

NEW MEXICO OIL CONSERVATION COMMISSION

COMMISSION HEARING

SANTA FE, NEW MEXICO

Hearing Date JANUARY 19, 1989 Time: 9:00 A.M.

NAME	REPRESENTING	LOCATION
Bule Hulin Vic Byron Jamaal Jennings	Byram OCD Red Bluff	Santa Fe "

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1 STATE OF NEW MEXICO  
2 ENERGY, MINERALS AND NATURAL RESOURCES DEPARTMENT  
3 OIL CONSERVATION COMMISSION  
4 STATE LAND OFFICE BUILDING  
5 SANTA FE, NEW MEXICO

6 19 January 1989

7 COMMISSION HEARING

8 IN THE MATTER OF:

9 Application of Mallon Oil Company CASE  
10 for compulsory pooling, Eddy County, 9458  
11 New Mexico. (De Novo)

12 BEFORE: William M. Humphries, Commissioner  
13 Erling Brostuen, Commissioner

14 TRANSCRIPT OF HEARING

15 A P P E A R A N C E S

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17 Attorney at Law  
18 Legal Counsel to the Division  
19 State Land Office Bldg.  
Santa Fe, New Mexico

20 For Mallon Oil Company: Ernest L. Padilla  
21 Attorney at Law  
22 PADILLA & SNYDER  
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23 For Red Bluff Water Power James T. Jennings  
24 Control District: Attorney at Law  
25 JENNINGS & CHRISTY  
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## I N D E X

1		
2		
3	STATEMENT BY MR. JENNINGS	6
4	STATEMENT BY MR. PADILLA	9
5		
6	KAREN E. McCLINTOCK	
7	Direct Examination by Mr. Padilla	11
8	Cross Examination by Mr. Jennings	26
9	Redirect Examination by Mr. Padilla	43
10	Recross Examination by Mr. Jennings	45
11	Questions by Mr. Humphries	48
12	Questions by Mr. Brostuen	51
13	Recross Examination by Mr. Jennings	53
14		
15	L. E. OPPERMANN	
16	Direct Examination by Mr. Padilla	61
17	Cross Examination by Mr. Jennings	69
18		
19	JOE H. COX, Jr.	
20	Direct Examination by Mr. Padilla	80
21	Cross Examination by Mr. Jennings	96
22	Questions by Mr. Brostuen	109
23		
24		
25		

## I N D E X Cont'd

1		
2		
3	DIRECT TESTIMONY BY JAMES T. JENNINGS	112
4	Questions by Mr. Stovall	113
5	Questions by Mr. Padilla	113
6	Questions by Mr. Humphries	116
7	Questions by Mr. Brostuen	121
8		
9	STATEMENT BY MR. PADILLA	122
10	STATEMENT BY MR. JENNINGS	124
11		
12		
13		
14	Mallon Exhibit One, Land Plat	15
15	Mallon Exhibit Two, Title Opinion	17
16	Mallon Exhibit Three, Operating Agreement	18
17	Mallon Exhibit Four, Letter	21
18	Mallon Exhibit Five, Data	25
19	Mallon Exhibit Six, Data	26
20	Mallon Exhibit Seven, Letter	65
21	Mallon Exhibit Eight, Letters	81
22	Mallon Exhibit Nine, Two Plats	82
23	Mallon Exhibit Ten, Letter	83
24	Mallon Exhibit Eleven, Letter	83
25	Mallon Exhibit Twelve, Topo Map	84

## E X H I B I T S Cont'd

1		
2		
3	Mallon Exhibit Thirteen, Data	85
4	Mallon Exhibit Fourteen, Cost Records	89
5	Mallon Exhibit Fifteen, Projection	90
6	Mallon Exhibit Sixteen, Production Data	93
7		
8	Red Bluff Exhibit One, Memo	55
9	Red Bluff Exhibit Two, Letter	78
10		
11		
12		
13		
14		
15		
16		
17		
18		
19		
20		
21		
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1 MR. BROSTUEN: In that case,  
2 we'll go to Case Number 9458, the de novo case, and read  
3 that.

4 MR. STOVALL: Application of  
5 Mallon Oil Company for compulsory pooling, Eddy County, New  
6 Mexico.

7 MR. BROSTUEN: The applicant  
8 in this case, it's a case that has been heard at one time  
9 previous by the -- an examiner. We have a request for a de  
10 novo hearing upon application of Red Bluff Water Power Con-  
11 trol District. The applicant initially in the case was  
12 Mallon Oil Company.

13 Have the attorneys in this  
14 case decided upon how they wish to proceed in this?

15 MR. PADILLA: Mr. Chairman, my  
16 name is Ernest L. Padilla, Santa Fe, New Mexico, for Mallon  
17 Oil Company.

18 To answer your question, we  
19 have have not gotten together as to how we shall proceed.

20 First, my inclination is that  
21 the applicant of the hearing should proceed to challenge  
22 the order of the Oil Conservation Division that was issued  
23 on October 28th, and accordingly, I would request that Mr.  
24 Jennings proceed with his part of the case first.

25 MR. BROSTUEN: In that case

1 I'll call for a response from Mr. Jennings.

2 MR. JENNINGS: Well, I am  
3 James T. Jennings and I am here on behalf of Red Bluff  
4 Reservoir. Unfortunately, our people aren't here. The  
5 manager of the project died since the last hearing and  
6 other people were not able to attend; however, it's my  
7 thought that in a de novo hearing such as this that it  
8 would be true de novo and we would hear all the evidence  
9 again so that the complete evidence is before -- you don't  
10 have the record before you or anything, and we would pro-  
11 ceed and let Mr. Padilla go forward with his -- with his  
12 case and again establish it.

13 If that is not -- I don't know  
14 where we are unless he does that. I could put these wit-  
15 nesses on and ask some things of them but it would be much  
16 simpler, since Mr. Padilla has a stack of exhibits at this  
17 time to let him proceed and go forward with that.

18 I might state at this time if  
19 you would want a statement of Red Bluff's position at this  
20 time --

21 MR. BROSTUEN: Mr. Jennings, I  
22 think at this time I simply -- I really would want to know  
23 if there's any agreement between attorneys.

24 I might call for appearances  
25 and then we will go into this case.

1 Mr. Padilla.

2 MR. PADILLA: Mr. Chairman,

3 Mr. Humphries, my name is Ernest L. Padilla, Santa Fe, New

4 Mexico, for Mallon Oil Company.

5 MR. BROSTUEN: And to you have

6 any --

7 MR. PADILLA: I have three

8 witnesses to be sworn.

9 MR. BROSTUEN: And could you

10 give me the names of the witnesses, please?

11 MR. PADILLA: Yes, sir. I

12 have Karen McKlintock, Les Oppermann and Joe Cox.

13 They will be testifying. Ms.

14 McClintock will be first and Mr. Oppermann second, and Mr.

15 Cox third.

16 MR. BROSTUEN: Mr. Jennings,

17 do you -- do you want to enter your appearance and witness-

18 ses?

19 MR. JENNINGS: I will. I

20 thought I had before, but I will enter it.

21 I'm James T. Jennings of Ros-

22 well, and I'll enter my appearance on behalf of Red Bluff

23 Water Power Control.

24 I do not have any witnesses.

25 MR. BROSTUEN: Would all those

1     testifying in Case Number 9458 please stand and take the  
2     oath?

3  
4                                     (Witnesses sworn.)

5  
6                                     MR. BROSTUEN: Is there a  
7     recommendation from the attorneys present as to whether we  
8     should incorporate the record in the previous case in this  
9     case, from either attorney?

10                                    MR. PADILLA: Mr. Chairman, I  
11    request that that record be incorporated and that adminis-  
12    trative notice be taken by the Commission of the record and  
13    the transcript that was taken in that hearing.

14                                    MR. BROSTUEN: Thank you, Mr.  
15    Padilla.

16                                    Mr. Jennings?

17                                    MR. JENNINGS: I don't object.

18                                    MR. BROSTUEN: You have no ob-  
19    jection to that?

20                                    In that case, inasmuch as Red  
21    Bluff Water Power Control District is the applicant in the  
22    de novo case, I would request that Mr. Jennings go forward  
23    with his case.

