 22 1002 0350
Mr. W. Thomas Kellahin
Kellahin and Kellahin
117 N. Guadalupe
Santa Fe, New Mexico

Re: TMBR/Sharp Drilling, Inc. vs. Arrington, et al.

Dear Tom:

I apologize that the preparation of this document has been so difficult, but we received a copy of the Proposed Order that was filed, and found several typographical errors that we thought should be corrected. Therefore, we enclose this new Order which we would appreciate your transmitting to the Division. The changes do not affect any substantive matters, but they do affect typographical errors.

Thank you for all your hard work.

Very truly yours,

COTTON, BLEDSOE, TIGHE & DAWSON, P.C.

Susan R. Richardson

SRR/aw
Enclosure

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

APPLICATION OF TMBR/SHARP DRILLING, INC. FOR COMPULSORY POOLING, N/2 (UNIT E) SECTION 25, T16S, R35E LEA COUNTY, NEW MEXICO	**CASE NO. 12816**
APPLICATION OF OCEAN ENERGY, INC. FOR COMPULSORY POOLING, W/2 (UNIT E) SECTION 25, T16S, R35E LEA COUNTY, NEW MEXICO	**CASE NO. 12841**
APPLICATION OF DAVID H. ARRINGTON OIL & GAS, INC. FOR COMPULSORY POOLING E/2 (UNIT A) SECTION 25, T16S, R35E LEA COUNTY, NEW MEXICO	**CASE NO. 12859**
APPLICATION OF OCEAN ENERGY, INC. FOR COMPULSORY POOLING W/2 (UNIT K) SECTION 25, T16S, R35E LEA COUNTY, NEW MEXICO	**CASE NO. 12860**

TMBR/SHARP DRILLING, INC.
PROPOSED ORDER

BY THE DIVISION:

This cause came on for hearing at 8:15 a.m. on May 16 and 17, 2002 at Santa Fe, New Mexico, before Examiner Michael E. Stogner.

NOW, on this ___ day of June, 2002, the Division Director, having considered the testimony, the record and the recommendation of the Examiner, and being fully advised in the premises,

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) Division Cases No. 12816, 12841, 12859 and 12860 were consolidated at the time of the hearing for the purpose of testimony, and, in order to provide a comprehensive decision in these cases, one order should be entered for all four cases.

SUMMARY OF PROCEEDINGS

(3) On August 6, 2001, TMBR/Sharp filed two applications for permit to drill ("APD") with the Hobbs Office of the Division requesting approval to drill:

(a) its Blue Fin "25" Well No. 1 in Unit E and dedicate to it the N/2 of Section 25, T16S, R35E.

(b) its Leavelle "23" Well No. 1 in Unit G and dedicate to it the E/2 of Section 23, T16S, R35E.

(4) On August 8, 2001, the Hobbs Office of the Division denied the TMBR/Sharp permits because Arrington Oil & Gas, Inc. already had conflicting permits on the acreage.

(5) On December 11, 2001, the Division entered Order R-11700, refusing to approve TMBR/Sharp's APDs because on July 17, 2001 and July 25, 2001 respectively, the Division approved APDs for David H. Arrington Oi & Gas, Inc. ("Arrington") for its:

(a) Triple Hackle Dragon "25" Well No. 1 for a spacing unit consisting of the W/2 of Section 25

(b) Blue Drake "23" Well No. 1 for a spacing unit consisting of the E/2 of Section 23

The Division based its decision on Arrington's "claim of colorable title" to the Hamilton/Stokes top leases, and stated that:

(a) "(22) Arrington has demonstrated at least a colorable claim of title that would confer upon it a right to drill its proposed wells, no basis exists to reverse or overrule the action of the District Supervisor in approving the Arrington APDs."

(b) "(21) The Oil Conservation Division has no jurisdiction to determine the validity of any title, or the validity or continuation in force and effect of any oi land gas lease. Exclusive jurisdiction of such matters resides in the courts of the State of New Mexico."

(6) On December 27, 2001, the Lea County District Court, exercised that jurisdiction, and ruled that TMBR/Sharp's Hamilton/Stokes leases are still valid and in effect and Arrington's Hamilton/Stokes top lease are not in effect.

(7) On March 26, 2002, the Commission held a De Novo hearing concerning Order R-011700.

(8) On April 26, 2002, the commission entered Order R-11700-B which rescinded the Division's approval of Arrington's APDs and ordered that the Division's District Supervisor approve TMBR/Sharp's two APDs filed on August 6, 2002 and August 7, 2001.

(9) On May 1, 2002, Chris Williams, Supervisor of the Hobbs Division of the OCD, voided the W/2 and E/2 APD of Arrington and granted the two APD's requested by TMBR/Sharp in August of 2001.

(10) By May 7, 2002, TMBR/Sharp, having voluntarily consolidated at least 82% of the working interest owners in the N/2 of Section 25, commenced drilling its Blue Fin "25" Well No. 1 in Unit E dedicated to the N/2 of Section 25, T16S, R35E.

(11) The following four (4) compulsory pooling applications which involved Section 25, T16S, R35E, were set for an Examiner Hearing on May 2, 2002 but then were continued until May 16, 2002 to be heard after the Commission entered its Order R-11700-B on April 26, 2002:

(a) TMBR/Sharp's application for compulsory pooling of the N/2 of Section 25 for its Blue Fin 25 Well No. 1 in Unit E of that section. Case 12816 filed January 25, 2002.

(b) Ocean Energy, Inc.'s ("Ocean") application for compulsory pooling of the W/2 of Section 25 for its Triple Hackle Dragon 25 Well No. 1 in Unit E of that section. Case 12841 filed February 2, 2002.

(c) Ocean's application for compulsory pooling of the W/2 of Section 25 for its Triple Hackle Dragon 25 Well No. 2 in Unit K of that section. Case 12860 filed April 9, 2002.

(d) Arrington's application for compulsory pooling of the E/2 of Section 25 for its Glass-Eye Midge 25 Well No. 1 in Unit A of that section. Case 12859 filed April 9, 2002.

ACREAGE CONFIGURATION

(12) Section 25 is subdivided as follows:

(a) The NW/4 is fee acreage referred to as the Stokes/Hamilton leases controlled by TMBR/Sharp which are the subject of litigation with Arrington over his top leases.

(b) The SW/4 is fee acreage referred to as the Ocean farm-in acreage obtained beginning on and after July 23, 2001; Ocean assigned a partial interest in such acreage to Arrington on November 11, 2001.

(c) The SE/4 is a State of New Mexico lease held by Yates.

(d) The NE/4 is divided between the E/2 and W/2, and TMBR/Sharp controls 63% and Arrington controls 31% of the leases covering said quarter section.

COMPULSORY POOLING

TMBR/Sharp's compulsory pooling case:

(13) On January 25, 2002, TMBR/Sharp filed an application for compulsory pooling for the remaining working interest owners in the N/2 of Section 25.

(14) In accordance with NMSA (1978) Section 70-2-17, and Order R-11700-B, on May 7, 2002, TMBR/Sharp spudded the Blue Fin 25 Well No. 1 after filing an application to compulsory pool the remaining working interest owners in the N/2 of Section 25.

(15) At the time of the hearing, TMBR/Sharp controlled 82% of the working interest ownership, Arrington controlled 16%, and two parties who could not be located controlled 2% of the N/2 of Section 25.

(16) TMBR/Sharp has 100% of the working interest in the NW/4 of Section 25, and its compulsory pooling case is necessary in order to consolidate certain owners in the NW/4 of Section 25 to consolidate a 320-acre spacing unit consisting of the N/2 of Section 25.

(17) TMBR/Sharp's geological and geophysical evidence demonstrates that the appropriate development of Section 25 is best accomplished by orientating the spacing units N/2 and S/2.

(18) TMBR/Sharp originally developed the concept for the exploration of Sections 23, 24, 25 and 26 (Big Tuna Prospect). The project started in 1991 and over time, over $7 million was spent on land, geological, geophysical analysis and drilling.

(19) Prior to commencing the Blue Fin 24 Well No. 1 in the SW/4 of Section 24, TMBR/Sharp offered to Ocean a share of the Bug Tuna Prospect on three different occasions, including a January 31, 2001 meeting in Ocean's office in Houston, Texas.

(20) After being afforded an opportunity for a detailed review of TMBR/Sharp's geology including its 3-D seismic data, Ocean declined to participate based on its belief that the Chester formation would be structurally too low and therefore too wet (water saturation too high to allow for commercial production of hydrocarbons).

(21) On March 27, 2001, Arrington top leased the TMBR/Sharp's Hamilton/Stroke leases which cover lands in Sections 23, 24 and 25, among others. Arrington was aware that TMBR/Sharp had obtained a drilling permit for the Blue Fin 24 We.. No. 1 in November of 2000.

(22) On March 29, 2001, TMBR/Sharp spudded its Blue Fin 24 Well No. 1 in the SW/4 of Section 24.

(23) June 29, 2001, TMBR/Sharp completed the Blue Fin 24 Well No. 1 for production from the Chester formation at an initial rate of 7 MMCF/day.

(24) On July 24, 2001, David H. Arrington personally told Jeff Phillips, President of TMBR/Sharp, that TMBR/Sharp would not be able to timely drill wells in Section 23 or 25. (TMBR/Sharp's Hamilton/Stokes leases have a 180-day continuous drilling clause between wells.)

(25) On July 19, 2001, Arrington obtained an approved APD from the Division for its well to be drilled in Unit E and dedicated to the W/2 of Section 25. Arrington had no intention of drilling a well but obtained its permit because it wanted to block TMBR/Sharp from obtaining a competing permit which was denied on August 8, 2001.

(26) TMBR/Sharp was the first working interest owner to propose a well in Section 25.

(27) At the time of filing of its compulsory pooling application, neither Ocean nor Arrington had an interest of record in the N/2 of Section 25. Arrington had no interest in the W/2 of Section 25.

(28) Ocean's farm-ins are confined to the SW/4 of Section 25 and Arrington did not receive an interest in Ocean's various farm-ins in the SW/4 of Section 25 until November 14, 2001.

Ocean's two compulsory pooling cases:

(29) Ocean's compulsory pooling applications are an attempt by Ocean to substitute itself for Arrington on the APD approved by the Division on July 19, 2001:

(a) on November 14, 2001, Ocean and Arrington entered into a Letter Agreement concerning their plans for the Triple Hackle Dragon "25" Well No. 1 for the W/2 of Section 25;

(b) which provided that Arrington would be the Operator;

(c) that if a drilling title opinion requirement deterred Arrington from drilling, Ocean would be the operator.

(d) Ocean now seeks a compulsory pooling order for Arrington's Triple Hackle Dragon "25" Well No. 1.

(30) Ocean has failed to take any reasonable action to preclude its farm-in's from expiring on July 1, 2002. Its farm-ins contain force majeure clauses which arguably could offer protection from expiration in appropriate circumstances.

Arrington's compulsory pooling cases:

CASE 12859

(31) On July 19, 2001 Arrington obtained an approved APD for his Triple Hackle Dragon 25 Well No. 1 dedicated to the W/2 of Section 25.

(32) On January 24, 2002, Arrington proposed the well to TMBR/Sharp.

(33) On April 9, 2002, Arrington filed a compulsory pooling application with the Division.

(34) This Case was heard on May 16-17, 2002.

CASE 12,859

(35) On December 17, 2001 Arrington, without notice to TMBR/Sharp, obtained an approved APD for its Glass-Eye Midge 25 Well No. 1 dedicated to the E/2 of Section 25.

(36) On December 17, 2001, Arrington held no interest in the NE/4 of Section 25. It obtained its interest from Huff by assignment recorded on February 4, 2002. The SE/4 of Section 25 is controlled by Yates Petroleum Corporation.

(37) On March 26, 2002, the Commission held a hearing concerning Arrington's APD for the W/2 of Section 25 and TMBR/Sharp's APD for the N/2 of Section 25.

(38) At no time during that hearing did Arrington inform the Commission that Arrington claimed an approved APD for the E/2 of Section 25 which would be in conflict with the APD for the N/2 (TMBR/Sharp) then being decided by the Commission.

(39) Arrington has waived any claim for a spacing unit consisting of the E/2 of Section 25 by its failure to raise this issue of its APD for the E/2 of Section 25 at the time of the Commission hearing.

(40) On April 9, 2002, Arrington filed a compulsory pooling application for the E/2 of Section 25 with the Division which was set for hearing on May 16, 2002.

(41) On May 1, 2002, the Division cancelled its approval of Arrington's APD for its Glass-Eye Midge 25 Well No. 1 dedicated to the E/2 of Section 25.

FINDING BY THE DIVISION

(42) After being afforded an opportunity for a detailed review of TMBR/Sharp's geology including its 3-D seismic data, Ocean declined to participate based on its belief that the Chester formation would be structurally too low and therefore too wet (water saturation too high to be commercially production of hydrocarbons).

(43) Ocean should not be allowed to take advantage of the fact that TMBR/Sharp had already developed the Big Tuna Prospect and offered Ocean an opportunity to participate.

(44) Ocean's and Arrington's applications are inconsistent with and contrary to the Commission determination that TMBR/Sharp had the prior right to drill the wells which it sought to drill in August 2001 until Arrington interfered with that right.

(45) But for Arrington's blocking of TMBR/Sharp's permit, TMBR/Sharp would have received its permits to drill and would have already drilled its wells in the N/2 of Section 25 and the E/2 of Section 23. The Commission has agreed with TMBR/Sharp which is now entitled to proceed with the drilling of its wells without further interference by Ocean and Arrington.

(46) In accordance with Commission Order R-11700-B, TMBR/Sharp is now entitled to drill and complete this well as approved by the Division and obtain a compulsory pooling order without further interference from Arrington or Ocean. The issuance of a compulsory pooling order to Ocean or Arrington will be in direct conflict with Commission Order R-11700-B and will preclude TMBR/Sharp from receiving and benefitting from an approved APD to which it was entitled and would have received but for the wrongful actions of Arrington.

TECHNICAL CASES

TMBR/Sharp's technical case:

(47) Commencing in 1995, Louis Mazzullo, began developing a geological model of a multisection area known as the "Big Tuna" Prospect which included Sections 23, 24, 25 and 26 of T16S, R35E. This study included the Wolfcamp, Atoka and portions of the upper Mississippi ("Chester") formations. **Transcript pages 116-118**[1]

(48) By 1997, Mr. Mazzullo had included 2-D and 3-D seismic data along with conventional geological (log) data, and concluded that the best opportunity for deep gas production from the "Chester formation" was to locate and drill wells in bowl shaped structure features which could be identified and located using 3-D Seismic data. As a result, Mr. Mazzullo identified "Chester bowls" in the SW/4 of Section 24, the NW/4 of Section 25, and the NE/4 of Section 23.

(49) Mr. Mazzullo shared his geological conclusions with a group of investors (collectively "TMBR/Sharp") who signed a Joint Operating Agreement in 1998.

(50) On January 31, 2001, after being afforded a private, detailed review of TMBR/Sharp's geology including its 3-D seismic data, Ocean declined to participate based on its belief (Mr. John Silver) that the Chester formation would be structurally too low and therefore too

[1]Transcript references are to the May 16-17, 2002 hearing of the OCD in case numbers 12,816; 12,841; 12,859; and 12,860.

wet (water saturation too high to allow for commercial production of hydrocarbons)[2] **Transcript page 118**

(51) On May 29, 2001, TMBR/Sharp, using Mr. Mazzullo's geological interpretation, then successfully drilled and completed the Blue Fin 24 Well No. 1 in the SW/4 of Section 24 for production from one of the low Chester bowls with first production on June 29, 2001.

(52) The success of the Blue Fin 24 Well No. 1, confirmed the accuracy of Mr. Mazzullo's geological model.