24                                    MR. JENNINGS: Well, I would  
25    say that unfortunately I didn't contemplate having to be

1 called upon to present Red Bluff for the Mallon applica-  
2 tion and I was further handicapped by the fact that I  
3 thought that last Friday morning, I thought the case had  
4 been continued until February the 16th and I learned this  
5 week, Tuesday at 11:00 o'clock, from the Commission that  
6 that is not the case and we would be on hand and we would  
7 not possibly -- it would be very awkward, I can go forward  
8 and bring out the points that I would want to bring out  
9 with adverse witnesses, but I think it would be much more  
10 orderly if Mr. Padilla went forward. He has his people  
11 here and he can go forward and then the Commission would be  
12 in a position to see -- to have the entire testimony pre-  
13 sented to them and they would be able to interrogate them  
14 and have the benefit of the other prior hearing, also.

15 I'd say that several things  
16 that have happened since October. One thing that changed  
17 the picture as of this date is the fact that the price of  
18 crude has improved to about \$13, a little over \$13.00 a  
19 barrel since October to -- now this is a spot market crude,  
20 has improved to \$19.26 a barrel as of yesterday.

21 And there's also been a very  
22 substantial increase in the posted price of crude, which is  
23 up, as I understand, in some areas, and I don't know where  
24 this crude has been marketed, but other parts of Eddy  
25 County, is \$17.75 cents a barrel.

1                   So this does make a substan-  
2 tial difference in everything.

3                   One other thing, I would like  
4 at this time to make an offer on behalf of Red Bluff Re-  
5 servoir to accept the proposal which was made, and I un-  
6 derstand it's since been withdrawn, and I don't know their  
7 position, it may be, but it would save everybody a lot of  
8 time and a lot of effort and money, if we -- we will be  
9 willing to assign Red Bluff's interest in the acreage to  
10 the proposed drilling formation and retain only a 5 percent  
11 overriding royalty and possibly Mr. Padilla would like to  
12 review this and if we do that, why, we can all go home.

13                   I wonder if there could be  
14 some water, it's awfully dry.

15                   MR. HUMPHRIES: I'll get some  
16 for you.

17                   Do you all want -- Mr. Chair-  
18 man, if they want to discuss this, make some further state-  
19 ments to the Commission, we could take a recess.

20                   MR. BROSTUEN: Would you like  
21 to, Mr. Padilla?

22                   MR. PADILLA: Mr. Chairman,  
23 Mr. Humphries, we have received the offer to accept a 5  
24 percent override that Mr. Jennings is speaking about. That  
25 was rejected last week.

1                   Mr. Jennings comes to us to-  
2 day without any witnesses, and he tells us he is unprepared  
3 to proceed. That was the same case before the Oil Conser-  
4 vation Division. The offer was made and actually withdrawn  
5 prior to the Division hearing.

6                   This is just simply too late  
7 in the game to start making any deals and as the evidence  
8 will show in this case, Mallon has had to obtain extensions  
9 of its farmout agreement with Amoco three times as the re-  
10 sult of delays in this case.

11                   There has been simply no  
12 agreement and at this point if Mr. Jennings' clients wish  
13 to participate in the well, they obviously have the right  
14 to participate, but to make deals on overriding royalty  
15 interest, we believe it is far too late and so we wish to  
16 proceed with our case. Mr. Jennings has asked that we pro-  
17 ceed with our case and I have no objection to proceeding  
18 with our part of the case, as long as the record reflects  
19 that we do not waive what we believe is Mr. Jennings'  
20 (unclear) of going forward first, but in the interest of  
21 orderly conduct of this hearing, I don't mind putting on  
22 my witnesses first.

23                   MR. BROSTUEN: Thank you, Mr.  
24 Padilla.

25                   The Commission will incorpor-

1 ate the previous record in this case. I would -- I know  
2 that Mr. Humphries and myself were not present when the  
3 previous testimony was given before the hearing examiner,  
4 and we believe we would like to incorporate the previous  
5 testimony and record as a means of, you might say, saving  
6 time and that sort of thing, because we don't really have  
7 to re-plow the same ground; however, in this case I do be-  
8 lieve that there should be full -- for myself, anyway, I  
9 need to have some sort of a -- I would appreciate a review  
10 of previous testimony and what was done in the past so that  
11 I have a basis for finding the decision.

12 MR. PADILLA: Mr. Chairman, we  
13 will present our testimony in the same fashion that we did  
14 before with additions, so in that respect you will have  
15 pretty much the same picture as we presented at the Oil  
16 Conservation Division in Santa Fe.

17 MR. BROSTUEN: Very well, I'd  
18 appreciate it.

19 Just a moment, we'll have a  
20 short recess here, maybe five minutes, so that we can get  
21 some water down here.

22 MR. JENNINGS: All right.

23  
24 (Thereupon a recess was taken.)  
25

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MR. BROSTUEN: So we'll continue the hearing. Mr. Padilla?

MR. PADILLA: Mr. Chairman, we call Karen McClintock.

KAREN E. McCLINTOCK,  
being called as a witness and being duly sworn upon her oath, testified as follows, to-wit:

DIRECT EXAMINATION

BY MR. PADILLA:

Q Ms. McClintock, for the record would you please state your name and where you're employed?

A My name is Karen McClintock and I'm a landman for Mallon Oil Company.

Q Is Mallon Oil Company the applicant in the original forced pooling application before the Oil Conservation Division?

A Yes.

Q Did you testify as land manager in that previous case for Mallon Oil Company?

A Yes, I did.

Q Have you previously testified before the Oil Conservation Division as a petroleum landman?

1           A           Yes, I have.

2           Q           Have your records been -- have your  
3 credentials been accepted as a matter of record as a petro-  
4 leum landman in previous hearings of the Oil Conservation  
5 Division?

6           A           Yes.

7                           MR. PADILLA: Mr. Chairman, we  
8 tender Ms. McClintock as a petroleum landman.

9                           MR. BROSTUEN: Her qualifica-  
10 tions are accepted.

11           Q           Ms. McClintock, briefly would you please  
12 state what your -- what the background of this hearing is,  
13 if you would, please?

14           A           Yes. Mallon Oil Company wants to drill  
15 a well in the northwest quarter of the southwest quarter of  
16 Section 27, Eddy County, New Mexico.

17                           Mallon Oil Company did not control  
18 through a farmout with Amoco 100 percent of the 40-acre  
19 proration unit. Mallon Oil Company, through a farmout with  
20 Amoco only controlled approximately 75 percent of the  
21 40-acre unit. The remaining approximately 25 percent,  
22 specifically 24.3175, is controlled by Red Bluff Water  
23 Power Control District.

24           Q           What efforts did you make to contact and  
25 reach agreement with Red Bluff Water Control Power

1 District?

2           A           Mallon Oil Company employed Les Opperman,  
3 landman who is very familiar with the area, and also  
4 with Red Bluff Water Power Control District, to negotiate  
5 with Red Bluff Water Power Control District, which he had  
6 been doing for over a year for -- on behalf of Mallon Oil  
7 Company.

8           Q           When did you first start making efforts  
9 to acquire the interest of -- controlled by Red Bluff?

10           A           Mallon Oil Company contacted the BLM because  
11 the acreage that Red Bluff Water Power Control District  
12 controls now was not available for lease. When I  
13 contacted the BLM there was a lot of confusion as to what  
14 to do with the Red Bluff acreage.

15                       Mallon Oil Company -- this was in 1987.  
16 Subsequently Mallon found, after the initial contact with  
17 the BLM, found that Mallon Oil Company was not eligible to  
18 bid on the acreage. It was a compulsory royalty agreement  
19 and due to the statutes, Red Bluff Water Power Control District,  
20 who had the right-of-way on the reservoir, and Amoco  
21 Production Company, who is the record title owner, were the  
22 only two companies able to bid on the acreage that Mallon  
23 Oil Company was interested in. The reservoir is pretty  
24 extensive. There were some other companies involved but  
25 Mallon Oil Company only had interest in acreage that Red

1 Bluff Reservoir controlled in Section 27 and 28.

2 Q When did you -- was a lease issued to  
3 Red Bluff eventually?

4 A Yes, it was.

5 Q And what efforts did you make to acquire  
6 that lease?

7 A Prior to the issuance of the lease we  
8 had Mr. Oppermann contact Red Bluff Water Power Control  
9 District. He contacted verbally and visited with both the  
10 manager, a Mr. John Hayes, and Mr. Fuller, the President of  
11 the Executive Committee of Red Bluff Water Power Control  
12 District.

13 Q What were the results of those efforts  
14 to obtain an agreement from Red Bluff?

15 A Mallon Oil Company had given Mr. Opper-  
16 mann (not clearly understood) to negotiate. We had in --  
17 prior to issuance of a lease we had attempted to negotiate  
18 an approximately 50 percent overriding royalty to Red Bluff  
19 Water Power Control District. It would be to farmout with  
20 no back in, simply an overriding royalty.

21 In June of last year Mr. Oppermann again  
22 contacted Red Bluff Water Power Control District and offer-  
23 ed a 5 percent overriding royalty.

24 Q Did they, did Red Bluff reject the 6 per  
25 cent?

1           A           Yes.    The information that Mr. Oppermann  
2   mann had given me over the phone after he had met with Mr.  
3   Hayes and Mr. Fuller was that the 5 percent would possibly  
4   be acceptable, and shortly after that Mr. Jennings, I was  
5   contacted by Mr. Jennings and it was not acceptable.

6           Q           When did you file for compulsory pooling  
7   of the reservoir interest?

8           A           It was in August of 1988.

9           Q           And was an order issued by the Division  
10  as a result of a hearing?

11          A           No.    The hearing for August, in the  
12  latter part of August, was postponed. It was postponed  
13  twice, due to the request of Mr. Jennings. It was issued  
14  in October of 1988.

15          Q           But an order was eventually issued?

16          Q           Yes, that is correct.

17          Q           Okay.   Let me -- let me have you refer  
18  to what we have marked as Exhibit Number One and have you  
19  identify that for the Commission, and tell the Commission  
20  what that contains.

21          A           Certainly.   This is a land plat of the  
22  acreage in Section 27, the northwest of the southwest (not  
23  clearly understood) the Amoco-Red Bluff Federal No. 1 Well,  
24  and I've identified with pink the Federal Lease NM-71599.  
25  That is the lease that is owned by Red Bluff Water Power

1 Control District.

2 In yellow is Federal Lease NM-38636,  
3 which is a lease that Mallon Oil Company has continuous  
4 drilling obligation with Amoco. It is owned currently,  
5 record title and operating rights, by Amoco Production  
6 Company. Mallon Oil Company has the farmout rights on that  
7 section.

8 I have broken down the acres involved  
9 pursuant to a plat prepared by John West Engineering. Ac-  
10 cording to Mr. West's plat, Red Bluff Lease 71599, is ap-  
11 proximately 9.727 acres, giving it a 24.3175 percent inter-  
12 est in the 40-acre proration unit. The (not clearly under-  
13 stood) payments would be the percentage they would pay.

14 Mallon Oil Company's lease, the Amoco  
15 Production Company lease, is 30.273 acres with 75.68250  
16 percent working interest, in the event that Red Bluff Water  
17 Power Control District will (not clear.)

18 Q Is the State acreage under water? Is  
19 that the -- do you know that?

20 A No, to my understanding it's not. Mr.  
21 Cox will be able to -- he's been out on the location.

22 Q But it's the acreage attributable to the  
23 Red Bluff lease?

24 A Correct.

25 Q Let's go on now to what we have marked

1 as -- well, do you have anything further concerning Exhi-  
2 bit Number One, before we move on?

3 A I would like to mention, on the origi-  
4 nal hearing that the interest is altered slightly from the  
5 original hearing and let me identify these changes. Mallon  
6 Oil Company, in the original hearing was under the impres-  
7 sion that the proration unit was 38.5 acres. We have found  
8 (unclear) 40-acre proration unit, that increases Red Bluff  
9 Water Power Control District's interest, not their acres,  
10 only their interest, by less than 1 percent on the original  
11 interest that Mallon Oil Company identified in the hearing  
12 was 25.26494 percent working interest for Red Bluff, and as  
13 you can see, it dropped down to 24.3175, so that's less  
14 than a 1 percent interest and I have contacted Mr. Jennings  
15 with the change.

16 Q Was that error based upon your percep-  
17 tion of the 40-acre tract being smaller than the standard  
18 40-acre tract?

19 A Yes, we had originally identified it as  
20 a 38.5 acre proration unit, and this, the changes, would  
21 have identified Exhibit One as the correct breakdown in  
22 terms of acreage and percentage.

23 Q Let's go on now to Exhibit Number Two,  
24 Ms. McClintock, and have you identify that for the Com-  
25 mission.

1           A           Yes.    This  is  a  drilling  title  opinion  
2  for  the  Amoco  Red  Bluff  No.  1  Well.  It  was  prepared  by  the  
3  (unclear)  in  Denver  and  is  (unclear).

4           Q           What  information  does  this  drilling  
5  title  opinion  contain  as  far  as  is  relevant  to  this  hear-  
6  ing?

7           A           It  does  identify  that  Red  Bluff  Water  
8  Power  Control  District  does  indeed  have  the  rights  to  
9  Federal  Lease  NM-71599  and  that  Amoco  Production  Company  
10 had  the  rights  to  Federal  Lease  NM-38636,  both  of  which  are  
11 involved  in  this  northwest  southwest  of  Section  27,  our  
12 drill  site.

13          Q           Let's  go  on  to  Exhibit  Number  Three,  Ms.  
14 McClintock,  and  have  you  identify  that  for  the  Commission.

15          A           Yes.  Exhibit  Number  Three  is  Mallon  Oil  
16 Company's  operating  agreement  dated  January  19,  1989,  
17 proposed  operating  agreement  between  Mallon  Oil  Company  and  
18 Red  Bluff  Water  Power  Control  District.

19          Q           What  is  the  area  covered  by  that  opera-  
20 ting  agreement?

21          A           We  have  limited  it  to  the  drill  site  
22 itself,  the  northwest  of  the  southwest  of  Section  27.

23          Q           What  --  let's  turn  now  to  the  COPAS  sec-  
24 tion  of  that  operating  agreement,  Ms.  McClintock,  and  iden-  
25 tify  that  location;  in  other  words,  what  page  is  the  COPAS

1 section of that agreement?

2 A Okay. The COPAS is attached as Exhibit  
3 C to the operating agreement.

4 Q Let me have you turn to page 4 of that  
5 COPAS section and have you tell the Commission what -- what  
6 the overhead charges that you have identified in that  
7 portion of the operating agreement are.

8 A The drilling well rate is \$3,056 and the  
9 producing well rate \$334.

10 Q Is this indicative of the overhead char-  
11 ges for this type of well in that area of New Mexico?

12 A Absolutely. These charges are the char-  
13 ges that we billed to our working interest owners and (not  
14 clearly audible) Mallon Oil Company.

15 Q How many wells is Mallon operating in  
16 that area?

17 A We have 13 in the area; this will be our  
18 14th well.

19 Q How many wells have you drilled using  
20 these figures?

21 A This figure changes every year and I be-  
22 lieve it was different as of last June.

23 Q Since last June are these figures stand-  
24 ard for your operating agreements in that area?

25 A Absolutely.

1           Q           Let's turn now to the penalty provisions  
2 of the operating agreement and will you tell the Division  
3 on what page those provisions are?

4           A           They're on page 6 of the operating  
5 agreement.

6           Q           What are those penalty provisions, Ms.  
7 McClintock?

8           A           400 percent.

9           Q           Is that more than the penalty provision  
10 allowed by the Oil Conservation Division as a result of the  
11 compulsory pooling -- as a result of the compulsory pooling  
12 hearing?