(53) Mr. Mazzullo predicted that a second Chester bowl is located in the NW/4 of Section 25 and that a third bowl is located between the north/south dividing line between the SW/4 and the SE/4 of Section 25. **See Transcript Page 142 (TMBR/Sharp's Exhibit 18-D)**

(54) Mr. Mazzullo further concludes:

(a) that each of these three Chester Bowls is a separate and distinct reservoir and they are separated by fault blocks; and

(b) that it would be necessary to drill a well in each bowl.

Ocean's technical case:

(55) On about January 31, 2001, John Silver on behalf of Ocean, was given a detailed review of TMBR/Sharp's geology (Mr. Mazzullo) including its 3-D seismic data, and concluded that Ocean should not participate based on his belief that the Chester formation would be structurally too low and therefore too wet (water saturation too high to allow for commercial production of hydrocarbons.)

(56) At the Hearing, Mr. Silver presented an isopach map of the Brunson Sand, being the lower portion of the Morrow formation, which included the Atoka (Brunson sand) wells and the Chester wells (which Ocean called the Austin). **(Ocean Exhibit 10)**

(57) Mr. Silver's isopach map concludes that there are no Brunson sand Wells in Section 23, 24, 25, or 26 but still seeks to seeks to extend the Brunson sand isopach into the W/2 of Section 25.[3] **Ocean Exhibit 17.**

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[2]Ocean on occasions calls the Chester, part of the lower Morrow, Transcript page 118. At the hearing Ocean referred to the "Chester bowls" as the Lower Mississippian Lime (See Ocean Exhibits 12, 13, 14)

[3]Mr. Mazzullo disagrees and has concluded that the Brunson Sand is not productive in Sections 23, 24, 25, 26.

(58) Mr. Silver's Brunson sand map (**Ocean Exhibit 17**) condemns the NE/4 of Section 25.

(59) Mr. Silver presented Time Structure Maps of the Austin, (Lower Mississippian Lime (**Ocean Exhibit 12**) and the Brunson interval of the Lower Morrow (**Ocean Exhibit 15**) both of which show three distinct "pods" which substantially agree with Mr. Mazzullo's time structure Map of his "Chester Bowls". **(TMBR/Sharp Exhibit 18-D).**

(60) Both TMBR/Sharp's and Ocean's maps demonstrate that the Chester Bowl in the S/2 of Section 25 is split between the SW/4 and the SE/4.

(61) Mr. Silver also presented an Austin Isopach (**Ocean Exhibit 17**) on which he drew the productive limits to connect together the Chester bowls in the SW/4 of Section 24 to the two Chester bowls in the NW/4 and the S/2 of Section 25.

(62) If Mr. Silver's interpretation is correct, then a single well in the NW/4 of Section 25 will drain the entire section including the SE/4 of Section 25 which will not share in production if Ocean's W/2 spacing unit is approved.

(63) Arrington limited its technical presentation at the hearing to presenting an isopach and structure map of the Brunson Sand, being the lower portion of the Morrow foundation which included the Atoka (Brunson sand) wells and the Chester wells (which Ocean called the Austin) **(Ocean Exhibit 10).**

(64) Arrington extends the Brunson sand from the Ocean well located in the NW/4 of Section 10 southward through Section 25.

(65) Contrary to Mr. Silver's map, Arrington concludes that the NE/4 of Section 25 is better than the NW/4 and the SW/4 of Section 25 is better than the NW/4. **(See Arrington Exhibit 8)**

Division Decision

(66) The Division finds that:

either in SW

(a) If Mr. Silver's interpretation is correct, then a single well in the NW/4 of Section 25 will drain the entire section including the SE/4 of Section 25 which will not share in production if Ocean's W/2 spacing unit is approved.

(b) Recent pressure data from the TMBR/Sharp Blue Find 24 Well No. 1 tends to demonstrate that the Chester Bowls are not connected as assumed by Ocean and that at least two wells will be needed in Section 25.

if the #2 well in the SW/4

(c) Arrington's Morrow maps support either "lay-down" or "stand-up" spacing units.

(d) Spacing units consisting of the N/2 and the S/2 of Section 25 will afford the opportunity for owners in each of the 4 quarter sections to share equitably in producing their respective shares of production from the reservoirs in question.

(67) Cases 12859, 12860 and 12841 have been made moot by the Commission's decision approving TMBR/Sharp's APD's for the N/2 of Section 25 and the E/2 of Section 23.

(68) The Commission's decision in favor of TMBR/Sharp eliminates the need for the Division to decide the Ocean and Arrington compulsory pooling cases, which attempt to pool spacing units in conflict with TMBR/Sharp's spacing unit.

(69) Ocean and Arrington's application are inconsistent with and contrary to the Commission's determination that TMBR/Sharp has the prior right to drill the wells which it sought to drill in August 2001 until Arrington interfered with that right.

(70) But for Arrington's blocking of TMBR/Sharp's permit, TMBR/Sharp would have received its permits to drill and would have already drilled its wells in the N/2 of Section 25 and the E/2 of Section 23.

(71) The Commission has agreed with TMBR/Sharp, who is now entitled to proceed with the drilling of its wells without further interference by Ocean and Arrington.

(72) The "New Mexico Oil and Gas Act" allows for the compulsory statutory pooling of interest in a spacing unit after the well has been drilled. TMBR/Sharp obtained the voluntary agreement of 82% of the interest owners; it intended to drill its NW/4 Section 25 well first, and then pool the remaining interest owners who either have refused to participate on a voluntary basis or who have not yet been contacted because they cannot be located.

(73) TMBR/Sharp should be designated the operator of the subject well and the N/2 unit.

(74) All parties agreed at the hearing that overhead rates of $6000.00 while drilling and $600.00 while producing should be adopted in this case.

(75) In addition, all parties proposed that a risk penalty of 200 percent be assessed against any non-consenting working interest owners.

(76) To avoid the drilling of unnecessary wells, to protect correlative rights, to avoid waste, and to afford to the owner of each interest in the above-described unit the opportunity to recover or receive without unnecessary expense its just and fair share of hydrocarbons, the application of TMBR/Sharp should be approved by pooling all uncommitted mineral interests, whatever they may be, within this unit.

(77) After pooling, uncommitted working interest owners are referred to as "non-consenting working interest owners." Any non-consenting working interest owner should be afforded the opportunity to pay its share of the estimated costs to the operator in lieu of paying its share of reasonable well costs out of production.

(78) Any non-consenting working interest owner should be afforded the opportunity to pay its share of estimated well costs first to TMBR/Sharp, as the operator, in lieu of paying its share of reasonable well costs out of production.

(79) Any non-consenting working interest owner who does not pay its share of estimated well costs should have withheld from production its share of the reasonable well costs plus an additional 200 percent thereof as a reasonable charge for the risk involved in the drilling of the well.

(80) Any non-consenting working interest owner should be afforded the opportunity to object to the actual well costs but actual well costs should be adopted as the reasonable well costs in the absence of such objection.

(81) Following determination of reasonable well costs, any non-consenting working interest owner who has paid its share of estimated costs should pay to the operator any amount that reasonable well costs exceed estimated well costs and should receive from the operator any amount that paid estimated well costs exceed reasonable well costs.

(82) Six Thousand Dollars ($6,000.00) per month while drilling and $600.00 per month while producing should be fixed as reasonable charges for supervision (combined fixed rates); the operator should be authorized to withhold from production the proportionate share of such supervision charges attributable to each non-consenting working interest, and in addition thereto, the operator should be authorized to withhold from production the proportionate share of actual expenditures required for operation the subject well, not in excess of what are reasonable, attributable to each non-consenting working interest.

(83) All proceeds from production from the subject well which are not disbursed for any reason should be placed in escrow to be paid to the true owner thereof upon demand and proof of ownership.

(84) Should all the parties to this forced pooling order reach voluntary agreement subsequent to entry of this order, this order shall thereafter be of no further effect.

(85) TMBR/Sharp as the operator of the well and this unit shall notify the Director of the Division in writing of the subsequent voluntary agreement of all parties subject to the pooling provisions of the order.

IT IS THEREFORE ORDERED THAT:

1. Pursuant to the application of TMBR/Sharp in Case No. 12816, all uncommitted mineral interests from the surface to the base of the Mississippi formation underling

the following acreage in Section 25, Township 16 South, Range 36 East, Lea County, New Mexico, are hereby pooled in the following manner:

a. the N/2 to form a 320-acre gas spacing and proration unit for formation and/or pools developed on 320-acre spacing within that vertical extent, including the Townsend-Morrow Gas Pool and the Townsend-Mississippi Gas Pool.

2. This spacing and proration unit is to be dedicated to TMBR/Sharp's Blue Fin "25" Well No. 1 which is being drilled and will be completed at a standard location within Unit E of this section.

3. Ocean Energy, Inc.'s application in Cases 12841 and 12860 are hereby **denied.**

4. David H. Arrington Oil & Gas, Inc.'s application in Cases 12859 is hereby **denied.**

5. TMBR/Sharp Drilling, Inc. is hereby designated the operator of the subject well and unit.

6. TMBR/Sharp, as operator of this unit, has commenced drilling the well and shall hereafter continue drilling the well with due diligence to a depth sufficient to test the Morrow formation.

7. Should the well not be drilled to completion or abandoned within 120 days after commencement, the operator shall appear before the Division Director and show cause why Ordering Paragraph (1) should not be rescinded.

8. Within 30 days from receiving a copy of this Order with schedule of estimated well costs attached, any non-consenting working interest owner shall have the right to pay its share of estimated well costs to TMBR/Sharp in lieu of paying its share of reasonable well costs out of production, and any such owner who pays its share of estimated well costs as provided above shall remain liable for operation costs but shall not be liable for risk charges.

9. The operator shall furnish the Division and each known non-consenting working interest owner an itemized schedule of actual well costs within 90 days following completion of the well. If no objection to the actual well costs is received by the Division and the Division has not objected within 45 days following receipt of said schedule, the actual well costs shall be the reasonable well costs; provided however, if there is objection to actual well costs within the 45-day period the Division will determine reasonable well costs after public notice and hearing.

10. Within 60 days following determination of reasonable well costs, any non-consenting working interest owner who has paid its share of estimated well costs in advance as provided above shall pay to the operator its share of the amount that reasonable well

costs exceed estimated well costs and shall receive from the operator its share of the amount that estimated well costs exceed reasonable well costs.

11. The operator is hereby authorized to withhold the following costs and charges from production:

a. the proportionate share of reasonable well costs attributable to each non-consenting working interest owner who has not paid its share of estimated well costs within 30 days from the date the schedule of estimated well costs is furnished; and

b. as a charge for the risk involved in the drilling of the well, 200 percent of the above costs.

c. The operator shall distribute the costs and charges withheld from production to the parties who advanced the well costs.

d. $6000.00 per month while drilling and $600.00 per month while producing are hereby fixed as reasonable charges for supervision (combined fixed rates); the operator is hereby authorized to withhold from production the proportionate share of such supervision charges attributable to each non-consenting working interest, and in addition thereto, the operator is hereby authorized to withhold from production the proportionate share of actual expenditures required for operation such well, not in excess of what are reasonable, attributable to each non-consenting working interest.

e. Any unleased mineral interest shall be considered a seven-eights (7/8) working interest and a one-eighth (1/8) royalty interest for the purpose of allocating costs and charges under the terms of this order.

f. Any wells costs or charges which are to be paid out of production shall be withheld only from the working interest's share of production, and no costs or charges shall be withheld from production attributable to royalty interests.

g. All proceeds from production from the well which are not disbursed for any reason shall immediately be placed in escrow in Lea County, New Mexico, to be paid to the true owner thereof upon demand and proof of ownership, the operator shall notify the Division of the name and address of the escrow agent within 30 days from the date of first deposit with the escrow agent.

h. Should all parties to this forced pooling order reach voluntary agreement subsequent to entry of this order, this order shall thereafter be of no further effect.

i. The operator of the well and unit shall notify the Director of the Division in writing of the subsequent voluntary agreement of all parties subject to the forced pooling provisions of this order.

j. Jurisdiction is hereby 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

MILLER, STRATVERT & TORGERSON, P.A.

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* NEW MEXICO BOARD OF SPECIALIZATION RECOGNIZED SPECIALIST IN NATURAL RESOURCES - OIL & GAS LAW
** NEW MEXICO BOARD OF SPECIALIZATION RECOGNIZED SPECIALIST IN REAL ESTATE LAW

June 6, 2002

HAND-DELIVERED
Mr. Michael Stogner
New Mexico Oil Conservation Division
1220 South St. Francis
Santa Fe, New Mexico 87505

Re: NMOCD Case Nos. 12816, 12841, 12859 and 12860; Applications of TMBR/Sharp Drilling, Inc., Ocean Energy, Inc. and David H. Arrington Oil and Gas, Inc. for Compulsory Pooling, Lea County, New Mexico

Dear Mr. Stogner:

Enclosed in hard copy and on a disk is a proposed draft order for your review in connection with the above-referenced matter. Please feel free to edit as you deem appropriate.

Thank you for your assistance.

Very truly yours,

MILLER, STRATVERT & TORGERSON, P.A.

J. Scott Hall /glb

J. Scott Hall

JSH/glb
Enclosure
cc: Counsel of Record
David Brooks, Esq.
David H. Arrington

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 OCEAN ENERGY, INC. FOR COMPULSORY POOLING, LEA COUNTY, NEW MEXICO. — **CASE NO. 12841**

APPLICATION OF TMBR/SHARP DRILLING, INC. FOR COMPULSORY POOLING, LEA COUNTY, NEW MEXICO. — **CASE NO. 12816**

APPLICATION OF DAVID H. ARRINGTON OIL & GAS, INC. FOR COMPULSORY POOLING, LEA COUNTY, NEW MEXICO. — **CASE NO. 12859**

APPLICATION OF OCEAN ENERGY, INC. FOR COMPULSORY POOLING, LEA COUNTY, NEW MEXICO. — **CASE NO. 12860**

ORDER OF THE DIVISION

(ARRINGTON'S PROPOSED DRAFT)

BY THE DIVISION:

THIS MATTER came on for hearing at 8:15 a.m. on May 16, 2002 at Santa Fe, New Mexico before examiner Michael E. Stogner on the Application of David H. Arrington Oil & Gas, Inc. for compulsory pooling, the Application of Ocean Energy, Inc. for compulsory pooling and the Application of TMBR/Sharp Drilling, Inc. for compulsory pooling in Section 25, Township 16S, Range 35E, NMPM, Lea County, New Mexico.

Now on this _____ day of June, 2002, the Division Director, having considered the testimony, the record and the recommendations of the Examiner,

FINDS THAT:

1. Due public notice has been given and the Division has jurisdiction of these cases and the subject matter thereof.

2. In Case No. 12859, David H. Arrington Oil and Gas, Inc., ("Arrington"), seeks an order pooling all mineral interests underlying the E/2 of Section 25, Township 16 South, 25 East, to form a standard 320 acre standup gas spacing and proration unit for any pool developed on 320 acre spacing within that vertical extent, including the undesignated Shoe Bar-Atoka Gas Pool, undesignated Townsend-Morrow Gas Pool and undesignated North Townsend-Mississippian Gas Pool. Arrington also seeks to pool the NE/4 of said Section 25 to form a standard 160 acre spacing and proration unit for any and all formations and/or pools developed on 160 acre spacing, as well as the E/2 NE/4 to form a standard 80 acre standup oil spacing and proration unit for any and all formations and/or pools developed on 80 acre spacing within that vertical extent. Arrington proposes to dedicate the pooled units to its Glass Eyed Midge 25 Well No. 1 to be drilled at a standard 320 acre spacing and proration unit gas well location 803' FNL and 962' FEL (Unit A) in the NE/4 of Section 25.