13          A           Yes, it is.

14          Q           You understand that under a compulsory  
15 pooling hearing you cannot obtain 400 percent.

16          A           That's correct.

17          Q           Let me ask you, also, is this 400 per-  
18 cent indicative of what's -- your standard operating agree-  
19 ments in the area, this particular portion of Eddy County,  
20 New Mexico?

21          A           Yes, it is. Our operating agreements in  
22 the area all carry a 400 percent penalty.

23          Q           In your opinion is this a reasonable  
24 penalty?

25          A           Yes, I think it is totally appropriate.

1 Q Ms. McClintock, let's move on now to  
2 what we have marked as Exhibit Number Four and have you  
3 tell the Commission what Exhibit Number Four is and what it  
4 contains.

5 A Yes. Mr. Jennings had mailed me a let-  
6 ter dated November 23rd, 1988, outlining some concerns he  
7 had concerning an operating agreement that I had mailed to  
8 him previously.

9 Q What is the -- without going -- without  
10 reading the entire contents of the letter, would you tell  
11 us more or less what -- what the letter -- what the corres-  
12 pondence is about?

13 A Yes. Mr. Jennings was concerned with  
14 basically two issues. Number one was the nonconsent pen-  
15 alty and the other one was the overhead charges in the  
16 COPAS. He felt like they were in error as compared to the  
17 ones previously mailed to him.

18 Q What was your response to his inquiries?

19 A My response was a letter dated November  
20 29th. I explained to him that -- well, I apologized for  
21 any confusion as to the content of any operating agreements  
22 we had previously mailed, but we felt that they were exam-  
23 ples.

24 We also felt that the penalty, although  
25 the order had specified 300 percent, I am under the impres-

1 sion that the operating agreement we mailed to him would be  
2 in the event that Red Bluff Water Power Control District  
3 elected to participate in the well, the order would not  
4 affect our operating agreement. I felt like a 400 percent  
5 penalty was fair and reasonable and in line with the other  
6 operating agreements everyone else has signed for this  
7 particular prospect.

8 His other concern were the overhead  
9 charges on the COPAS and that was an error and I explained  
10 to him I was not changing it because of the order. He had  
11 intimated in his letter that I needed to change it because  
12 of the order. I changed it because it behooved our ac-  
13 counting department to have one overhead charge as opposed  
14 opposed to two overhead charges, so it would be fair to Mr.  
15 Jennings and our accounting department to have one, the  
16 same overhead charge.

17 Q Was that a lower overhead charge?

18 A Yes, it was. I originally had 4000 for  
19 drilling and completing, 400 for producing, and I had re-  
20 duced it to the 3056 for drilling and completing and 334  
21 for producing.

22 Q Ms. McClintock, what other communica-  
23 tions did you have with Mr. Jennings or anyone from Red  
24 Bluff since the issuance of the Division order in October,  
25 1988?



1 amount of time, money, and effort we'd put into this, the  
2 negotiations for Red Bluff Water Power Control District  
3 with the Amoco No. 1 Well, Mallon Oil Company could not  
4 justify economically accepting an offer that we had offered  
5 eight months ago and they had rejected.

6 Q Was that offer of 5 percent withdrawn  
7 before the Oil Conservation Division hearing in October?

8 A Yes.

9 Q After that offer was rejected, what was  
10 your course of action insofar as compulsory pooling was  
11 concerned? Did you have a choice as to what you wanted to  
12 do? In other words, was your only avenue at that point  
13 compulsory pooling?

14 A You mean as of last week or initially?

15 Q Well, initially.

16 A Initially? We had no other choice.  
17 Mallon Oil Company, this was, according to our geologist  
18 and engineer, this was the best location for us to drill  
19 and we did not want to take a risk and jump over and drill  
20 on property that Mallon Oil Company controlled 100 percent.  
21 This was our best location, we felt. We had no other  
22 choice. Red Bluff Water Power Control District did not  
23 want to participate and they did not want to accept our  
24 terms.

25 Q Ms. McClintock, before I forget, Mallon

1 Oil Company desires to be named the operator in any order  
2 issued by the Oil Conservation Commission.

3 A That's correct.

4 Q Let me refer you to what we have marked  
5 as Exhibit Number Five and have you identify that for the  
6 Commission.

7 A This is a memo from Elizabeth Redmond in  
8 our office to myself dated October 6, 1988. It was just an  
9 outline of potential overriding royalties for Federal Lease  
10 NM-38636, which is the Amoco Production Company lease that  
11 Mallon Oil Company controls.

12 Q What is the effect of those numbers on  
13 that memo?

14 A The overriding royalty identified on  
15 this memo affects only Federal Lease NM-36 -- I'm sorry --  
16 38636. It does not affect Red Bluff Waster Power Control  
17 District's lease.

18 Q In terms of economics of drilling the  
19 well, how does -- how does the total lease burden affect  
20 your drilling plans?

21 A I believe Mr. Cox can best address that.

22 Q Okay. This simply is just a memorandum  
23 from someone under your supervision telling you what the  
24 burden is?

25 That's correct. Those burdens were

1 created through a farmout agreement Mallon Oil Company has.

2 Q Okay. Let me refer you to what we have  
3 marked as Exhibit Number Six, and have you identify that,  
4 please.

5 A Yes. This information is on completion  
6 costs and administrative overhead costs for the Amoco Red  
7 Bluff Federal No. 1 Well.

8 Q Have these figures been submitted to Red  
9 Bluff for the drilling of this well?

10 A Yes, they have.

11 Q Ms. McClintock, do you have anything  
12 further concerning your testimony with regard to Exhibits  
13 One through Six?

14 A No.

15 MR. PADILLA: Mr. Chairman, we  
16 would tender Exhibits One through Six.

17 MR. BROSTJEN: Without objec-  
18 tion they will be admitted.

19 MR. PADILLA: And we pass the  
20 witness at this time.

21 MR. BROSTJEN: Mr. Jennings?

22

23 CROSS EXAMINATION

24 BY MR. JENNINGS:

25 Q Ms. McClintock, when did you say you

1 first became aware of Red Bluff's interest in part of the  
2 acreage under this particular 40-acre subdivision?

3 A We were aware that Amoco Production  
4 Company did not control 100 percent of the 40-acre prora-  
5 tion unit. At that time it was not leased. That acreage  
6 was owned by the Red Bluff Reservoir and not by Red Bluff  
7 Water Power Control District, and that was when we initial-  
8 ly elected to drill that location.

9 Q Well, when did you -- is that the infor-  
10 mation you obtained from the Bureau of Land Management?  
11 The Bureau of Land Management (not clearly understood.)

12 A The Bureau of Land Management confirmed  
13 that Red Bluff Reservoir had a portion of the acreage  
14 within the proration unit.

15 Q Then I think you've testified that was  
16 about the time that you were considering bidding on that  
17 acreage?

18 A We elected or we had decided to try --  
19 to attempt to bid on the acreage but I really don't remem-  
20 ber if it was after or at the same time. I truly don't  
21 remember.

22 Q When was the original location staked?

23 A I believe you'll have to ask Mr. Cox  
24 that question.

25 Q Would you ask Mr. Cox and tell us?

1 MR. STOVALL: If I may inter-  
2 ject, Mr. Chairman, is that information in the original  
3 proceedings, do you remember, Mr. Padilla, in the trans-  
4 cript?

5 MR. PADILLA: I believe -- I  
6 can't recall for sure. I think that question was asked of  
7 someone at the last hearing, if I'm not mistaken. That's  
8 what I'm trying to establish.

9 MR. COX: Yeah, I think it was  
10 -- I don't know the exact date, December of 1987, that's  
11 when our APD was filed for the Amoco well at the time.

12 MR. PADILLA: Well, I'll stip-  
13 ulate to that in the record.

14 MR. BROSTUEN: Excuse me, what  
15 was the date again?

16 MR. COX: December, '87.

17 MR. JENNINGS: Well, can we  
18 put it on the record?

19 MR. BROSTUEN: December, 1987,  
20 will that suffice to answer your question, Mr. Jennings?

21 MR. JENNINGS: Yes.

22 Q At the time that you made this location,  
23 were you aware -- you were not aware -- let me say this.  
24 At the time you made the location you were not aware of Red  
25 Bluff's position.

1           A           Mr. Cox has identified the location in  
2 December, '87. Mallon Oil Company was aware previous to  
3 that the Mallon Oil Company, Amoco Production Company Fed-  
4 eral lease did not cover the entire 40-acre proration unit,  
5 so Mallon Oil Company was aware that Red Bluff Reservoir,  
6 the interest of Red Bluff Reservoir controlled at least  
7 part of the location.

8                           We were aware prior to the staking.

9           Q           Did your application show -- show that,  
10 your application to drill?

11           A           I believe the application to drill shows  
12 the 40-acre proration unit in the quarter quarter section.

13           Q           Do you know when the drilling pad was  
14 constructed?

15           A           Again, Mr. Cox handled that.

16           Q           I believe you testified that your offer  
17 of 5 percent, to pay a 5 percent overriding royalty was  
18 withdrawn before the last hearing.

19           A           Mallon Oil Company felt that the fact  
20 that the offer had been rejected, and we were forced to go  
21 through with a compulsory pooling, that it was not open for  
22 negotiation. We felt like the forced pooling was actually  
23 the way to proceed.

24           Q           Well, you said that, that your offer was  
25 withdrawn before the last hearing. I understood you to

1 testify that Mallon had withdrawn the offer, and I just  
2 wanted to (not clearly audible).

3 A Yes, it had been withdrawn.

4 Q How?

5 A We had proceeded with the forced  
6 pooling. Mallon Oil Company and Red Bluff Water Power  
7 Control District had not settled on any type of percentage  
8 or any type of penalty in terms of percentage or

9 Q Did you ever notify Red Bluff that the  
10 offer was withdrawn?

11 A I feel that the notification of forced  
12 pooling would be adequate.

13 Q Answer -- I mean not how you feel, did  
14 you notify them?

15 A We notified them through the application  
16 for forced pooling, Mr. Jennings.

17 Q That's the only way?

18 A Yes, at least from my standpoint.

19 Q Do you ever remember any conversation  
20 with me about the time this location was first announced  
21 telling you of Red Bluff's interest?

22 A Yes, I had a conversation with you when  
23 this location was first announced, (not clearly understood)  
24 Red Bluff Water Power Control District did not have a  
25 lease.

1           Q           Well, I know that but I told you at that  
2 time it would be hazardous to go forward with the drilling,  
3 announce a location and drilling without that other acre-  
4 age, did I not?

5           A           I believe so, but I felt that it was im-  
6 material to how you felt about it when Mallon Oil Company  
7 had every right to proceed. I contacted the BLM, question-  
8 ed them, and I felt like Mallon Oil Company's best position  
9 was to proceed.

10          Q           Well, why did they -- why did they not  
11 proceed, then?

12          A           Mallon Oil Company cannot drill a well  
13 without getting some type of settlement in terms of working  
14 interest, overriding royalty, or whatever you want to call  
15 it, in terms of having 100 percent of a proration unit.

16                   Mallon Oil Company proceeded building,  
17 staking, and things like that. We did proceed with that.  
18 We did not proceed when I talked to you prior to Red Bluff  
19 Water Power Control getting the lease because we felt we  
20 could not drill without at least talking with Red Bluff.

21          Q           But you were aware of all this when you  
22 made the location.

23          A           Yes, we were. The location is 100 per-  
24 cent on NM-38636 lease. The location is not all on Red  
25 Bluff's lease.

1           Q           I'll refer you to your Exhibit Number  
2 Five and ask you what your net revenue interest would be on  
3 this lease NM-38636?

4           A           The exhibit you're referring to is a  
5 memo from Elizabeth Redmond (unclear)?

6           Q           Yes. Elizabeth Redmond.

7           A           Okay. For this particular well?

8           Q           Yes.

9           A           Amoco Red Bluff No. 1 Well would have a  
10 burden of, Amoco Production Company, JSM Oil & Gas, Inc.,  
11 and Interfirst Bank of Abilene, and Don and Micki Carol  
12 Wright control that interest, and the Minerals Management  
13 Service.

14          Q           Well, I'm just asking you to state what  
15 your net revenue interest will be in the well.

16          A           I'd have to calculate that. I don't  
17 have that written down anywhere right now, right offhand.

18          Q           Well, if you have a 30 percent burden  
19 and you have 100 percent --

20          A           No, Mr. Jennings, you didn't listen to  
21 me.

22                       Mr. Bettis and Mr. Oppermann will have  
23 an undivided royalty (not clearly understood).

24          Q           And if you would accept Red Bluff's  
25 offer and take an assignment of the lease, at least a

1 partial assignment of the lease, as to the other acreage,  
2 as to the Red Bluff portion, you would then have 81 per-  
3 cent net revenue interest.

4 A On the Red Bluff lease that would be  
5 correct.

6 Q Wouldn't that be substantially better  
7 than you have on what you're going to drill on?

8 A You've got to understand that the Lease  
9 38636, Mallon Oil Company got their interest in that in  
10 1983. We had no choice at that time (not clearly under-  
11 stood) that lease. We felt they were acceptable at the  
12 time. We feel that the 5 percent that we had offered to  
13 you in June, or Red Bluff Water Power Control District, was  
14 acceptable in June, without the added expense of attorneys  
15 and the (not clearly understood) we had to have.

16 Q Well, what amount was that expense?

17 A The attorney's fees?

18 Q Yeah.

19 A The time --

20 Q What's the dollar amount?

21 A I don't have that figure, Mr. Jennings.

22 Q Well --

23 A Mr. Jennings, I don't have that figure.

24 Q Do you have any idea? Was it \$100,000,  
25 a Million Dollars, or --

1           A           Well, we have Mr. Padilla's expense, Mr.  
2 Oppermann's expense, my time, Mr. Cox's time, and the trips  
3 down here have all added in.

4           Q           Well, you don't know whether it's \$5000,  
5 \$10,000 or what?

6           A           No, I don't.

7           Q           You feel that -- it's your feeling, the  
8 reason is that you just don't want to allow Red Bluff any  
9 overriding royalty because you've been out some expense on  
10 this?

11          A           Not only that, Mr. Jennings, but as I  
12 explained to you in my telephone conversation and earlier  
13 in the hearing, is that we had two deadlines that we have  
14 to meet, and when you initially offered this to us, and  
15 now, we do not feel that we could accept a 5 percent over-  
16 riding royalty.

17          Q           You didn't tell me why, but didn't I  
18 tell you that if we were going to do it, we could get it  
19 done before the first of your deadlines?

20          A           Yes, Mr. Jennings, you did mention that  
21 that would be a possibility. Personally, I felt, and my  
22 company felt, that we could not -- we did not want to take  
23 that chance that something might prevent us from drilling  
24 on the deadline. We did not accept that just because you  
25 said that it could be done. We felt that we just could not

1 accept it.

2 Q You just didn't want to have anything to  
3 do with it, is that it?

4 A Mr. Jennings, we felt like we'd been  
5 fair with Red Bluff Water Power Control District in offer-  
6 ing the same overriding royalty back in June; in fact, the  
7 year before we'd offered them an additional 1 percent for a  
8 total of 6 percent. We felt like we had a deal with Red  
9 Bluff Water Power Control District; it had been changed  
10 when we received a phone call from you.

11 We feel that we have given Red Bluff  
12 Water Power Control District ample time and opportunity to  
13 either participate or accept an overriding royalty from  
14 Mallon Oil Company.

15 We felt your phone call a week before  
16 this hearing and very close to our deadline, that was just  
17 not acceptable.

18 Q Have you made any efforts -- what was  
19 the last effort you made to settle this matter with --  
20 with Red Bluff?

21 A If I recall correctly, we were scheduled  
22 for an August hearing. That was postponed because we  
23 thought perhaps there might be a chance to negotiate some  
24 type of settlement. I believe it was extended into Septem-  
25 ber. As of September we have not been able to reach a set-

1 tlement with Red Bluff Water Power Control District, so I  
2 would say September was the last time we actively attempted  
3 to negotiate with Red Bluff.