3. In Case No. 12841, Ocean Energy, Inc., ("Ocean"), seeks to pool all interests from the surface to the base of the Mississippian formation underlying the W/2 of said Section 25 to form a standard 320 acre gas spacing and proration unit for all formations and pools developed on 320 acre spacing, including but not limited to the undesignated Townsend-Morrow Gas Pool and the undesignated Townsend-Mississippian Gas Pool. Ocean proposes to dedicate the pooled units to its Triple Hackle Dragon 25 Well No. 1 to be drilled at a standard 320 acre gas well location in the SW/4 NW/4 (Unit E) of Section 25. Ocean also seeks the establishment of escrow accounts for the purpose of holding and disbursing funds pending resolution of a title dispute affecting the NW/4 of said Section 25.

4. In Case No. 12860, as an alternative application, Ocean Energy, Inc. seeks to pool all interests from the surface to the base of the Mississippian formation also underlying the W/2 of Section 25 to form a standard 320 acre gas spacing and proration unit for all formations and pools developed on 320 acre spacing which it proposes to dedicate to its Triple Hackle Dragon 25 Well No. 2 to be drilled at a 320 acre gas well location in the NE/4 SW/4 (Unit K) of Section 25.

5. In Case No. 12816, TMBR/Sharp Drilling, Inc., ("TMBR/Sharp"), seeks to pool all interests from the surface to the base of the Mississippian formation underlying the N/2 of said Section 25 to form a standard 320 acre gas spacing and proration unit for all formations developed on 320 acre spacing, including the Townsend-Morrow and Townsend-Mississippian Gas Pools. TMBR/Sharp proposes to dedicate the unit consisting of the N/2 of Section 25 to its Blue Fin 25 Well No. 1 which it began drilling on May 7, 2002.

6. There are interest owners in each of the proposed spacing and proration units covering the E/2, the N/2 and W/2 of Section 25 who have not agreed to pool their interests.

7. The four competing applications affecting said Section 25 were consolidated for hearing on May 16, 2002.

8. On July 17, 2001, Arrington filed an Application for Permit to Drill (Form C-101) for its proposed Triple Hackle Dragon 25 Well No. 1 to be located in the W/2 of Section 25, Township 16 South, Range 25 East, Lea County, New Mexico at a standard location in the SW/4 NW/4 (Unit E), 750' FWL and 1815' FNL of the Section. The Division's District I office in Hobbs approved Arrington's APD on July 17, 2001.

9. On or about August 7, 2001, TMBR/Sharp filed an Application for Permit to Drill (Form C-101) for its proposed Blue Fin 25 Well No. 1 to be located in the N/2 of Section 25, Township 16 South, Range 25 East, Lea County, New Mexico, at a standard location in the SW/4 NW/4 (Unit E), 924' FWL and 1913' FNL of the Section. On August 8, 2001, the Division's District I office in Hobbs denied the TMBR/Sharp APD due to the previous issuance of the APD for Arrington's proposed Triple Hackle Dragon 25 Well No. 1.

10. On November 29, 2001, Arrington filed an Application for Permit to Drill (Form C-101) for its proposed Glass Eyed Midge 25 Well No. 1 to be located in the NE/4 of Section 25, Township 16 South, Range 35 East, Lea County, New Mexico. Arrington simultaneously filed a C-102 Acreage Dedication Plat form proposing to dedicate the E/2 of said Section 25 to its proposed well. On December 17, 2001, the Division's District I office in Hobbs approved Arrington's Permit to Drill the Glass Eyed Midge 25 Well No. 1.

11. At the time of the filing of the APDs by both Arrington and TMBR/Sharp, there were owners of other interests in the N/2 and E/2 of Section 25, respectively, who had not voluntarily agreed to participate in the drilling of the proposed wells. Neither Arrington or TMBR/Sharp had consolidated the interests of all of the non-participating owners in the conflicting spacing units either by way of a voluntary agreement, communization agreement or compulsory pooling order.

12. The APDs described in findings 8 and 9, above, were the TMBR/Sharp and Arrington APDs that were the subject of the application filed by TMBR/Sharp in Case No. 12731 heard by the Division on October 18, 2001. Case No. 12731 was consolidated with Case No. 12744 and resulted in the issuance by the Division on December 13, 2001 of Order No. R-11700 that denied TMBR/Sharp's application to stay Arrington from commencing drilling operations and to set aside the District supervisor's decision denying approval of TMBR/Sharp's APD. Case Nos. 12731 and 12744 were subsequently heard, *de novo*, by the Oil Conservation Commission on March 26, 2002 which resulted in the issuance on April 26, 2002 of the Commission's Order No. R-11700-B. That Order granted TMBR/Sharp's application in Case No. 12731 to void the permits to drill obtained by Arrington and further ordered that the Division's District I office approve the APD originally filed by TMBR/Sharp in August, 2001.

13. The drilling permits in Case Nos. 12731 and 12744 addressed by Order No. R-11700-B are not at issue in these consolidated cases currently before the Division. Moreover, it is noted that Order No. R-11700-B states: "An application for a permit to drill serves different objectives than an application for compulsory pooling and the two proceedings should not be confused." That Order goes on to say: "Issuance of the permit to drill does not prejudge the results of a compulsory pooling proceeding, and any suggestion that the acreage dedication plat attached to an application to drill somehow "pools" acreage is expressly disavowed."

14. On April 27, 2002, TMBR/Sharp filed a Motion to Continue Case No. 12816 and to dismiss Case Nos. 12859, 12860 and 12841. In its motion, TMBR/Sharp cited to Order No. R-11700-B and stated: "The Commission decision in favor of TMBR/Sharp eliminates the need for the Division to decide the Ocean and Arrington compulsory pooling cases," and "precludes the Division from entering an Order granting the relief sought in Cases 12841, 12859 and 12860." TMBR/Sharp's Motion to Continue and to Dismiss was denied by the Division's examiner on May 14, 2002.

15. At the May 14, 2002 hearing on the TMBR/Sharp motion, it was learned that TMBR/Sharp had begun drilling its Blue Fin 25 Well No. 1 on May 7, 2002 without having consolidated the unjoined interests and without allowing the Division to determine the final configuration of the spacing and proration units in Section 25.

16. When deliberating on any application for compulsory pooling under NMSA 1978 §§ 70-2-17(C) and 70-2-18, the Division will consider evidence relating to, among other matters: (1) the presence or absence of a voluntary pooling agreement; (2) whether a reasonable and good faith effort was made to obtain the voluntary participation of others; (3) reasonableness of well costs; (4) geologic and engineering evidence bearing on the avoidance of waste and the protection of correlative rights, including, where applicable, avoiding the drilling of unnecessary wells; (5) the assessment of a risk penalty; and (6) whether the application is otherwise in the interest of conservation.

17. None of these issues were included within the scope of the applications in Case Nos. 12731 and 12744 referenced in paragraph 12 above, and consequently no geologic or engineering evidence was presented in either the Division Examiner or Commission hearings in Case Nos. 12731 and 12744.

18. On May 15, 2002, Arrington filed with the Division its Application To Reinstate Drilling Permit, (NMOCD Case No. 12876; Application of David H. Arrington Oil and Gas, Inc. to Reinstate Drilling Permit, Lea County, New Mexico), whereby it seeks an order directing the Division's District I office to reinstate the drilling permit for its Glass Eyed Midge 25 Well No. 1 previously approved on December 17, 2001. A hearing on Arrington's application in that matter remains pending.

19. Evidence presented by Arrington's Landman witness established that Arrington owns or controls approximately 17.348% of the working interests underlying the E/2 of Section 25 and that the remainder of the unjoined interests consist of working interests owned by Yates Petroleum Corporation and certain unleased mineral interests. The evidence further established that Arrington has owned its lease interests in the E/2 of said Section 25 since March of 2001 and that its interests were unaffected by the title dispute currently pending between Arrington and TMBR/Sharp relating to lands in the NW/4 of Section 25 that is the subject of litigation pending before the 5th Judicial District Court in Lovington, New Mexico. Accordingly, Arrington was eligible to become the operator of the Glass Eyed Midge 25 Well No. 1 and properly received the permit to drill that was issued to it by the Division's Hobbs District office on December 17, 2001.

20. TMBR/Sharp has taken the position both in the District Court litigation and before the Division that the filing of a C-102 acreage dedication plat is sufficient to "consolidate" interests and correspondingly determine the unit configuration which will in turn determine the ultimate development of the entirety of Section 25. It is noted, however, that TMBR/Sharp's position is contra-indicated by the express findings and conclusions of Order No. R-11700(B) which states, at paragraph 33, as follows: "An application for a permit to drill serves different objections than an application of compulsory pooling and the two proceedings should not be confused." Therefore, consistent with the Commission's determination, Order No. R-11700(B) did not serve to adjudicate the conflicting claims of the parties or approve, by implication or otherwise, the creation of a N/2 spacing unit for TMBR/Sharp's Blue Fin 25 Well No. 1. A determination of the proper configuration of the spacing units and the further development of Section 25 must instead be based upon land, geologic and engineering evidence having direct relevance to avoiding the drilling of unnecessary wells, or to protect correlative rights, or to prevent waste.

21. Arrington is an owner of oil and gas working interests within the E/2 unit. Arrington has the right to drill and proposes to drill its Glass Eyed Midge 25 Well No. 1 (the "proposed well") to the common source of supply at a standard well location within the unit.

22. Arrington proposes to complete its Glass Eyed Midge 25 Well No. 1 in the Brunson Sand interval of the Atoka formation.

23. TMBR/Sharp presented testimony through its landman witnesses that through an operating agreement it entered into with Ameristate Oil and Gas Company in July of 1988, it obtained the right to drill in the NW/4 of Section 25 under oil and gas leases it executed in 1997 by Madeline Stokes and Irma Stokes Hamilton that covered portions of lands in Sections 23 and 25, among others. The evidence further established that David H. Arrington Oil and Gas, Inc.'s landman, James D. Huff, acquired top leases from Madeline Stokes and Irma Stoked Hamilton in 2001. The validity of the 1997 lease

to Ameristate and Arrington's top lease are currently pending before the Fifth Judicial District Court in Lovington. Also at issue in that litigation is whether the filing of a C-102 form with the Division's District I office in Hobbs for TMBR/Sharp's Blue Fin 24 No. 1 Well in Section 24, T16S, R35E, was sufficient to perpetuate TMBR/Sharp's leases from Madeline Stokes and Irma Stokes Hamilton covering portions of lands in Section 23 and in Section 25, among others.

24. TMBR/Sharp's land witness also testified that the Fifth Judicial District Court has issued a ruling establishing the existence of *force majeure* conditions that obviated the need for TMBR/Sharp to proceed with the drilling of the Blue Fin 25 Well No. 1 in order to satisfy the continuous drilling obligations under the Stokes/Hamilton oil and gas lease.

25. Further testimony established that TMBR/Sharp filed its application for compulsory pooling in Case No. 12816 on January 28, 2002. It was further established that the first effort made by TMBR/Sharp to obtain the voluntary participation of the other interest owners in the N/2 of Section 25 was made on January 22, 2002 when it sent a well proposal letter to James D. Huff. Arrington's land witness testified that James D. Huff has previously assigned his entire interest in the N/2 of Section 25 to Arrington on September 17, 2001, effective March 27, 2001. The assignment by Huff to Arrington was filed of record with the Lea County Clerk's office on September 19, 2001. The testimony further established that TMBR/Sharp made no effort to obtain the voluntary participation of David H. Arrington Oil and Gas, Inc. or Dale Douglas until its well proposal letter dated May 1, 2002. It was also established that TMBR/Sharp made no effort to obtain the voluntary participation of a number of unleased mineral interest owners, including, among others, Mark and Bonnie Caldwell, Mr. and Mrs. R. N. Williams, George O'Brien and Mary Francis Antweil.

26. TMBR/Sharp's geology witness testified that its primary objective for its Blue Fin 25 Well No. 1 was the "Chester" interval of the Upper-Mississippian formation, with secondary targets in the Wolfcamp and then Atoka formations. TMBR/Sharp's geology witness also noted that there is disagreement over nomenclature for the various formations in the area and that the Morrow and Chester formations are often referred to interchangeably.

27. TMBR/Sharp's geologist testified that with the aid of 2-D seismic data he identified two isolated "bowls" or "closed lows" consisting formational depressions that were filled in with Brunson limestone cherty detritus intermingled with other eroded sandstones. The largest of these bowls is located primarily in the NW/4 of Section 25 with a smaller bowl located in the NE/4 SW/4 and extending slightly into the SE/4 of Section 25. According to TMBR/Sharp's geologist, based on well data obtained from the TMBR/Sharp Blue Fin 24 Well No. 1, these Chester bowls are believed to approximately 24 feet thick and having a porosity of 24%. TMBR/Sharp's geologist testified that he believed the two bowls he identified were not in communication with one another, and

therefore, the geologic features could be most effectively drained with one well located in the NW/4 and a second well located in the SW/4.

28. TMBR/Sharp's geologist testified that the depositional mechanism for the localized Chester reservoirs were not related to channel development but rather to the localized erosion along deep faults affecting Chester Limestone rocks shortly after their deposition and prior to the deposition of the Morrow. TMBR/Sharp's geologist testified that determining the exact location, size and shape of Chester formation reservoirs is more difficult than trying to determine locations, widths and thicknesses of channels in the Morrow because they are not fluvially derived materials with established with continuity that can be traced from conventional subsurface data. Accordingly, TMBR/Sharp's geologist placed primary emphasis on 2-D seismic data utilized to locate the existence of faults along trends outside those areas of established Chester production. TMBR/Sharp's geologist testified that he compared his analysis of 2-D seismic data with a series of maps based on 3-D seismic data prepared by an independent consulting geophysicist who identified a series of low areas as potential gathering points for Chester reservoir rock. However, TMBR/Sharp did not present evidence of the geophysicist's maps or his conclusions with respect to the Chester reservoir in Section 25.

29. TMBR/Sharp's geologist established that the Atoka and Chester thicken and ascend toward the north to the point where the Chester pinches out. However, the geologic and geophysical evidence presented was insufficient to determine the location and extent of the Chester reservoir to the south through Section 25.

30. The TMBR/Sharp geologist testified that he believed the Chester reservoir features identified by him in Sections 24 and 25 were localized and not in communication with each other, and drained only 36 acre and 54 acre areas respectively. Moreover, the geologist witness testified that he had not taken into consideration any of the porosity, bottom hole pressure, water saturation or other production data from the Blue Fin 24 No. 1 Well in Section 24 to substantiate his conclusions with respect to the areal extent of the Chester reservoirs identified in Sections 24 and 25.

31. While TMBR/Sharp's geologist testified a single well would adequately drain reserves in the Chester bowls in the N/2 of Section 25, no testimony was offered with respect whether a single well in the NW/4 would be capable of draining reserves from the Morrow and Mississippian formations underlying the NE/4 of Section 25.

32. Utilizing producing rate data, bottom hole pressure and surface pressure data, porosity and water saturation estimates and reserve estimates provided by TMBR/Sharp's engineering witness, Ocean Energy presented additional evidence that established that a reasonable estimate of the area drained by the Blue Fin 24 No. 1 Well in Section 24 is 219 acres. Accordingly, the preponderance of the evidence established that the areal extent of the reservoirs portrayed on the TMBR/Sharp geologic exhibits do not accurately reflect the size of the Chester reservoirs or the drainage areas for the Blue

Fin 24 No. 1 Well or that can reasonably be expected to be encountered by the Blue Fin 25 No. 1 Well.

33. The net sand isopach map of the Chester formation presented by Ocean Energy established that the areal extent of that reservoir is much more extensive than shown by TMBR/Sharp's geologic maps. Accordingly, a preponderance of the geologic evidence establishes that the Chester reservoir is located along a northwest to southeast trend underlying the W/2 of Section 25 and that those reserves are best developed by way of a stand-up W/2 spacing unit dedicated to a single well in the NW/4.

34. Ocean Energy's witnesses testified that if N/2 and S/2 lay-down spacing units are established for Section 25 it will be necessary to immediately drill an additional well in the SW/4 of said Section 25 to preserve its lease and to protect its correlative rights. As a consequence there would be a reasonable probability that three wells would be completed within the same reservoir underlying the W/2 of Section 25 and the SW/4 of Section 24, all situated within approximately four thousand feet.

35. Arrington's geology witness testified that his company had been involved in approximately fifteen wells specifically targeting the Chester deposits in trenches or grabens in the vicinity of the subject lands and that data derived from those wells established that production from Chester reservoirs is not confined to the low features.

36. Arrington's geology witness presented a Morrow Limestone structure map showing the existence of two northwest to southeast trending structures known as the North Shoe Bar and East Shoe Bar fields.

37. The primary target for the Arrington Glass Eyed Midge 25 No. 1 Well which it identifies as the Lower Atoka Brunson Sand is a very prolific sand that is produced across multiple townships in the immediate vicinity of the subject lands. The existence of the Atoka Brunson reservoir in the E/2 of Section 25 was established using actual subsurface well control data.

38. The geologic evidence presented by Arrington further established that all of the locations for potential Morrow formation development are located exclusively within the W/2 of Section 25. Moreover, the evidence establishes that a structural low is situated between the Morrow prospective area in the W/2 and the Brunson Atoka feature underlying the E/2 of Section 24 running along a north south access through the center of Section 25.

39. The geologic evidence further establishes that the Glass Eyed Midge 25 Well No. 1 proposed to be located in the NE/4 of Section 25 presents the only potential stand alone development prospect for the Brunson Atoka Sand formation in the Section. Moreover, the geologic evidence and isopac map presented by Arrington establishes that the thickest portion of the Atoka formation Sandstone is located in the NE/4 of this

section and that a well located there would be best situated to produce the reserves underlying the E/2 of said Section 25.

40. The geologic evidence establishes that the location of the two barrier bar systems in the E/2 and W/2 of Section 25 respectively will preclude the Blue Fin 25 No. 1 Well from draining any of the Atoka Brunson reserves from the E/2 of the section.

41. The evidence further established that there is currently insufficient well control to justify the drilling of a well in the SE/4 of Section 25.

42. A preponderance of the evidence establishes that the Blue Fin 25 No. 1 Well located in the NW/4 of Section 25 is best situated to drain reserves from the Chester/Mississippian formation underlying the W/2 of the section.

43. A preponderance of the evidence establishes that if lay-down N/2 and S/2 320 acre spacing units are established for Section 25, there is a reasonable probability that the E/2 of said Section 25 would not be developed.

44. A preponderance of the geologic and engineering evidence establishes that Section 25 is best developed with two wells located on stand-up 320 acre spacing units comprised of the E/2 and the W/2 of Section 25. Moreover, the establishment of stand-up units is consistent with the predominant spacing and development pattern in the area.

45. Arrington's geology witness used extensive 3-D seismic data to verify its conclusions.

46. The geologic evidence presented by all the parties suggests that, at most, approximately 10% to 15 % of the Chester/Mississippian reservoir underlying the W/2 of Section 25 extends into the SE/4 of the section. The evidence further establishes that while there is a possibility a single well located in the NW/4 of Section 25 would drain those reserves underlying the SE/4, the correlative rights of those interest owners in the SE/4 could be protected by the drilling of an additional well in that quarter-section location if justified by reserve economics.

47. In addition, while the owners of the reserves underlying the SE/4 would have the opportunity to protect their correlative rights, the prevention of waste and the avoidance of unnecessary wells must be given precedence to the protection of correlative rights in any event.

48. A preponderance of the geologic and engineering evidence establishes that the reserves underlying the W/2 of Section 25 are best developed by way of a north-south 320 acre stand-up spacing unit, thereby avoiding the drilling of an additional well in the SW/4 of said Section 25.

49. The drilling of a well in the SW/4 of Section 25 would be unnecessary and would therefore constitute waste.

50. A preponderance of the evidence establishes that by creating a spacing unit comprised of the W/2 of Section 25 the drilling of an additional unnecessary well is avoided and waste is prevented.

51. In addition, subject to the competing claims of Arrington and TMBR/Sharp to the ownership of the oil and gas lease covering the NW/4 of Section 25, 100% of the interest owners in the W/2 of said Section 25 are in favor of the creation of a W/2 spacing unit for the Blue Fin 25 No. 1 Well.

52. The testimony and exhibits presented through Arrington's landman witnesses established that Arrington had made a good faith effort to obtain the voluntary joinder of the owners of the other working interests and the unleased mineral interests in the E/2 of Section 25 on a timely basis.

53. It has been the consistent, long-standing interpretation by the Division of NMSA 1978 § 70-2-18 (A) that an operator making application for an order pooling interests must affirmatively demonstrate that it had first made a good faith effort to obtain voluntary agreements pooling the lands. (*See* Morris, Richard, *Compulsory Pooling of Oil and Gas Interests in New Mexico,* 3 Nat. Resources J. 316 [1963].)

54. NMSA 1978 § 70-2-17 (C) provides, in part, as follows: "Where, however, such owner or owners have not agreed to pool their interests, and where one such separate owner, or owners, who has the right to drill has drilled or proposes to drill a well on said unit to a common source of supply, the division, to avoid the drilling of unnecessary wells or to protect correlative rights, or to prevent waste, shall pool all or any part of such lands or interest or both in the spacing or proration unit as a unit." That same section goes on to say "Such pooling order shall make definite provision as to any owner, or owners, who elects not to pay his proportionate share in advance for the prorata reimbursement solely out of production to the parties advancing the costs of the development and operation...".

55. NMSA 1978 § 70-2-18 (B) provides: "Any operator failing to obtain voluntary agreements, or failing to apply for an order of the division pooling the lands dedicated to the spacing or proration unit as required by this section, shall nevertheless be liable to account to and pay each owner of minerals or leasehold interest...either the amount to which each interest would be entitled if pooling had occurred or the amount to which each interest is entitled in the absence of pooling, whichever is greater."

56. The Division must construe §§ 70-2-17 (C) and 70-2-18 (A) and (B) in *pari materia.*

57. The evidence in this case establishes that TMBR/Sharp did not make a good faith effort to obtain voluntary agreements from the other owners of minerals or leasehold interests in the N/2 of Section 25 before it filed its application for compulsory pooling in Case No. 12816. Therefore, because it failed to satisfy the statutory pre-conditions of NMSA 1978 § 70-2-18 (A), TMBR/Sharp further failed to demonstrate it is entitled to an order granting any of the relief that may otherwise be afforded under § 70-2-17 (C), including pooling of the unleased and unjoined interests, establishing non-consent a non-consent penalty and making any provision for the reimbursement of development and operation costs. To do otherwise would be inconsistent with the provisions of NMSA 1978 § 70-2-18 (B).

58. At the conclusion of the hearing on the consolidated applications, Arrington moved to dismiss the TMBR/Sharp Application for Compulsory Pooling in Case No. 12816 for the reason that the Applicant failed to make a prima facie case that it was entitled to the relief requested. Moreover, by its January 25, 2002 Application, TMBR/Sharp, as a "working interest owner" sought to pool only unjoined "mineral interests". For these reasons, and the reasons set forth above, Arrington's motion to dismiss is well taken and should be **granted** and TMBR/Sharp's Application should otherwise be denied.

59. At the hearing, Ocean proposed that it be allowed to take over operations once the Blue Fin 25 Well No. 1 reaches total depth and that it further be allowed to complete the well.

60. To avoid the drilling of unnecessary wells, protect correlative rights, prevent waste and afford to the owner of each interest in the unit the opportunity to recover or receive without unnecessary expense its just and fair share of hydrocarbons, Ocean Energy's Application in Case No. 12841 should be approved by pooling all uncommitted interests, whatever they may be, within the W/2 unit.

61. Ocean Energy should be designated the operator of the Blue Fin 25 Well No. 1 immediately after the well reaches total depth, but before completion.

62. For the reasons set forth above, TMBR/Sharp is not entitled to avail itself of the provisions of NMSA 1978 § 70-2-17 (C) to obtain reimbursement out of production or otherwise as a party advancing the costs of development and operation. Similarly, under these circumstances, there is no reason to provide TMBR/Sharp with the opportunity to pay its share of pre-completion well costs to Ocean Energy as operator of the Blue Fin 25 Well No. 1 proportionate to the interest claimed by TMBR/Sharp in the NW/4 of Section 25.

63. Ocean Energy was not a party advancing the costs of development and operation for the Blue Fin 25 Well No. 1 and therefore should not recover a charge for the risk involved in drilling the well prior to the point of completion. However, from the

time it becomes operator of the well, Ocean Energy should be able to recover reasonable charges for completing the well and for supervision while operating the well.

64. Reasonable charges for completing the Blue Fin 25 No. 1 Well are $649,291.00.

65. Reasonable charges for supervision (combined fixed rates) should be fixed at $600.00 per month while producing, provided that this rate should be adjusted annually pursuant to § III.1.A(3) of the COPAS form titled "Accounting Procedure-Joint Operations". Ocean Energy, as operator, should be authorized to withhold from production the proportionate share of both the supervision charges and the actual expenditures required for operating the well, not in excess of what are reasonable, attributable to each non-consenting working interest.

66. From the time the Blue Fin 25 No. 1 Well reaches total depth and on a monthly basis thereafter, TMBR/Sharp and Arrington may each tender 50% of the completion costs and the monthly operating costs and supervision charges to Ocean Energy which, in-turn, shall place such payments into an escrow account pending judicial resolution of the dispute between Arrington and TMBR/Sharp over the ownership of the oil and gas lease covering the NW/4 of Section 25. Once judicial resolution of the ownership of the lease interests in the NW/4 is final, Ocean shall refund one-half of such escrowed proceeds to the non-prevailing party. Similarly, Ocean Energy shall place into escrow production proceeds equal to one hundred percent of the working interest attributable to the NW/4 pending judicial resolution of the ownership of the lease interests. Once judicial resolution is final, all of those escrowed proceeds shall be paid to the prevailing party. In the interim, Ocean Energy, as Operator, shall be responsible for the payment of all severance taxes and royalties attributable to the NW/4 of said Section 25.

67. To avoid the drilling of unnecessary wells, protect correlative rights, prevent waste and afford to the owner of each interest in the unit the opportunity to recover or receive without unnecessary expense its just and fair share of hydrocarbons, Arrington's application should be approved by pooling all uncommitted mineral interests, whatever they may be, within the E/2 unit.

68. Arrington should be designated the operator of the Glass Eyed Midge 25 Well No. 1 and of the E/2 unit.

69. After pooling, uncommitted working interest owners are referred to as non-consenting working interest owners. ("Uncommitted working interest owners" are owners of working interests in the unit, including unleased mineral interests, who are not parties to an operating agreement governing the unit). Any non-consenting working interest owner should be afforded the opportunity to pay its share of estimated well costs

of the proposed Glass Eyed Midge 25 Well No. 1 to the operator in lieu of paying its share of reasonable well costs out of production.

70. Any non-consenting working interest owner who does not pay its share of estimated well costs should have withheld from production its share of reasonable well costs plus an additional 200% thereof as a reasonable charge for the risk involved in drilling the Glass Eyed Midge 25 Well No. 1.

71. Any non-consenting working interest owner should be afforded the opportunity to object to the actual well costs, but actual well costs should be adopted as the reasonable well costs in the absence of objection.

72. Following determination of reasonable well costs, any non-consenting working interest owner who has paid its share of estimated costs should pay to the operator any amount that reasonable well costs exceed estimated well costs and should receive from the operator any amount that paid estimated well costs exceed reasonable well costs.

73. Reasonable charges for supervision (combined fixed rates) should be fixed at $6,000.00 per month while drilling and $600.00 per month while producing, provided that these rates should be adjusted annually pursuant to § III.1.A(3) of the COPAS form titled "Accounting Procedure-Joint Operations." The operator should be authorized to withhold from production the proportionate share of both the supervision charges and the actual expenditures required for operating the well, not in excess of what are reasonable, attributable to each non-consenting working interest.

74. All proceeds from production from the Glass Eyed Midge 25 No. 1 Well that are not disbursed for any reason should be placed in escrow to be paid to the true owner thereof on demand and proof of ownership.

IT IS THEREFORE ORDERED THAT:

1. Pursuant to the application of David H. Arrington Oil and Gas, Inc., all uncommitted mineral interests underlying the E/2 of Section 25, Township 16 South, Range 25 East, NMPM, Lea County, New Mexico, are hereby pooled, as follows:

(a) The E/2 to form a standard 320 acre gas spacing and proration unit for any and all formations and/or pools developed on 320 acre spacing within that vertical extent, which presently include but are not limited to the Undesignated Shoe Bar-Atoka Gas Pool, Undesignated Townsend-Morrow Gas Pool and the Undesignated Townsend-Mississippian Gas Pool;

(b) The NE/4 to from a standard 160 acre gas spacing and proration unit for any and all formations and/or pools developed on 160 acre spacing within that vertical extent; and

(c) The E/2 NE/4 to form a standard 80 acre oil spacing and proration unit for any and all formations and/or pools developed on 80 acre spacing within that vertical extent.

2. The units shall be dedicated to Arrington's Glass Eyed Midge 25 Well No. 1 to be drilled at a standard well location 803' FNL and 962' FEL in the NE/4 of Section 25.

3. The operator of the unit shall commence the Glass Eyed Midge 25 Well No. 1 on or before September 1, 2002, and shall thereafter continuing drilling the well with due diligence to test the Atoka, Morrow and Mississippian formations.

4. In the event the operator does not commence the Glass Eyed Midge 25 Well No. 1 on or before September 1, 2002, ordering paragraph one shall be of no effect, unless the operator obtains a time extension from the Division Director for good cause.

5. Should the Glass Eyed Midge 25 Well No. 1 not be drilled to completion, or be abandoned, within 120 days after commencement thereof, the operator shall appear before the Division Director and show cause why ordering paragraph one should not be rescinded.

6. Applicant Arrington is hereby designated the operator of the Glass Eyed Midge 25 Well No. 1 and of the units underlying the E/2 of Section 25.

7. After pooling, uncommitted working interest owners are referred to as non-consenting working interest owners. After the effective date of this Order, the operator shall furnish the Division and each known non-consenting working interest owner in the unit an itemized schedule of estimated well costs of the Glass Eyed Midge 25 Well No. 1.

8. Within thirty (30) days from the date the schedule of estimated well costs for the Glass Eyed Midge 25 No. 1 Well is furnished, any non-consenting working interest owner shall have the right to pay its estimated well costs to the operator in lieu of paying its share of reasonable well costs out of production as hereinafter provided, and any such owner who pays its share of estimated well costs as provided above shall remain liable for operating costs but shall not be liable for risks charges.

9. The operator shall furnish the Division and each known non-consenting working interest owner an itemized schedule of actual well costs within ninety (90) days following completion of the Glass Eyed Midge 25 Well No. 1. If no objection to the

actual well costs is received by the Division, and the Division has not objected within forty-five (45) days following receipt of the schedule, the actual well costs shall be deemed to be the reasonable well costs. If there is an objection to actual well costs within the forty-five (45) day period, the Division will determine reasonable well costs after public notice and hearing.