4 Q Well, do you feel that the additional 11  
5 percent that you would get interest under this acreage com-  
6 pared to the other acreage would not offset your legal ex-  
7 penses, a substantial interest?

8 A We feel that the burdens (not clearly  
9 understood) were not Mallon's choices or (unclear). We  
10 feel that these people are entitled to some type of over-  
11 riding royalty and whether accepting a higher net revenue  
12 interest on Red Bluff's lease would offset our legal expen-  
13 ses is not really for me to say or to calculate at this  
14 time.

15 We feel the climate in the industry now  
16 could not warrant a heavier burden than 5 percent; at least  
17 we felt that was in June of 1988.

18 Q Well, have you re-evaluated it in the  
19 light of the recent substantial increase in the price of  
20 crude (not clearly audible)?

21 A If I understand what you're getting at,  
22 this particular well --

23 Q Just answer my question.

24 A I'm sure that (unclear) more and more  
25 detail. These are very expensive wells to drill and we

1 feel the price of crude is immaterial at this point, at  
2 least in the industry as it stands now with the fluctuation  
3 in the price of oil.

4 Q Have you ever made any offer, cash offer  
5 to Red Bluff to acquire their interest in the lease?

6 A In the entire lease?

7 Q No, it this 40 acres, the acreage in  
8 question, the 40 acres.

9 A No, we've not. At least I have not per-  
10 sonally.

11 Q You haven't explored that?

12 A No, we haven't.

13 Q Do you think that lease has any value?

14 A I'm sure Mr. Cox will be able to answer  
15 that from an engineering and geological standpoint.

16 Q Well, you're a qualified land person,  
17 you ought to know that.

18 A I'm sure it would have some value large-  
19 ly depending on the area and the wells we have drilled.

20 Q Well, what would you say the value is as  
21 a qualified land person?

22 A I think that would be difficult to an-  
23 swer because of the fact that we had to not pay for the  
24 lease from Amoco. We earned it through a farmout. I be-  
25 lieve Mr. Oppermann is more familiar with the dollar value

1 of acreage in that area.

2 Q Do you now feel that forced pooling will  
3 allow Red Bluff to get a fair and equitable treatment to  
4 protect their interest in this 40-acre subdivision?

5 A Yes, I do.

6 Q Are you not just using the forced pool-  
7 ing statute to attempt to browbeat Red Bluff into giving  
8 you a lease?

9 A I hardly think so, Mr. Jennings. I feel  
10 like we've given Red Bluff Water Power Control District  
11 ample opportunity to participate or accept an overriding  
12 royalty. I would hardly call over nine months of negotia-  
13 tions browbeating.

14 Q I think I understand you can't testify  
15 to these negotiations because all these have been carried  
16 out by Mr. Oppermann.

17 A At my direction.

18 Q One other thing, if Mr. Oppermann ac-  
19 quired this lease would you have been obligated to pay Mr.  
20 Oppermann and Mr. Bettis a 5 percent overriding royalty on  
21 it?

22 A Under the terms of the Bettis/Oppermann  
23 agreement which Mallon Oil Company was subject to by virtue  
24 of the Amoco farmout, yes, if Les Oppermann was responsible  
25

1 for the negotiation and the acceptances of some type of  
2 settlement from Red Bluff Water Power Control District,  
3 yes, under the terms of the contract they would, Bettis and  
4 Oppermann would receive a 5 percent, 2-1/2 percent apiece,  
5 which would be proportionately reduced.

6 Q But you were willing to give them 5  
7 percent rather than deal direct with Red Bluff.

8 A I had hired Mr. Oppermann to handle the  
9 negotiations because we are extremely busy and I did not  
10 have time to do it. He's familiar with Red Bluff Water  
11 Power Control District, specifically Mr. Haynes and Mr.  
12 Fuller, and I felt at the time it was worth the expense to  
13 have Mr. Oppermann negotiate it.

14 Since that time, not only have we (not  
15 clearly understood) and of course that does change things  
16 quite a bit.

17 Q But does that offset the 5 percent over-  
18 riding royalty under a well? It seems to me that's a  
19 pretty big bonus just to get the lease when you could get  
20 it direct from someone else without having them in it.

21 A We were willing to pay Red Bluff Water  
22 Power Control District. We were willing to give them a 5  
23 percent overriding royalty regardless of what Mr. Oppermann  
24 and Mr. Bettis' fee, but we feel that regardless of what  
25 Mr. Oppermann and Bettis' fee, we feel that our offer to

1 Red Bluff Water Power Control District was fair and reason-  
2 able.

3 Q Well, that would have involved you  
4 having a better net revenue interest but you would still  
5 not have -- you'd only have 76 percent in the event, would  
6 you not, or 75 percent?

7 A In the event that Mr. Oppermann was suc-  
8 cessful in his negotiations?

9 Q Yes.

10 A We offered a 5 percent and 5 percent  
11 would have gone to Mr. Bettis and I believe that's 10 per-  
12 cent overriding royalty.

13 Q 10 percent overriding royalty, and we  
14 had (not clearly understood), but now you don't want to --  
15 I understand -- are you going to give Mr. Oppermann 5 per-  
16 cent overriding royalty on this well?

17 A He will have an overriding royalty on  
18 Federal Lease 38636.

19 Q But do you have any obligation to him on  
20 the Red Bluff Lease, which is No. 71599, or something like  
21 that?

22 A Mr. Oppermann was not successful in his  
23 negotiation, no, he's not entitled to an overriding roy-  
24 alty.

25 Q Well, now, your position is better,

1 then, if you give Red Bluff their 5 percent, you -- you  
2 would now be six points better off than you were.

3 A It's what you consider better, Mr. Jen-  
4 nings, we've also put a lot of money into this particular  
5 well in addition to the normal expenses in terms of legal  
6 and having Mr. Oppermann, and Mr. Oppermann has put a lot  
7 of time and effort into this, due to this sort of hearing,  
8 and that type of thing.

9 Q Well, all these legal expenses will be  
10 borne by all of your other people, all of your other par-  
11 ticipants in the well, will they not?

12 A Yes, sir, but we do have an obligation  
13 to our working interest partners to keep the expenses at a  
14 minimum. We do agree to that in the operating agreement,  
15 to be a prudent operator.

16 Q Yeah, but the clause in which you would  
17 include the legal fees in your overhead, that would be  
18 stricken from the operating agreement, would it not?

19 A We do not include our legal fees in our  
20 overhead charge. No, we don't. They are billed out sep-  
21 arately.

22 Q That is stricken from the COPAS form.  
23 The COPAS form does (unclear) leave that out.

24 A We would have it stricken from the  
25 actual operating agreement, part of the formal operating

1 agreement, not the COPAS. I believe it's in the COPAS,  
2 also, but we've taken it out of the original operating  
3 agreement, also.

4 Q Did you make any offer to Red Bluff for  
5 its interest?

6 A We would like -- I have talked to Mr.  
7 Fuller, we would like to follow through to Red Bluff on the  
8 additional wells drilled the --

9 Q No, I'm talking about this one.

10 A If you wish to talk about the condition  
11 of this particular well, the Amoco Federal No. 1 Well, no,  
12 Mallon --

13 Q You're determined to force pool them and  
14 nothing else. That's the only thing that will satisfy you.

15 A I believe you're the one determined, but  
16 we at Mallon Oil Company feel that we have no other choice.

17 Q So you'll make money with any override,  
18 you just want to earn it under the provisions of the  
19 statute.

20 A We feel that they have every right to  
21 participate.

22 Q I think we're well aware of that, but  
23 that's the only thing they can do, is participate.

24 A At this stage of this hearing, yes.

25 Q And you have not made any effort since

1 last September to make a deal with Red Bluff and that ef-  
2 fort was made when it would have been burdened by a 5 per-  
3 cent overriding royalty for Mr. Oppermann and Mr. Bettis.

4 A Yes.

5 MR. JENNINGS: That's all.

6 MR. BROSTUEN: Mr. Padilla?

7

8 REDIRECT EXAMINATION

9 BY MR. PADILLA:

10 Q Ms. McClintock, has Red Bluff accepted  
11 any offer that you have made to Red Bluff, any kind of  
12 joinder or made any kind of a deal?

13 A Not to me, no. It was intimated by Mr.  
14 Oppermann that they had agreed on 5 percent but we have  
15 never received that in writing nor was that confirmed later  
16 on by Red Bluff.

17 Q Have these delays -- you have -- well,  
18 let me ask this question first. Do you have a continuous  
19 drilling obligation in this project or this (unclear)?

20 A Yes, we do, under the Amoco farmout  
21 we're required to drill a well every 90 days.

22 Q Have you been delayed in your drilling  
23 program as a result of the delays that you have encountered  
24 in this case?

25 A Yes.

1           Q           Have you had to negotiate with Amoco  
2 concerning extensions of time for your farmout agreements  
3 as a result of the delays in this case?

4           A           Yes, we have.

5           Q           If you force pool the interest of Red  
6 Bluff, you will have to pay and carry the working interest  
7 of Red Bluff, is that correct?

8           A           That is correct, and share it with our  
9 working interest owners, if (not clearly audible).

10          Q           Approximately how much money in rough  
11 terms would you have to provide to drill or provide for Red  
12 Bluff's interest?

13          A           We would be responsible for 100 percent  
14 of the working interest, which is the 24 percent identified  
15 in Exhibit, the 24.3175, and the AFE charges, which are --  
16 24 percent of whatever the AFE charges on Mallon Oil Com-  
17 pany, et al, is responsible for carrying.

18          Q           So very close to one-fourth, is that --

19          A           That is correct.

20          Q           And what are the total drilling costs  
21 that you have shown on your exhibit? I believe it's  
22 Exhibit Six.

23          A           Yes. The total completed well costs are  
24 \$313,600.

25          Q           So in order to drill the well you would

1 have to provide one-fourth of that cost to carry the Red  
2 Bluff interest.

3 A Yes, over and above Mallon Oil Company's  
4 original working interest.

5 Q Are your economics for drilling this  
6 well based on the entire 40-acre proration unit?

7 A Mr. Cox prepared the economics.

8 Q Okay. Ms. McClintock, do you believe  
9 that all of the offers that you made to Red Bluff were  
10 reasonable?

11 A Yes, I do.

12 MR. PADILLA: I believe that's  
13 all I have, Mr. Chairman.

14 MR. BROSTUEN: All right,  
15 thank you.

16 Mr. Jennings?

17 MR. JENNINGS: Just a couple  
18 of questions.

19

20 RE CROSS EXAMINATION

21 BY MR. JENNINGS:

22 Q How many -- when did you first get this  
23 farmout from Worth?

24 A Worth took a farmout from Amoco, I mean  
25 from Harry Bettis in September, 1983, and Mallon Oil Com-

1 pany negotiated with Worth Petroleum in 1985, I believe.

2 Q And how many extensions of -- since 1985  
3 I believe, you've drilled how many wells? Six?

4 A No. Mallon Oil Company has only been  
5 (unclear) made operator, so if you're talking about when  
6 Mallon Oil Company was operator how many --

7 Q No, no, how many wells did you drill  
8 since you became operator?

9 A Since we became operator, Mallon Oil  
10 Company has drilled four, I believe -- five.

11 Q Five wells.

12 A Since Mallon Oil Company has been the  
13 operator.

14 Q And you were named operator in 1985?

15 A To be quite honest with you, I don't re-  
16 call when. It was over a length of time. We were invol-  
17 ved in a lawsuit with Mr. Worth (not clearly audible) with  
18 Worth Petroleum.

19 Q You don't know when you became operator?

20 A I do not --

21 Q Do you have the same operating agreement  
22 now that you had with Worth?

23 A No, we don't.

24 Q Was the operating agreement that you had  
25 with Worth, did that have a 400 percent penalty clause in

1 it?

2 A Yes, it did.

3 Q And you signed that one, too; you were a  
4 non-operator in that one.

5 A We were a non-operator when we accepted  
6 this farmout from Amoco.

7 Q Well, you said that you got a number of  
8 extensions from Amoco. How many extensions have you gotten  
9 or when did you get the last extension?

10 A For this particular well we've had to  
11 request three different extensions, so I believe the last  
12 extension was through October 1st to the 15th and then at  
13 that time, we knew we would not meet that deadline and we  
14 requested a February 1st deadline -- extension, which it  
15 was granted.

16 Q Do you have a copy of that?

17 A No, I don't, not here.

18 Q Is it in your files?

19 A Yes, it is.

20 Q Would you furnish us and the Commission  
21 copies of the 1st two extensions?

22 A Certainly.

23 MR. PADILLA: I have no objec-  
24 tion.

25 MR. BROSTUEN: Does anyone

1 else have any further questions of the witness?

2 Bill?

3

4 QUESTIONS BY MR. HUMPHRIES:

5 Q When you first contacted -- maybe I'd  
6 better restate that.

7 Were you first contacted by Red Bluff or  
8 did you contact Red Bluff?

9 A In the initial negotiation?

10 Q Uh-huh.

11 A Mr. Oppermann contacted Red Bluff.

12 Q And at that time it was obvious that Red  
13 Bluff did not have a lease?

14 A Mr. Oppermann contacted Red Bluff and  
15 they did not have a lease. The lease was issued, I be-  
16 lieve, in June of '88, so it was very recent.

17 Q The lease was issued in June of '88  
18 under what authority?

19 A It's really (unclear), I think it's  
20 actually a right-of-way and we've got a copy of that, I be-  
21 lieve, or at least at the last hearing we did. It was a  
22 compensatory royalty agreement and that's the authority it  
23 was issued under. It was my understanding from the BLM it  
24 was rather unusual.

25 Q So it was not issued subject to Federal

1 oil and gas leases.

2 A To be honest with you, I do not recall.  
3 I do know when we got it it was different from the standard  
4 oil and gas -- Federal oil and gas leases, and with the  
5 drilling title opinion I believe my attorney went into some  
6 detail concerning that issue and what are the differences  
7 between the two leases. It's a very unusual lease.

8 Q So that at some point Red Bluff indi-  
9 cated to you that they were certain they were going to ac-  
10 quire this royalty interest and it was only a matter of  
11 time.

12 A Yes. What had happened was when I talk-  
13 ed to the BLM in order to be able to bid on the compensa-  
14 tory royalty agreement, we were informed that Mallon Oil  
15 Company, because they were not a record title owner, could  
16 not bid; only Amoco Production Company, who is the record  
17 title owner, could bid, as well as Red Bluff.

18 When I contacted Amoco to see if they  
19 would bid, they informed me they could not tell me. It was  
20 later on when I contacted I don't recall the name of the  
21 individual, she said that it had been at least preliminar-  
22 ily issued to Red Bluff Water Power Control District, only  
23 a certain portion of it because they were waiting for the  
24 final stamp of approval.

25 At that point we wanted to be -- we'd

1 been contacting Red Bluff, I mean Mr. Oppermann the year  
2 before, and we actually waited until after a lease was  
3 issued in order to finalize any agreement we could make,  
4 you know, prior to the lease being issued.

5 Q When you say "bid" was it competitively  
6 bid at one of the BLM sales?

7 A No. It was most unusual. What they do,  
8 is they don't -- it's my understanding, Mr. Jennings might  
9 be able to correct me, I don't believe it's bid in terms of  
10 any monetary amount but actually bid on the royalty, how  
11 much you're going to pay for a royalty, so no money is ac-  
12 tually paid, I believe. I believe you just bid on the  
13 royalty.

14 Q That would account for a 14 percent --

15 A Right.

16 Q -- royalty.

17 MR. PADILLA: I'll be glad to  
18 inform the Commission about the lease.

19 MR. HUMPHRIES: No, I under-  
20 stand now how -- why Red Bluff would have anticipated the  
21 lease on the bid.

22 Q Now, you indicated and I apologize, I  
23 was -- I didn't have the time to listen to your answer,  
24 that you informed Red Bluff, I believe you and Mr. Jennings  
25 did, that although the Commission not only is to allow for

1 a 400 percent penalty, you felt like that your agreement  
2 was not subject to the ruling of the Oil Conservation Div-  
3 ision examiner hearing?