10. Within sixty (60) days following determination of reasonable well costs for the Glass Eyed Midge 25 No. 1 Well, any non-consenting working interest owner who has paid its share of estimated costs in advance as provided above shall pay to the operator its share of the amount that reasonable well costs exceed estimated well costs and shall receive from the operator its share of the amount that estimated well costs exceed reasonable well costs.

11. The operator is hereby authorized to withhold the following costs and charges from production:

(a) For the Glass Eyed Midge 25 Well No. 1, the proportionate share of reasonable well costs attributable to each non-consenting working interest owner who has not paid its share of estimated well costs within thirty (30) days from the date the schedule of estimated well costs is furnished; and

(b) As a charge for the risk involved in drilling the Glass Eyed Midge 25 Well No. 1, 200% of the above costs.

12. The operator shall distribute the costs and charges withheld from production proportionately. to the parties who advanced the well costs.

13. For the Glass Eyed Midge 25 Well No. 1, reasonable charges for supervision (combined fix rates) are hereby fixed at $6,000.00 per month while drilling and $650.00 per month while producing, provided that these rates shall be adjusted annually pursuant to § III.1.A(3) of the COPAS form entitled "Accounting Procedure-Joint Operations." The operator is authorized to withhold from production the proportionate share of both the supervision charges and the actual expenditures required for operating the Glass Eyed Midge 25 Well No. 1, not in excess of what are reasonable, attributable to each non-consenting working interest.

14. Except as provided in ordering paragraphs 10 and 12 above, all proceeds from production from the Glass Eyed Midge 25 Well No. 1 that are not disbursed for any reason shall be placed in escrow in Lea County, New Mexico, to be paid to the true owner thereof on demand and proof of ownership. The operator shall notify the Division of the name and address of the escrow agent within thirty (30) days from the date of first deposit with the escrow agent.

15. Any unleased mineral interest shall be considered a seven-eighth (7/8) working interest and one-eighth (1/8) royalty interest for the purpose of allocating costs and charges under this order. Any well costs and charges that are to be paid out of production shall be withheld only from the working interest share of production and no costs or charges shall be withheld from production attributable to royalty interest.

16. Ocean Energy's Application in Case No. 12841 pooling all uncommitted interests, whatever they may be, within the W/2 unit is approved.

17. Ocean Energy is designated the operator of the Blue Fin 25 Well No. 1 immediately after the well reaches total depth, but before completion.

18. From the time it becomes operator of the well, Ocean Energy may recover reasonable charges for completing the well and for supervision while operating the well.

19. Reasonable charges for completing the Blue Fin 25 No. 1 Well are $649,291.00.

20. Reasonable charges for supervision (combined fixed rates) should be fixed at $600.00 per month while producing, provided that this rate should be adjusted annually pursuant to § III.1.A(3) of the COPAS form titled "Accounting Procedure-Joint Operations". Ocean Energy, as operator, is authorized to withhold from production the proportionate share of both the supervision charges and the actual expenditures required for operating the well, not in excess of what are reasonable, attributable to each non-consenting working interest.

21. From the time the Blue Fin 25 No. 1 Well reaches total depth and on a monthly basis thereafter, TMBR/Sharp and Arrington may each tender 50% of the completion costs and the monthly operating costs and supervision charges to Ocean Energy which, in-turn, shall place such payments into an escrow account pending judicial resolution of the dispute between Arrington and TMBR/Sharp over the ownership of the oil and gas lease covering the NW/4 of Section 25. Once judicial resolution of the ownership of the lease interests in the NW/4 is final, Ocean shall refund one-half of such escrowed proceeds to the non-prevailing party. Similarly, Ocean Energy shall place into escrow production proceeds equal to one hundred percent of the working interest attributable to the NW/4 pending judicial resolution of the ownership of the lease interests. Once judicial resolution is final, all of those escrowed proceeds shall be paid to the prevailing party. In the interim, Ocean Energy, as Operator, shall be responsible for the payment of all severance taxes and royalties attributable to the NW/4 of said Section 25.

22. Pursuant to the Application of Ocean Energy, In, all uncommitted interests underlying the W/2 of Section 25, Township 16 South, Range 35 East, NMPM, Lea County, New Mexico, are hereby pooled as follows:

The W/2 to form a standard 320 acre gas spacing and proration unit for any and all formations and/or pools developed on 320 acres within that vertical extent which presently include but are not limited to the Undesignated Shore Bar- Atoka Gas Pool, Undesignated Townsend-Morrow Gas Pool ant the Undesignated Townsend-Mississippian Gas Pool.

23. Should all parties to this compulsory pooling order reach voluntary agreement subsequent to entry of this Order, this Order shall thereafter be of no further effect.

24. The operators of each of the wells and units shall notify the Division in writing of the subsequent voluntary agreement of all parties subject to the forced pooling provisions of this Order.

25. The Application of TMBR/Sharp Drilling, Inc. in Case No. 12816 for compulsory pooling of the N/2 of Section 25, Township 16 South, Range 36 East, NMPM, Lea County, is **dismissed with prejudice** and is otherwise **denied**.

26. Jurisdiction of this case 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

KELLAHIN AND KELLAHIN
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JASON KELLAHIN (RETIRED 1991)

TELEPHONE (505) 982-4285
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June 6, 2002

HAND DELIVERED

Mr. Michael E. Stogner
Oil Conservation Division
1220 South Saint Francis Drive
Santa Fe, New Mexico 87505

Re: TMBR/SHARP'S PROPOSED ORDER OF THE DIVISION

NMOCD Case 12816
Application of TMBR/Sharp Drilling, Inc.
for compulsory pooling N/2 (Well in Unit E) Section 25, T16S, R35E
Lea County, New Mexico.

NMOCD Case 12859
Application of David H. Arrington Oil & Gas, Inc.
for compulsory pooling
E/2 (Well in Unit A) Section 25, T16S, R35E, Lea County, New Mexico.

NMOCD Case 12860
Application of Ocean Energy, Inc for compulsory pooling
W/2 (Well in Unit K) Section 25, T16S, R35E Lea County, New Mexico.

NMOCD Case 12841
Application of Ocean Energy, Inc for compulsory pooling
W/2 (Well in Unit E) Section 25, T16S, R35E Lea County, New Mexico.

Dear Mr. Stogner:

Please find enclosed for your consideration, TMBR/Sharp's proposed order for entry in the referenced cases.

Very truly yours,

W. Thomas Kellahin

Hand Delivered:
David K. Brooks, Esq.
Division Attorney

James Bruce, Esq. (505) 982-2151
Attorney for Ocean Energy. Inc.
William F. Carr. Esq. (505) 983-6043
Attorney for Yates Petroleum Corporation
Scott Hall, Esq. (505) 989-9857
Attorney for David H. Arrington Oil & Gas, Inc
TMBR/Sharp (915) 683-672
Rick Montgomery, Esq.
Susan Richardson, Esq.

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

APPLICATION OF TMBR/SHARP DRILLING, INC. FOR COMPULSORY POOLING, N/2 (UNIT E) SECTION 25, T16S, R35E LEA COUNTY, NEW MEXICO	**CASE NO. 12816**
APPLICATION OF OCEAN ENERGY, INC. FOR COMPULSORY POOLING, W/2 (UNIT E) SECTION 25, T16S, R35E LEA COUNTY, NEW MEXICO	**CASE NO. 12841**
APPLICATION OF DAVID H. ARRINGTON OIL & GAS, INC. FOR COMPULSORY POOLING E/2 (UNIT A) SECTION 25, T16S, R35E LEA COUNTY, NEW MEXICO	**CASE NO. 12859**
APPLICATION OF OCEAN ENERGY, INC. FOR COMPULSORY POOLING W/2 (UNIT K) SECTION 25, T16S, R35E LEA COUNTY, NEW MEXICO	**CASE NO. 12860**

TMBR/SHARP DRILLING, INC.
PROPOSED ORDER

BY THE DIVISION:

This cause came on for hearing at 8:15 a.m. on May 16 and 17, 2002 at Santa Fe, New Mexico, before Examiner Michael E. Stogner.

NOW, on this ____ day of June, 2000, the Division Director, having considered the testimony, the recorded and the recommendations of the Examiner, and being fully advised in the premises,

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) Division Cases No. 12816, 12841, 12859 and 12860 were consolidated at the time of the hearing for the purpose of testimony, and, in order to provide a comprehensive decision in these cases, one order should be entered for all four cases.

SUMMARY OF PROCEEDINGS

(3) On August 6, 2001, TMBR/Sharp Drilling, Inc. ("TMBR/Sharp") filed two application for permit to drill ("APD") with the Hobbs Office of the Division requesting approval to drill:

> (a) its Blue Fin "25" Well No. 1 in Unit E and to dedicated it to the N/2 of Section 25, T16S, R35E.
>
> (b) its Leavelle "23" Well No. 1 in Unit G and to dedicated it to the E/2 of Section 23, T16S, R35E.

(4) On August 8, 2001, the Hobbs Office of the Division denied the TMBR/Sharp permits becuase David H. Arrington Oil & Gas, Inc. ("Arrington") already had conflicting permits on the acreage.

(5) On December 13, 2001, the Division entered Order R-11700, refused to approve TMBR/Sharp's APD because on July 19, 2001, the Division approved an APD for Arrington for its:

> (a) Triple Hackle Dragon "25" Well No. 1 for a spacing unit consisting of the W/2 of Section 25
>
> (b) Blue Drake "23" Well No. 1 for a spacing unit consisting of the E/2 of Section 23

The Division based its decision on Arrington's "claim of colorable title" to the Hamilton/Stokes top leases, and stated that:

> (a) "(22) that "Arrington has demonstrated at least a colorable claim of title that would confer upon it a right to drill its proposed wells, no basis exists to reverse or overrule the

action of the District Supervisor in approving the Arrington APDs."

(b) "(21) The Oil Conservation Division has no jurisdiction to determine the validity of any title, or the validity or continuation in force and effect of any oil and gas lease. Exclusive jurisdiction of such matters resides in the courts of the State of New Mexico."

(6) On December 27, 2001, the Lea County District Court, has exercised that jurisdiction, and has ruled that TMBR/Sharp's Hamilton/Stokes leases are still valid and in effect and Arrington's Hamilton/Stokes top leases are not in effect.

(7) On March 26, 2002, the Commission held a De Novo hearing concerning Order R-11700.

(8) On April 26, 2002, the Commission entered Order R-11700-B which rescinded the Division's approved of the Arrington's APD and ordered that the Division's district supervisor approve TMBR/Sharp's two APD filed in August 6 and 7, 2001.

(9) On May 1, 2002, Chris Williams, Supervisor of the Hobbs Office of the Division, voided the W/2 and E/2 APDs of Arrington and granted the two APDs requested by TMBR/Sharp in August of 2001.

(10) On May 7, 2002, TMBR/Sharp, having voluntarily consolidated 82% of the working interest owner in the N/2 of Section 25, commence drilling its Blue Fin "25" Well No. 1 in Unit E dedicated to the N/2 of Section 25, T16S, R35E.

(11) The following four (4) compulsory pooling applications which involved Section 25, T16S, R35E, were set for an Examiner Hearing in May 2, 2002 but then continued until May 16, 2002 to be heard after the Commission entered it Order R-11700-B on April 26, 2002:

(a) TMBR/Sharp's application for compulsory pooling of the N/2 of Section 25 for its Blue Fin 25 Well No. 1 in Unit E of that section. Cases 12816 filed January 25, 2002

(b) Ocean Energy, Inc. ("Ocean") application for compulsory pooling of the W/2 of Section 25 for its Triple Hackle Dragon 25 Well No. 1 in Unit E of that section. Case 12841 filed February 2, 2002

(c) Ocean Energy, Inc. ("Ocean") application for compulsory pooling of the W/2 of Section 25 for its Triple Hackle Dragon 25 Well No. 2 in Unit K of that section. Case 12860 filed April 9, 2002

(d) Arrington's application for compulsory pooling of the E/2 of Section 25 for its Glass-Eyed Midge 25 Well No 1 in Unit A of that section. Cases 12859 filed April 9, 2002

ACREAGE CONFIGURATION

(12) Section 25 is subdivided as follows:

(a) The NW/4 is fee acreage referred to as the Stokes/Hamilton leases controlled by TMBR/Sharp which are the subject of litigation with Arrington over his top leases;

(b) the SW/4 is fee acreage refereed to as the Ocean farmout acreage obtained beginning or and after July 32, 2001; Ocean assigned a partial interest of Arrington on November 11, 2001;

(c) the SW/4 is a State of New Mexico lease held by Yates;

(d) The NE/4 is divided between the E/2 and W/2 such that TMBR/Sharp now control 63 % and Arrington controls 31 %.

COMPULSORY POOLING

TMBR/Sharp's compulsory pooling case:

(13) On January 25, 2001, TMBR/Sharp filed an application for compulsory pooling for the remaining working interest owners in the N/2 of Section 25

(14) In accordance with NMSA (1979) Section 70-2-17, and Order R-11700-B, On May 7, 2002, TMBR/Sharp spudded the Blue Fin 25 Well No. 2 after filing an application to compulsory pooling the remaining working interest owners in the N/2 of Section 25.

(15) At the time of the hearing, TMBR/Sharp controlled 82% of the working intest ownership, Arrington controlled 16% and two parties who could not be located controlled 2% of the N/2 of Section 25.

(16) TMBR/Sharp has 100% of the working interest in the NW/4 of Section 25, and its compulsory pooling case is necessary in order to consolidate certain owner in the NW/4 of Section 25 to form a 320-acre spacing unit consisting of the N/2 of Section 25.

(17) TMBR/Sharp geological and geophysical evidence which demonstrated that the appropriate development of Section 25 is best accomplished by orientation the spacing units N/2 and S/2.

(18) TMBR/Sharp originally developed the concept for the exploration of Section 23, 24, 25 and 26. (Big Tune prospect). The project stated in 1991 and over time, over $7 million was spent on land, geological, geophysical analysis and drilling.

(19) Prior to commenced the Blue Fin 24 Well No. 1 in the SW/4 of Section 24, TMBR/Sharp offer to Ocean a share of the Big Tuna Prospect on three different occasions, including January 31, 2001 meeting in Ocean's office in Houston, Texas.

(20) After being afford an opportunity for a detail review of TMBR/Sharp's geology including its 3-D seismic data, Ocean declined to participate based on its belief that the Chester formation would be structurally too low and therefore to wet (water saturation too high to allow for commercial production of hydrocarbons.)

(21) On March 27, 2001, Arrington top leases the TMBR/Sharp's Hamilton/Stokes leases which cover lands in Section 23, 24, 24 and 25, among others. Arrington was aware that TMBR/Sharp had obtained a drilling permit for the Blue Fin 24 Well No. 1 in November of 2000.

(22) On March 29, 2001, TMBR/Sharp's spudded its Blue Fin 24 Well No. 1 in the SW/4 of Section 24.

(23) On June 29, 2002, TMBR/Sharp completed the Blue Fin "24" Well No .1 for production from the Chester Formation.

(24) On July 24, 2002, David H. Arrington personally told Jeff Phillips, President of TMBR/Sharp, that TMBR/Sharp would not be able to timely drill wells in Section 23 or 25. (TMBR/Sharp's Hamilton/Stokes leases have a 180 day continuation drilling clause between wells.)

(25) On July 19, 2001, Arrington obtained an approved APD from the Division for its well to be drilled in Unit E and dedicated to the W/2 Section 25. Arrington had no intention of drilling a well but obtained its permit because it wanted by block TMBR/Sharp for obtained a competing permit which was denied on August 8, 2001.

(26) TMBR/Sharp was the first working interest owner to propose a well in Section 25.

(27) At the time of filing of its compulsory pooling application, neither Ocean or Arrington had an interest of record in the N/2 of Section 25. Arrington had no interest in the W/2 of Section 25.

(28) Ocean's farm-ins are confined to the SW/4 of Section 25 and Arrington did not receive an interest in Ocean's various farm-ins in the SW/4 of Section 25 until November 14, 2001.

Ocean's two compulsory pooling cases:

(29) On July 19, 2001 Arrington obtained an approved APD for his Triple Hackle Dragon 25 Well No.1 dedicated with the W/2 of Section 25.

(30) On January 24, 2002, Arrington proposed the well to TMBR/Sharp

(31) On April 9, 2002, Arrington filed a compulsory pooling application with the Division.

(32) This Case was heard on May 16-17, 2002.

(33) Ocean's compulsory pooling applications are an attempt by Ocean to substitute itself for Arrington on the APD approved by the Division on July 19, 2001:

> (a) on September 10, 2001, Ocean and Arrington entered into a Letter Agreement concerning their plans for the Triple Hackle Dragon "25" Well No. 1 for the W/2 of Section 25;
>
> (b) which provide that Arrington would be the Operator;
>
> (c) that if a drilling title opinion requirement deterred Arrington from drilling, Ocean would be the operator;

(b) Ocean now seeks a compulsory pooling order for the Arrington's Triple Hackle Dragon "25" Well No. 1.

(34) Ocean has failed to take any reasonable action to preclude its farm-ins from expiring on July 1, 2002. Its farm-ins contain force majeurae clauses which arguably could offer protection from expiration in appropriate circumstances.

Arrington's compulsory pooling case

CASE 12859

(35) On December 17, 2001 Arrington, within notice to TMBR/Sharp, obtained a approved APD for his Glass-Eye Midge 25 Well No.1 dedicated with the E/2 of Section 25.

(36) On December 17, 2001, Arrington held no interest in the NE/4 of Section 25. It obtained its interest from Huff by assignment recorded on February 4, 2001. The SE/4 of Section 25 is controlled by Yates Petroleum Corporation.

(37) On March 26, 2002, the Commission's held a hearing concerning Arrington APD for the W/2 of Section 25 and TMBR/Sharp's APD for the N/2 of Section 25.

(38) At no time during that hearing, did Arrington informed the Commission that Arrington claimed an approved APD for the E/2 of Section 25 which would be in conflict with the APD's for the N/2 (TMBR/Sharp) then being decided by the Commission.

(39) Arrington has waive any claim for a spacing unit consisting of the E/2 of Section by its failure to raise this issue of his APD for the E/2 of Section 25 at the time of the Commission hearing.

(40) On April 9, 2002, Arrington filed a compulsory pooling application for the E/2 of Section 25 with the Division which has been set for hearing on May 16, 2002.

(41) On May 1, 2001, the Division canceled is approval of Arrington's APD for his Glass Eye Midge 25 Well No.1 dedicated with the E/2 of Section 25.

(42) On May 21, 2002, Arrington filed a compulsory pooling application for the E/2 of Section 25 with the Division which has been set for hearing on May 16, 2001.

FINDING BY THE DIVISION

(43) After being afford an opportunity for a detail review of TMBR/Sharp's geology including its 3-D seismic data, Ocean decline to participate based on his belief that the Chester formation would be structurally too low and therefore to wet (water saturating too high to be commercial production of hydrocarbons.)

(44) Ocean should not be allowed to take advantage of the fact that TMBR/Sharp had already developed the Big Tuna Prospect and offered Ocean an opportunity to participate.

(45) Ocean and Arrington's application are inconsistence with and contrary to the Commission determination that TMBR/Sharp has the prior right to drill the wells which it sought to drill in August 2001 until Arrington interfered with that right.

(46) But for Arrington's blocking of TMBR/Sharp's permit, TMBR/Sharp would have received its permits to drill and would have already drilled its well in the N/2 of Section 25 and the E/2 of Section 23. The Commission has agreed with TMBR/Sharp who is now entitled to proceed with the drilling of its wells without further interference by Ocean and Arrington.

(47) In accordance with Commission Order R-11700-B, TMBR/Sharp is now entitled to have drill and complete this well as approved by the Division and obtain a compulsory pooling order without further inference from Arrington or Ocean.29) The issuance of a compulsory pooling order to Ocean or Arrington will be in direct conflict with Commission Order R-11700-B and will preclude TMBR/Sharp from receive an approved APD to which it was entitled and would have received but for the wrongful actions of Arrington.

TECHNICAL CASES

TMBR/Sharp's technical case:

(48) Commencing in 1995, Louis Mazzullo, began developing an geological model of a multisection area known as the "Big Tuna" Prospect which including Sections 23, 24, 25 and 26 of T16S, R35E. This study included the Wolfcamp, Atoka and an portion of the upper Mississippi ("Chester") formations. **Transcript page 116-118**

(49) By 1997, Mr. Mazzullo had included 2-D and 3-D seismic data along with conventional geological (log) data, and concluded that the best opportunity for deep gas production from the "Chester formation" was to located and drill wells in bowl shaped structural features which could be identified and located using 3-D Seismic data. As a result, Mr. Mazzullo identified "Chester bowls" in the SW/4 of Section 24, the NW/4 of Section 25, and the NE/4 of Section 23.

(50) Mr. Mazzullo shared his geologic conclusions with a group of investors (collectively "TMBR/Sharp") who signed a Joint Operating Agreement in 1998.

(51) On January 31, 2001, after being afford an private detail review of TMBR/Sharp's geology including its 3-D seismic data, Ocean decline to participate based on its belief (Mr. John Silver) that the Chester formation would be structurally too low and therefore to wet (water saturating too high to be commercial production of hydrocarbons.)[1] **Transcript Page 118**

(52) On May 29, 2001, TMBR/Sharp, using Mr. Mazzullo geologic interpretation, then successfully drilled and competed the Blue Fin 24 Well No. 1 in the SW/4 of Section 24 for production for one of the Chester bowls with first production on June 29, 2001.

(53) The success of the Blue Fin 24 Well No. 1, confirmed the accuracy of Mr. Mazzullo geological model.

(54) Mr. Mazzullo predicted that a second Chester bowl is located in the NW/4 of Section 25 and that a third bowl is located between the north/south dividing line between the SW/4 and the SE/4 of Section 25. **See Transcript 142 (TMBR/Sharp"s Exhibit 18-D**

(55) Mr. Mazzullo further concludes:

> (a) that each of these three Chester Bowl is a separate and distinct reservoir and are separate by fault blocks; and

[1] Ocean on occasions call the Chester part of the lower Morrow. Transcript page 118 At the hearing Ocean referred to the "Chester bowls" as the Lower Mississippian Lime (See Ocean Exhibit 12, 13, 14)

(b) that it would be necessary to drill a well in each bowl.

Ocean's technical case:

(56) On about January 31, 2001, John Silver on behalf of Ocean, was given a detail review of TMBR/Sharp's geology (Mr. Mazzullo) including its 3-D seismic data, and concluded that Ocean should not participate based on his belief that the Chester formation would be structurally too low and therefore to wet (water saturating too high to contain commercial production of hydrocarbons.)

(57) At the Hearing, Mr. Silver presented a isopach map of the Brunson Sand, being the lower portion of the Morrow formation, which included the Atoka (Brunson sand) wells and the Chester wells (which Ocean called the Austin. (Ocean Exhibit 10)

(58) Mr. Silver's isopach map concludes that there are no Brunson sand Wells in Section 23, 24, 25, 26 but still seeks to extent the Brunson sand isopach in the W/2 of Section 25.[2] **Ocean Exhibit 17.**

(59) Mr. Silver's Brunson sand map **(Ocean Exhibit 17)** condemns the NE/4 of Section 25

(60) Mr. Silver presented Time Structure Maps of the Austin, (Lower Mississippian Lime **(Ocean Exhibit 12)** and the Brunson interval of the Lower Morrow **(Ocean Exhibit 15)** both of which show three distinct "bowls" which substantially agree with Mr. Mazzullo's time structure Map of his "Chester Bowls". **(TMBR/Sharp Exhibit 18-D)**

(61) Both TMBR/Sharp and Ocean's maps demonstrate that the Chester Bowl in the S/2 of Section 25 is split between the SW/4 and the SE/4.

(62) Mr. Silver also presented a Austin Isopach **(Ocean Exhibit 17)** on which he drew the productive limits to connect together the Chester bowls in the SW/4 of Section 24 two the two Chester bowls in the in NW/4 and the S/2 of Section 25.

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[2] Mr. Mazzullo disagrees and have concluded that the Brunson Sand in not productive in Sections 23, 24, 25, 26.

(63) If Mr. Silver's interpretation is correct, then a single well in the NW/4 of Section 25 will drain the entire section including the SE/4 of Section 25 which will not share in production if Ocean's W/2 spacing unit is approved.

Arrington's technical case:

(64) Arrington limited is technical pretention at the hearing to presenting a isopach and structure map of the Brunson Sand, being the lower portion of the Morrow formation which included the Atoka (Brunson sand) wells and the Chester wells (which Ocean called the Austin (**Ocean Exhibit 10**).

(65) Arrington extends the Brunson sand from the Ocean well located in the SW/4 of Section 10 southward through Section 25

(66) Contrary to Mr. Silver's map, Arrington concludes that the NE/4 of Section 25 if better than the NW/4 and the SW/4 of Section 25 is better than the NW/4. **(See Arrington Exhibit 8)**

Division Decision

(67) The Division finds that:

(a) If Mr. Silver's interpretation is correct, then a single well in the NW/4 of Section 25 will drain the entire section including the SE/4 of Section 25 which will not share in production if Ocean's W/2 spacing unit is approved.

(b) Recent pressure data from the TMBR/Sharp Blue Fin 24 Well No. 1 tends to demonstrate that the Chester Bowl are not connected as assumed by Ocean and that at least two wells will be needed in Section 25.

(c) Arrington's Morrow maps support either "lay-down" or "stand-up" spacing units.

(d) Spacing units consisting of the N/2 and the S/2 of Section 25 will afford the opportunity for owners in each of the 4 quarter sections to share equitable in producing their respective shares of production from the reservoirs in

question.

(68) Cases 12859, 12860 and 12841 have been made moot by the Commission's decision approving TMBR/Sharp's APDs for the N/2 of Section 25 and the E/2 of Section 23.

(69) The Commission decision in favor of TMBR/Sharp eliminates the need for the Division to decide the Ocean and Arrington compulsory pooling case all of which attempts to pool spacing units in conflict with TMBr/Sharp's spacing unit.

(70) Ocean and Arrington's application are inconsistence with and contrary to the Commission determination that TMBR/Sharp has the prior right to drill the wells which it sought to drill in August 2001 until Arrington interfered with that right.

(71) But for Arrington's blocking of TMBR/Sharp's permit, TMBR/Sharp would have received its permits to drill and would have already drilled its well in the N/2 of Section 25 and the E/2 of Section 23.

(72) The Commission has agreed with TMBR/Sharp who is now entitled to proceed with the drilling of its wells without further interference by Ocean and Arrington.

(73) The "New Mexico Oil and Gas Act" allows for to the pooling of interest in a spacing unit after the well has been drill. TMBR/Sharp, has obtained the voluntary agreement 82% of the interest owners, intend to drill this well first and then pool the remaining interest owners who either have refused to participate on a voluntary basis or who have not yet been contracted.

(74) TMBR/Sharp should be designated the operator of the subject well and the unit.

(75) Both parties agreed at the hearing that overhead rates of $6000.00 while drilling and $600.00 while producing should be adopted in this case.

(76) In addition, all parties proposed that a risk penalty of 200 percent be assessed against any non-consenting working interest owners.

(77) To avoid the drilling if unnecessary wells, to protect correlative rights, to avoid waste, and to afford to the owner of each interest in the above-describe units the opportunity to recover or receive with out unnecessary expense its just and fair share of

hydrocarbons, the application of TMBR/Sharp should be approved by pooling all uncommitted mineral interests, whatever they may be, within these units.

(78) After pooling, uncommitted working interest owners are referred to as "non-consenting working interest owners." Any non-consenting working interest owner should be afforded the opportunity to pay its share of the estimated costs to the operator in lieu of paying its share of reasonable well costs out of production.

(79) Any non-consenting working interest owner should be afforded the opportunity to pay its share of estimated well costs first to Santa Fe, as the operator, respectively, in lieu of paying its share of reasonable well costs out of production.

(80) Any non-consenting working interest owner who does not pay its share of estimated well costs should have withheld from production its share of the reasonable well costs plus an additional 200 percent thereof as a reasonable charge for the risk involved in the drilling of the well.

(81) Any non-consenting working interest owner should be afforded the opportunity to object to the actual well costs but actual well costs should be adopted as the reasonable well costs in the absence of such objection.

(82) Following determination of reasonable well costs, any non-consenting working interest owner who has paid its share of estimated costs should pay to the operator any amount that reasonable well costs exceed estimated well costs and should receive from the operator any amount that paid estimated well costs exceed reasonable well costs.

(83) $6000.00 per monthly while drilling and $600.00 per month while producing should be fixed as reasonable charges for supervision (combined fixed rates); the operator should be authorized to withhold from production the proportionate share of such supervision charges attributable to each non-consenting working interest, and in addition thereto, the operator should be authorized to withhold from production the proportionate share of actual expenditures required for operation the subject well, not in excess of what are reasonable, attributable to each non-consenting working interest.

(84) All proceeds from production from the subject well which are not disbursed for any reason should be placed in escrow to be paid to the true owner thereof upon demand and proof of ownership.

(85) Should all the parties to this forced pooling order reach voluntary agreement subsequent to entry of this order, this order shall thereafter be of no further effect.

(86) TMBR/Sharp as the operator of the well and this unit shall notify the Director of the Division on writing of the subsequent voluntary agreement of all parties subject to the pooling provisions of the order.

IT IS THEREFORE ORDERED THAT:

(1) Pursuant to the application of TMBR/Sharp in Case No. 12816, all uncommitted mineral interest from the surface to the base of the Mississippi formation underling the following acreage in Section 25, Township 16 South, Range 36 East, Lea County, New Mexico, are hereby pooled in the following manner: the N/2 to form a 320-acre gas spacing and proration unit for formations and/or pools developed on 320-acre spacing within that vertical extent, including the Townsend-Morrow Gas Pool and the Townsend-Mississippi Gas Pool.

(2) This spacing and proration unit are to be dedicated to the TMBR/Sharp's Blue Fin "25" Well No, 1 to be drilled and completed at a standard location within Unit E of this section.

(3) Ocean Energy, Inc.'s application in Cases 12841 and 12860 are hereby **denied.**

(4) David H., Arrington Oil & Gas Inc.'s application in Cases 12859 is hereby **denied.**

(5) TMBR/Sharp Drilling, Inc. is hereby designated the operator of the subject well and units.

(6) TMBR/Sharp, as operator of this unit, has commenced drilling the well and shall continue drilling the well with due diligence to a depth sufficient to test the Morrow formation.

(7) In the event, Santa Fe either fails to commence drilling its well on or before September 31, 2000, Ordering Paragraph (1) shall be of no effect, unless the operator obtains a time extension from the Division Director for good cause shown.

(8) Should the well not be drilled to completion or abandoned within 120 days after commencement, the operator shall appear before the Division Director and show cause why Ordering Paragraph (1) should not be rescinded.

(9) After pooling, uncommitted working interest owners are referred to as "non-consenting working interest owners." After the effective date of this order and within 90 days prior to commencing said well, Santa Fe shall furnish the Division and each known non-consenting working interest owner in the units an itemized schedule of estimated well costs.

(10) After the entry of a order in this case and within 30 days from the date the schedule of estimated well costs is furnished, any non-consenting working interest owner shall have the right to pay its share of estimated well costs to Santa Fe in lieu of paying its share of reasonable well costs out of production, and any such owner who pays its share of estimated well costs as provided above shall remain liable for operation costs but shall not be liable for risk charges.

(11) The operator shall furnish the Division and each known non-consenting working interest owner an itemized schedule of actual well costs within 90 days following completion of the well. If no objection to the actual well costs is received by the Division and the Division has not objected within 45 days following receipt of said schedule, the actual well costs shall be the reasonable well costs; provided however, if there is objection to actual well costs within the 45-day period the Division will determine reasonable well costs after public notice and hearing.

(12) Within 60 days following determination of reasonable well costs, any non-consenting working interest owner who has paid its share of estimated well costs in advance as provided above shall pay to the operator its share of the amount that reasonable well costs exceed estimated well costs and shall receive from the operator its share of the amount that estimated well costs exceed reasonable well costs.

(13) The operator is hereby authorized to withhold the following costs and charges from production:

(a) the proportionate share of reasonable well costs attributable to each non-consenting working interest owner who has not paid its share of estimated well costs within 30 days from the date the schedule of estimated well costs is furnished; and

(b) as a charge for the risk involved in the drilling of the well, 200 percent of the above costs.

(14) The operator shall distribute the costs and charges withheld from production to the parties who advanced the well costs.

(15) $6000.00 per month while drilling and $600.00 per month while producing are hereby fixed as reasonable charges for supervision (combined fixed rates); the operator is hereby authorized to withhold from production the proportionate share od such supervision charges attributable to each non-consenting working interest, and in addition thereto, the operator is hereby authorized to withhold from production the proportionate share of actual expenditures required for operation such well, not in excess of what are reasonable, attributable to each non-consenting working interest.

(16) Any unleased mineral interest shall be considered a seven-eighths (7/8) working interest and a one-eighth (1/8) royalty interest for the purpose of allocating costs and charges under the terms of this order.

(17) Any well costs or charges which are to be paid put of production shall be withheld only from the working interest's share of production, and no costs or charges shall be withheld from production attributable to royalty interests.

(18) All proceeds from production from the well which are not disbursed for any reason shall immediately be placed in escrow in Lea County, New Mexico, to be paid to the true owner thereof upon demand and proof of ownership, the operator shall notify the Division of the name and address of the escrow agent within 30 days from the date of first deposit with the escrow agent.

(19) Should all parties to this forced pooling order reach voluntary agreement subsequent to entry of this order, this order shall thereafter be of no further effect.

(20) The operator of the well and unit shall notify the Director of the Division in writing of the subsequent voluntary agreement of all parties subject to the forced pooling provisions of this order.

(21) Jurisdiction is hereby 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

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June 6, 2002

Hand Delivered

Michael E. Stogner
Oil Conservation Division
1220 South St. Francis Drive
Santa Fe, New Mexico 87505

Re: Ocean-Arrington-TMBR/Sharp
Case Nos. 12816, 12841, 12859, and 12860

Dear Mr. Stogner:

Enclosed is Ocean's proposed order (hard copy and disk).

As discussed at the hearing, Ocean's farmout expires on June 30th, so a prompt decision is necessary. Thank you.

Very truly yours,

James Bruce

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:

APPLICATION OF TMBR/SHARP
DRILLING, INC. FOR COMPULSORY
POOLING, LEA COUNTY, NEW MEXICO. No. 12816

APPLICATION OF OCEAN ENERGY,
INC. FOR COMPULSORY POOLING,
LEA COUNTY, NEW MEXICO. No. 12841

APPLICATION OF DAVID H. ARRINGTON
OIL & GAS, INC. FOR COMPULSORY
POOLING, LEA COUNTY, NEW MEXICO. No. 12859

APPLICATION OF OCEAN ENERGY,
INC. FOR COMPULSORY POOLING,
LEA COUNTY, NEW MEXICO. No. 12860

ORDER NO. R-_____

ORDER OF THE DIVISION
(Proposed by Ocean Energy, Inc.)

BY THE DIVISION:

This cause came on for hearing at 8:15 a.m. on May 16, 2002, at Santa Fe, New Mexico, before Examiner Michael E. Stogner.

NOW, on this _____ day of June, 2002, the Division Director, having considered the testimony, the record, and the recommendations of the Examiner,

FINDS THAT:

(1) Due public notice has been given, and the Division has jurisdiction of these cases and their subject matter.

(2) In Case No. 12816, TMBR/Sharp Drilling, Inc. ("TMBR/Sharp") seeks an order pooling all mineral interests from the surface to the base of the Mississippian formation underlying the N½ of Section 25, Township 16 South, Range 35 East, N.M.P.M. for any and all formations developed on 320-acre spacing within that vertical extent, which presently include but are not limited to the Townsend-Morrow Gas Pool and the Townsend-Mississippian Gas Pool. The unit is to be dedicated to TMBR/Sharp's Blue Fin 25 Well No. 1, located 1913 feet from the north line and 924 feet from the east line (Unit E) of Section 25. TMBR/Sharp has commenced drilling the subject well.

(3) In Case No. 12841, Ocean Energy, Inc. ("Ocean") seeks an order pooling all mineral interests from the surface to the base of the Mississippian formation underlying the W½ of Section 25, Township 16 South, Range 35 East, N.M.P.M. for any and all formations developed on 320-acre spacing within that vertical extent, which presently include but are not limited to the Undesignated Townsend-Morrow Gas Pool and the Undesignated Townsend-Mississippian Gas Pool. The unit was to be dedicated to the Triple Hackle Dragon 25 Well No. 1, to be located 1815 feet from the north line and 750 feet from the west line (Unit E) of Section 25.

(4) In Case No. 12859, David H. Arrington Oil & Gas, Inc. ("Arrington") seeks an order pooling all mineral interests from the surface to the base of the Mississippian formation underlying the following described acreage in Section 25, Township 16 South, Range 35 East, N.M.P.M., and in the following manner:

(a) The E½ to form a standard 320-acre gas spacing and proration unit for any and all formations and/or pools developed on 320-acre spacing within that vertical extent, which presently include but are not limited to the Undesignated Shoe Bar-Atoka Gas Pool, Undesignated Townsend-Morrow Gas Pool and the Undesignated Townsend-Mississippian Gas Pool;

(b) The NE¼ to form a standard 160-acre gas spacing and proration unit for any and all formations and/or pools developed on 160-acre spacing within that vertical extent; and

(c) The E½NE¼ to form a standard 80-acre oil spacing and proration unit for any and all formations and/or pools developed on 80-acre spacing within that vertical extent.

The units are to be dedicated to Arrington's Glass-Eyed Midge 25 Well No. 1, to be located 803 feet from the north line and 962 feet from the east line (Unit A) of Section 25.

(5) In Case No. 12860, Ocean seeks an order pooling all mineral interests from the surface to the base of the Mississippian formation underlying the W½ of Section 25, Township 16 South, Range 35 East, N.M.P.M. for any and all formations developed on 320-acre spacing within that vertical extent, which presently include but are not limited to the Undesignated Townsend-Morrow Gas Pool and the Undesignated Townsend-Mississippian Gas Pool. The unit is to be dedicated to the Triple Hackle Dragon 25 Well No. 2, to be located 1980 feet from the south and west lines (Unit K) of Section 25.

(6) Case Nos. 12816, 12841, 12859, and 12860 were consolidated for purposes of hearing.

(7) Yates Petroleum Corporation entered an appearance in the consolidated cases.

(8) There are interest owners in the proposed proration units who have not agreed to pool their interests.

(9) The land testimony presented in this matter showed the following approximate leasehold working interest ownership in the various well units:

W½ of Section 25:
Ocean Energy, Inc. 35%
David H. Arrington Oil & Gas, Inc. 15%
Uncertain (NW¼ of Section 25) 50%

N½ of Section 25:
TMBR/Sharp Drilling, Inc. 33.4%
David H. Arrington Oil & Gas, Inc. and others 16.4%
Uncertain (NW¼ of Section 25) 50.0%

Ownership of the working interest in the NW¼ of Section 25 is the subject of litigation in Lea County District Court between Arrington and TMBR/Sharp. Whoever ultimately wins will own 100% of the working interest in the NW¼ of Section 25.

E½ of Section 25:
David H. Arrington Oil & Gas, Inc. 17.3%
TMBR/Sharp Drilling, Inc. and others 32.7%
Yates Petroleum Corporation 50.0%

(10) The land testimony presented in this matter further showed the following:

(a) TMBR/Sharp acquired its interest in the NW¼ of Section 25 by a lease from Madeline Stokes effective December 7, 1997 (the "bottom lease"). **TMBR/Sharp Exhibit 1.**

(b) Due to questions regarding the effectiveness of the bottom lease, Arrington acquired a lease covering the NW¼ of Section 25 from Madeline Stokes dated March 27, 2001 (the "top lease"). **TMBR/Sharp Exhibit 2.** The assignment of the lease to Arrington was recorded with the Lea County Clerk in September 2001.

(c) The effectiveness of the top lease and bottom lease are being litigated in Lea County District Court.

(d) Arrington and TMBR/Sharp also own working interests in the N½ of Section 25 which are not covered by the top lease and bottom lease.

(e) Ocean acquired farmouts covering the entire working interest in the SW¼ of Section 25 in July 2001. Arrington now owns a portion of the farmouts as to the SW¼ of Section 25. The farmouts expire on June 30, 2002 unless there is drilling on lands covered thereby or on acreage pooled therewith.

(f) Arrington obtained an approved APD for a well in the NW¼ of Section 25, with a W½ unit, in July 2001. Arrington also obtained an approved APD for a well in the NE¼ of Section 25, with an E½ unit, in December 2001. TMBR/Sharp subsequently obtained an approved APD for a well in the NW¼ of Section 25, with a N½ unit, in May 2002. These matters are the subject of Order No. R-11700-B issued by the Oil Conservation Commission (the "Commission") on April 26, 2002.

(g) Ocean had agreed to let Arrington operate the W½ unit, and to drill a well in the NW¼ of Section 25. However, as soon as Arrington's APD became an issue, Ocean proposed its well in the NW¼ of Section 25 in late January 2002. **Ocean Exhibit 3A.** Ocean subsequently filed its pooling application in Case No. 12841 in late February 2002.

(h) Due to issues raised by the Commission regarding the right of an operator to drill on another party's lease, Ocean proposed its well in the SW¼ of Section 25, with a W½ unit, in early April 2002. **Ocean Exhibit 5.** Ocean thereafter filed its pooling application in Case No. 12860.[1]

(i) Arrington proposed its well in the NE¼ of Section 25, with an E½ unit, in late January 2002. **Arrington Exhibits 4 and 5.** Arrington subsequently filed its pooling application in Case No. 12859 in April 2002.

(j) TMBR/Sharp filed its pooling application on or about January 28, 2002. TMBR/Sharp did not propose its Blue Fin 25 Well No. 1 to the interest owners until early May 2002. **TMBR/Sharp Exhibits 4 and 5.** Therefore, **the first**

[1]The pooling statute states that "All operations for the pooled oil or gas, or both, which are conducted on any portion of the unit shall be deemed for all purposes to have been conducted upon each tract within the unit by the owner or owners of such tract." **NMSA 1978 §70-2-17.C.** Therefore, drilling on the NW¼ of Section 25 is equivalent to drilling on the SW¼ of Section 25, and the operator under a pooling order is allowed to drill on any tract within a well unit.

correspondence that the interest owners received from TMBR/Sharp regarding its proposed well was the notice of the compulsory pooling application in Case No. 12816.

(k) TMBR/Sharp accused Ocean of "stealing" its prospect. However, (a) Ocean did not buy the prospect from TMBR/Sharp because the price was too high, **Testimony of Derold Maney, Transcript at 186**, (b) TMBR/Sharp could have tried to obtain farmouts on the SW¼ of Section 25 just as Ocean did, and (c) TMBR/Sharp showed the prospect at the North American Petroleum Exposition ("NAPE") in Houston in January 2001, and anyone who attended NAPE could have viewed TMBR/Sharp's prospect and then sought to obtain farmouts on the SW¼ of Section 25. Thus, TMBR/Sharp's complaint is without merit.

(l) TMBR/Sharp also complained that it would have commenced its well last fall without "interference" by Ocean and Arrington. However, TMBR/Sharp did not even propose its well until recently. **See TMBR/Sharp's AFE dated April 23, 2002 (Exhibit 4) and Joint Operating Agreement dated April 20, 2000 (Exhibit 6)**. Moreover, Ocean would have taken action to pool the W½ unit and preserve its rights last fall if TMBR/Sharp had sought to move forward at that time. **Testimony of Derold Maney, Transcript at 194-195.**

(m) TMBR/Sharp is drilling on a lease which it may not own. Should it lose the District Court lawsuit the only way it will participate in production from the reservoir in the W½ of Section 25 is through its ownership of working interests in the NE¼ of Section 25. Therefore its N½ unit is based on land reasons, rather than geologic or engineering considerations. **See TMBR/Sharp Exhibit 17.**

(n) If TMBR/Sharp is unsuccessful in the District Court litigation, 100% of the working interest owners in the W½ of Section 25 desire to form a W½ unit.

(11) The geological and geophysical evidence presented in this matter shows as follows:

(a) Development in this area is based on well control and seismic data.

(b) The primary zones of interest in this area are the Brunson (Atoka) sand and the Mississippian formation.

(c) The Atoka and Mississippian reservoirs in this area are formed at structural lows.

(d) Ninety percent (90%) of the potential Mississippian reservoir in Section 25 is located in the W½ of Section 25. There is no Mississippian reservoir in the NE¼ of Section 25. **Testimony of Jeffrey D. Phillips, Transcript at 85; TMBR/Sharp Exhibits 17 and 18-D; Ocean Exhibits 10 and 12.**

(e) It is undisputed that the potential Atoka reservoir is located entirely in the W½ of Section 25, and a separate Atoka reservoir is located entirely in the E½ of Section 25. **Ocean Exhibit 10; Arrington Exhibit 8.**

(f) Both the Atoka and Mississippian reservoirs in this area trend north-northwest/south-southeast. However, the Atoka reservoir is displaced slightly to the west of the Mississippian reservoir. **Ocean Exhibits 10 and 12.**

(g) The best location to test both the Atoka formation and the Mississippian formation in the W½ of Section 25 is a well located in the SW¼NW¼ of Section 25.

(h) If a well is drilled in the SW¼ of Section 25, it must test either the Atoka formation or the Mississippian formation; one well cannot adequately test both zones, unlike a well in the SW¼NW¼ of Section 25. **Testimony of Frank Messa, Transcript at 245.**

(i) The Morrow formation is a secondary zone in Section 25. Again, that reservoir is confined to the W½ of Section 25. **Arrington Exhibit 6.**

(j) A 200% non-consent penalty is a proper risk factor for drilling any well in Section 25.

(12) The engineering evidence presented in this matter shows as follows:

(a) TMBR/Sharp has drilled and completed its Blue Fin 24 Well No. 1, located in the SW¼SW¼ of adjoining Section 24, in the Mississippian formation. The well is producing at a restricted rate of 4 MMCFGPD and 220 BCPD. The well has approximately 5 BCF of original gas in place. **Testimony of Jeffrey D. Phillips, Transcript at 169.**

(b) TMBR/Sharp asserted that drainage in the Mississippian reservoir is restricted to the "bowl" or deepest part of the reservoir. These areas are calculated to be 36.5 acres for the Blue Fin 24 Well No. 1, and 54.6 acres for the currently drilling Blue Fin 25 Well No. 1. **TMBR/Sharp Exhibit 18-D.**

(c) Based on reservoir data provided by TMBR/Sharp, the Blue Fin 24 Well No. 1 will drain over 200 acres. **Testimony of Ray Payne, Transcript at 330.** Thus, TMBR/Sharp Exhibit 18-D, which is not a drainage map, is without merit.

(d) Reserves in the W½ of Section 25 are equivalent to those in the Blue Fin 24 Well No. 1. **Testimony of Jeffrey D. Phillips, Transcript at 80, 169.** Therefore, the well in the SW¼NW¼ of Section 25 will drain over 200 acres, and will recover the reserves in the SW¼ of Section 25 in addition to the reserves in the NW¼ of Section 25.

(e) If a W½ unit is formed, the interest owners can produce the well in the SW¼NW¼ of Section 25 for a reasonable period, and then determine if another Atoka or Mississippian well in the SW¼ of Section 25 is necessary. However, if laydown units are formed at least one, and possibly two, wells will need to be drilled in the SW¼ of Section 25 in the immediate future. **Testimony of Charles W. Sledge, Transcript at 420-423; Testimony of Frank Messa, Transcript at 245.**

(f) Requiring laydown units will result in the drilling of unnecessary wells. **Id.**

(13) The AFE's and operating costs of the parties are comparable for any well drilled in Section 25, and they are not an issue in these cases.

(14) TMBR/Sharp claims that it has an approved APD, and therefore no one may challenge its proposed N½ unit. However, TMBR/Sharp ignores the terms of Commission Order No. R-11700-B, which states:

> Issuance of the [APD] does not prejudge the results of a compulsory pooling proceeding, and any suggestion that the acreage dedication plat attached to an application to drill somehow "pools" acreage is expressly disavowed.

Order No. R-11700-B, Finding Paragraph 34. The order continues:

> Thus, where compulsory pooling is **not required** because of voluntary agreement or because of common ownership of the dedicated acreage, the practice of designating the acreage to be dedicated to the well on the [APD] furthers administrative expedience. Once the application is approved, no further proceedings are necessary.[2]

[2]The last sentence applies only where pooling is <u>not</u> required.

Order No. R-11700-B, Finding Paragraph 35 (emphasis added). The order further states:

> Thus, the process fosters efficiency by permitting a simple approach in cases **where ownership is common and pooling, voluntary or compulsory, is not required.**

Order No. R-11700-B, Finding Paragraph 36 (emphasis added).

(15) Leasehold ownership is not common in Section 25, and there are no voluntary agreements covering any well unit in Section 25.

(16) Based on the foregoing, TMBR/Sharp's APD does not control well unit orientation and operatorship, and the Division must decide the competing pooling cases based on the factors established in the Oil and Gas Act and in prior Commission orders. The primary factors controlling a decision in these cases are geology, engineering, and good faith negotiations. **NMSA 1978 §§70-2-17, 18; Commission Order No. R-10731-B.**

(17) Based on the forgoing, the Division concludes that:

(a) TMBR/Sharp did not make a good faith effort to obtain the voluntary joinder of the interest owners in the proposed N½ well unit. Therefore, TMBR/Sharp's Case No. 12816 must be dismissed. **Id.; Division Order No. R-10977.**

(b) Ocean made a good faith effort to obtain the voluntary joinder of the working interest owners in the W½ of Section 25.

(c) Arrington made a good faith effort to obtain the voluntary joinder of the working interest owners in the E½ of Section 25.

(d) TMBR/Sharp's N½ well unit is based solely on land considerations, because there is no Mississippian reservoir in the NE¼ of Section 25.

(e) Unnecessary wells may be drilled if a N½ unit is approved, thereby causing waste. Therefore, W½ and E½ units should be established, and the applications of Ocean in Case Nos. 12841 and 12860 and of Arrington in Case No. 12859 must be approved.

(f) Because TMBR/Sharp has commenced drilling a well in the SW¼NW¼ of Section 25, it should be allowed to continue drilling and operating the well until it reaches total depth

in order to minimize well costs. Upon reaching total depth, TMBR/Sharp shall turn over operations to Ocean (unless the well is a dry hole), and Ocean shall be designated the operator of the subject well and unit. At that time TMBR/Sharp shall execute the necessary Form C-102 as required by Division rules and regulations.

(18) To avoid the drilling of unnecessary wells, to protect correlative rights, to avoid waste, and to afford to the owner of each interest in the W½ unit the opportunity to recover or receive without unnecessary expense its just and fair share of hydrocarbon production in any pool resulting from this order, the applications in Case Nos. 12841 and 12860 should be approved by pooling all mineral interests, whatever they may be, within the unit comprised of the W½ of Section 25.

(19) To avoid the drilling of unnecessary wells, to protect correlative rights, to avoid waste, and to afford to the owner of each interest in the units in the E½ of Section 25 the opportunity to recover or receive without unnecessary expense its just and fair share of hydrocarbon production in any pool resulting from this order, the application in Case No. 12859 should be approved by pooling all mineral interests, whatever they may be, within the units in the E½ Section 25 described in Finding Paragraph No. (4) above.

(20) Any non-consenting working interest owner should be afforded the opportunity to pay its share of estimated well costs to the operator in lieu of paying its share of reasonable well costs out of production.

(21) Any non-consenting working interest owner who does not pay its share of estimated well costs should have withheld from production its share of the reasonable well costs plus an additional 200 percent thereof as a reasonable charge for the risk involved in drilling the well.

(22) Any non-consenting working interest owner should be afforded the opportunity to object to the actual well costs, but actual well costs should be adopted as the reasonable well costs in the absence of such objection.

(23) Following determination of reasonable well costs, any non-consenting working interest owner who has paid its share of estimated costs should pay to the operator any amount that reasonable well costs exceed estimated well costs and should receive from the operator any amount that paid estimated well costs exceed reasonable well costs.

(24) $6000 per month while drilling and $600 per month while producing should be fixed as reasonable charges for supervision (combined fixed rates). The operator should be authorized to withhold from production the proportionate share of such supervision charges attributable to each non-consenting working interest, and in addition thereto, the operator should be authorized to withhold from production the proportionate share of actual expenditures required for operating the subject well, not in excess of what are reasonable, attributable to each non-consenting working interest.

(25) Due to the title dispute affecting the NW¼ of Section 25, all potential interest owners in the disputed tract, if they elect to join in the Blue Fin 25 Well No. 1, shall pay their proportionate share of well costs into an escrow account to be established by Ocean in a bank located in Lea County. Funds in the escrow account shall be used to pay costs attributable to the NW¼ of Section 25, with any balance accruing interest until the title dispute is resolved. At such time, the funds in the account shall be returned to the unsuccessful parties in the dispute.

(26) All proceeds from production from the subject wells which are not disbursed for any reason should be placed in escrow to be paid to the true owner thereof upon demand and proof of ownership.

(27) If all parties to the forced pooling of the W½ of Section 25 reach voluntary agreement subsequent to entry of this order, the compulsory pooling provisions of this order should become of no effect.

(28) Upon the failure of the operator of the pooled unit comprising the W½ of Section 25 to commence drilling operations on the Triple Hackle Dragon 25 Well No. 2 on or before January 1, 2003, or if all parties to this forced pooling reach voluntary agreement subsequent to entry of this order, the compulsory pooling provisions of this order should become of no effect.

(29) Upon the failure of the operator of the pooled unit comprising the E½ of Section 25 to commence drilling operations on the Glass-Eyed Midge 25 Well No. 1 on or before October 1, 2002, or if all parties to this forced pooling reach voluntary agreement subsequent to entry of this order, the compulsory pooling provisions of this order should become of no effect.

(30) The operator of the wells and units should notify the Division in writing of the subsequent voluntary agreement of all parties to the compulsory pooling provisions of this order.

IT IS THEREFORE ORDERED THAT:

(1) The application of Ocean Energy, Inc. in Case No. 12841 is hereby approved, and all uncommitted mineral interests, whatever they may be, from the surface to the base of the Mississippian formation in the W½ of Section 25, Township 16 South, Range 35 East, N.M.P.M., are hereby pooled. The unit is to be dedicated to the currently drilling Blue Fin Well No. 1, located 1913 feet from the north line and 924 feet from the west line (Unit E) of Section 25.

(2) The application of Ocean Energy, Inc. in Case No. 12860 is hereby approved, and all uncommitted mineral interests, whatever they may be, from the surface to the base of the Mississippian formation in the W½ of Section 25, Township 16 South, Range 35 East, N.M.P.M., are hereby pooled. The unit is to be dedicated to the applicant's proposed Triple Hackle Dragon Well No. 2, to be located 1980 feet from the south and west lines (Unit K) of Section 25.

PROVIDED HOWEVER THAT the operator of the unit shall commence drilling operations on the well on or before the 1st day of January, 2003, and shall thereafter continue the drilling of the well with due diligence to a depth sufficient to test the Mississippian formation.

PROVIDED FURTHER THAT in the event the operator does not commence drilling operations on the well on or before the 1st day of January, 2003, Ordering Paragraph No. (2) shall be of no effect, unless the operator obtains a time extension from the Division Director for good cause shown.

PROVIDED FURTHER THAT should the well not be drilled to completion, or abandonment, within 120 days after commencement thereof, the operator shall appear before the Division Director and show cause why Ordering Paragraph No. (2) of this order should not be rescinded.

(3) The application of David H. Arrington Oil & Gas, Inc. in Case No. 12859 is hereby approved, and all uncommitted mineral interests, whatever they may be, from the surface to the base of the Mississippian formation underlying the following described acreage in Section 25, Township 16 South, Range 35 East, N.M.P.M., are hereby pooled in the following manner:

(a) The E½ to form a standard 320-acre gas spacing and proration unit for any and all formations and/or pools developed on 320-acre spacing within that vertical extent, which presently include but are not limited to the

Undesignated Shoe Bar-Atoka Gas Pool, Undesignated Townsend-Morrow Gas Pool and the Undesignated Townsend-Mississippian Gas Pool;

(b) The NE¼ to form a standard 160-acre gas spacing and proration unit for any and all formations and/or pools developed on 160-acre spacing within that vertical extent; and

(c) The E½NE¼ to form a standard 80-acre oil spacing and proration unit for any and all formations and/or pools developed on 80-acre spacing within that vertical extent.

The units are to be dedicated to the applicant's proposed Glass-Eyed Midge 25 Well No. 1, to be located 803 feet from the north line and 962 feet from the east line (Unit A) of Section 25.

PROVIDED HOWEVER THAT the operator of the units shall commence drilling operations on the well on or before the 1st day of October, 2002, and shall thereafter continue the drilling of the well with due diligence to a depth sufficient to test the Mississippian formation.

PROVIDED FURTHER THAT in the event the operator does not commence drilling operations on the well on or before the 1st day of October, 2002, Ordering Paragraph No. (3) shall be of no effect, unless the operator obtains a time extension from the Division Director for good cause shown.

PROVIDED FURTHER THAT should the well not be drilled to completion, or abandonment, within 120 days after commencement thereof, the operator shall appear before the Division Director and show cause why Ordering Paragraph No. (3) of this order should not be rescinded.

(4) The application of TMBR/Sharp Drilling, Inc. in Case No. 12816 is hereby dismissed.

(5) Ocean Energy, Inc. is hereby designated the operator of the Blue Fin 25 Well No. 1 and the unit comprised of the W½ of Section 25, provided that TMBR/Sharp Drilling, Inc. shall operate the well until total depth is reached, at which time operations shall be turned over to Ocean Energy, Inc. unless the well is a dry hole.

(6) The Hobbs District Office shall accept for filing and approve a Form C-102 to be submitted by Ocean Energy, Inc. designating a unit for the Blue Fin 25 Well No. 1 comprised of the W½ of Section 25.

(7) David H. Arrington Oil & Gas, Inc. is hereby designated the operator of the Glass-Eyed Midge 25 Well No. 1 and the unit comprised of the E½ of Section 25.

(8) The Hobbs District Office shall reinstate David H. Arrington Oil & Gas, Inc.'s Application for Permit to Drill for the Glass-Eyed Midge 25 Well No. 1.

(9) After pooling, uncommitted working interest owners are referred to as "non-consenting working interest owners." Within 30 days the effective date of this order, the operator shall furnish the Division and each known non-consenting working interest owner in the units an itemized schedule of estimated well costs.

(10) Within 30 days from the date the schedule of estimated well costs is furnished to it, any non-consenting working interest owner shall have the right to pay its share of estimated well costs to the operator in lieu of paying its share of reasonable well costs out of production, and any such owner who pays its share of estimated well costs as provided above shall remain liable for operating costs but shall not be liable for risk charges.

(11) The operator shall furnish the Division and each known non-consenting working interest owner an itemized schedule of actual well costs within 90 days following completion of the well. If no objection to the actual well costs is received by the Division and the Division has not objected within 45 days following receipt of the schedule, the actual well costs shall be the reasonable well costs; provided however, if there is objection to actual well costs within the 45-day period, the Division will determine reasonable well costs after public notice and hearing.

(12) Within 60 days following determination of reasonable well costs, any non-consenting working interest owner who has paid its share of estimated well costs in advance as provided above shall pay to the operator its pro rata share of the amount that reasonable well costs exceed estimated well costs and shall receive from the operator its pro rata share of the amount that estimated well costs exceed reasonable well costs.

(13) The operator of each well is hereby authorized to withhold the following costs and charges from production:

(a) The pro rata share of reasonable well costs attributable to each non-consenting working interest owner who has not paid its share of estimated well costs within 30 days from the date the schedule of estimated well costs is furnished; and

(b) As a charge for the risk involved in drilling the well, 200 percent of the above costs.

(14) The operator of each well shall distribute the costs and charges withheld from production to the parties who advanced the well costs.

(15) Reasonable charges for supervision (combined fixed rates) for each well are hereby fixed at $6,000.00 per month while drilling and $600.00 per month while producing, provided that this rate shall be adjusted annually pursuant to Section III.1.A.3 of the COPAS form titled "Accounting Procedure-Joint Operations." The operator is hereby authorized to withhold from production the proportionate share of such supervision charges attributable to each non-consenting working interest, and in addition thereto, the operator is hereby authorized to withhold from production the proportionate share of actual expenditures required for operating such wells, not in excess of what are reasonable, attributable to each non-consenting working interest.

(16) Any unleased mineral interest shall be considered a seven-eighths (7/8) working interest and a one-eighth (1/8) royalty interest for the purpose of allocating costs and charges under the terms of this order.

(17) Any well costs or charges which are to be paid out of production shall be withheld only from the working interest's share of production, and no costs or charges shall be withheld from production attributable to royalty interests.

(18) All potential interest owners in the NW¼ of Section 25, if they elect to join in the well, shall pay their proportionate share of well costs into an escrow account to be established by Ocean in a bank located in Lea County. Funds in the escrow account shall be used to pay costs attributable to the NW¼ of Section 25, with any balance accruing interest until the title dispute is resolved. At such time, the funds in the account shall be returned to the unsuccessful parties in the dispute.

(19) All proceeds from production from the subject wells which are not disbursed for any reason shall immediately be placed in escrow in Lea County, New Mexico, to be paid to the true owner thereof upon demand and proof of ownership; and the operator shall notify the Division of the name and address of the escrow agent within 30 days from the date of first deposit with the escrow agent.

(20) Should all the parties to this forced pooling order reach voluntary agreement subsequent to entry of this order, this order

shall thereafter be of no further effect.

(21) The operators of the well and units shall notify the Director of the Division in writing of the subsequent voluntary agreement of all parties subject to the forced pooling provisions of this order.

(22) Jurisdiction is hereby retained for the entry of such further orders as the Division may deem necessary.

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

STATE OF NEW MEXICO
OIL CONSERVATION DIVISION

LORI WROTENBERY
Director

[Seal]