4 A It was my understanding that we had 30  
5 days from the decision of the hearing in which to allow  
6 them time to participate. At that point I mailed them our  
7 operating agreement and AFE giving them 30 days to elect to  
8 participate.

9 Q To elect to participate as a working in-  
10 terest.

11 A Correct. And to the operating agreement  
12 we felt wouldn't deny -- was not affected by the decision  
13 and we felt the 400 percent was fair and reasonable.

14 MR. HUMPHRIES: I have no fur-  
15 there questions.

16 MR. BROSTUEN: I only have one  
17 question for clarification.

18  
19 QUESTIONS BY MR. BROSTUEN:

20 Q I've heard reference to the Red Bluff  
21 Reservoir and the Red Bluff Water Power Control District.  
22 What are the relationships between those two entities and  
23 perhaps you can explain that to me.

24 A Perhaps Mr. Jennings would be better to  
25 answer that.

1 MR. JENNINGS: We just refer  
2 to it as Red Bluff. It's all one organization. It's a  
3 water power control established in the early 1940's for ir-  
4 rigation and power, although we no longer develop it for  
5 power but it's all one and the same. They are not two  
6 different entities. Red Bluff Reservoir is where the water  
7 is but the right-of-way and the lease goes to Red Bluff  
8 Water Power Control District.

9 MR. BROSTUEN: I see, it's all  
10 one.

11 MR. HUMPHRIES: May I follow  
12 up?

13 I'm not -- do I understand,  
14 the, it's a Texas corporation and not a federally endorsed  
15 irrigation project?

16 MR. JENNINGS: Well, I'm sure  
17 the Federal put the money up for it.

18 MR. HUMPHRIES: But would it  
19 be similar to --

20 MR. JENNINGS: The Bureau of  
21 Reclamation was involved in it at that time, as I under-  
22 stand, and they made the reservoir at the time, you know,  
23 it's on the Pecos River.

24 MR. HUMPHRIES: Would it be  
25 similar to a conservancy district or authorized irrigation

1 district?

2 MR. JENNINGS: I would say  
3 that, yes. They're definitely not involved in (unclear) so  
4 they can participate in the well; they're owned by the  
5 water users or what not, and this -- this is under the act  
6 of I believe it was May 21, 1930, (not clearly audible)

7 MR. HUMPHRIES: Thank you.

8

9

RE CROSS EXAMINATION

10 BY MR. JENNINGS:

11 Q There's one thing. Do you remember me  
12 calling you in Santa Fe and I can't remember what -- just  
13 after the sale had been conducted by the Bureau of Land  
14 Management and advising you that Red Bluff Water Power Con-  
15 trol District was successful bidder?

16 A Yes.

17 Q Do you remember me advising you a long  
18 time ago just after I talked to the -- or just after I saw  
19 your location of Red Bluff's interest?

20 A Yes.

21 MR. PADILLA: Mr. Chairman, I  
22 have nothing further.

23 MR. BROSTUEN: Okay, did you  
24 wish to enter these exhibits at this time?

25 MR. PADILLA: Yes, sir. We'll

1 offer Exhibits One through Six.

2 MR. BROSTUEN: They will be  
3 admitted.

4 We'll recess for ten minutes.

5

6 (Thereupon a recess was taken.)

7

8 MR. BROSTUEN: Ms. McClintock,  
9 we're going to recall you to the stand, please.

10 Mr. Jennings?

11 Q Ms. McClintock, I want to hand you here  
12 a memorandum which I just took from my file concerning this  
13 matter and the first date is August 20, 1987, and there's a  
14 little note on there dated 8-24, and there's another memo-  
15 randum dated September 21, 1987, about Red Bluff, and these  
16 were -- this was taken from my file.

17 I want you to read this, it will take a  
18 minute, it's three pages, if the Commission will bear with  
19 me while she can read it and then tell me what statements  
20 recited in this memorandum are not correct.

21 MR. PADILLA: May I have a  
22 second to read that memorandum?

23 MR. BROSTUEN: Sure.

24 You may proceed, Mr. Jennings.

25 Q Ms. McClintock, after you've read that I

1 wish you would point out the areas that you want -- the  
2 areas, the statements therein that you feel are not cor-  
3 rect.

4 MR. BROSTUEN: Can we please  
5 identify the memorandum?

6 MR. JENNINGS: I will -- I  
7 will do it for this purpose. I -- I don't have any copies  
8 yet but we will identify this as Red Bluff Exhibit Number  
9 One.

10 MR. BROSTUEN: And it's a  
11 memorandum from whom to whom?

12 MR. JENNINGS: It's a memoran-  
13 dum, I thought I stated this, maybe I didn't, but from me  
14 to my file in connection with the transactions. These are  
15 memos made in the course of negotiations which I prepared  
16 and placed in my file. I'm a pretty old guy and it's hard  
17 to remember everything and I just want to offer these to  
18 this witness.

19 MR. HUMPHRIES: Mr. Chairman,  
20 may I suggest I'll take Mr. Jennings and get a copy of that  
21 made so the Commission may have it.

22 MR. BROSTUEN: Very good.  
23 Let's -- Mr. Padilla's got something.

24 MR. PADILLA: Mr. Chairman --

25 MR. JENNINGS: That's fine.

1 I'll be glad for you -- that would be great. You can read  
2 it. I want you to read it now.

3 MR. BROSTUEN: Mr. Padilla.

4 MR. PADILLA: I'm going to  
5 object to the -- to this introduction of this memorandum.  
6 If Mr. Jennings wants to testify or bring witnesses, he may  
7 bring witnesses to refute anything that Ms. McClintock may  
8 have said. I'm not sure what the purpose of introducing  
9 his own internal memorandum is. As I understand, that's an  
10 internal memorandum and it's Mr. Jennings version of what-  
11 ever may have occurred in conversation, or whatever was  
12 said in conversation between Mr. Jennings and Ms. McClin-  
13 tock here. Obviously he's trying to, I believe, refute  
14 anything that -- something that she may have said in her  
15 testimony.

16 On that basis I believe that's  
17 hearsay. If Mr. Jennings is willing to take the stand and  
18 testify concerning that, I suppose that he should be sworn  
19 in to introduce this memorandum in that fashion.

20 MR. BROSTUEN: Well, I sustain  
21 your objection.

22 Mr. Jennings, would it be your  
23 intention to want to be placed under oath and present your  
24 memorandum yourself?

25 MR. JENNINGS: No, sir. I'm

1 not a professional witness. I'm a lawyer and I don't  
2 propose to testify. I think this is an exception to the  
3 hearsay rule. It's a memorandum made in the ordinary  
4 course of business. And this memorandum is a memorandum  
5 that I made and placed in my file back in 1987 after con-  
6 versations with Ms. McClintock, and I want to offer this to  
7 show the history of the relations and conversations we had,  
8 I have personally had with her about Red Bluff being --  
9 containing a lease and then making a deal with Mallon and  
10 -- concerning this lease in question, and I think it's an  
11 exception to the hearsay rule. I think counsel would ad-  
12 vise you it's a memorandum made in the ordinary course of  
13 business. That's the only reason I offer it, to show what  
14 -- maybe Mr. Hayes could -- but he's dead, unfortunately,  
15 being in his position, he may have talked to the young lady  
16 about some of the deal and I just want to show what -- and  
17 this will give you some idea about Red Bluff's participa-  
18 tion without Mr. Oppermann's help.

19 MR. PADILLA: Mr. Chairman, I  
20 don't have any quarrel with Mr. Jennings' assessment of the  
21 hearsay rule with respect to records used in the ordinary  
22 course of business, if Mr. Jennings was a witness or some-  
23 one in his organization or his side was the one presenting  
24 the memorandum. I just don't think it's proper for Mr.  
25 Jennings to try to discredit Ms. McClintock with something

1 that she did not write.

2 MR. BROSTUEN: I agree. Mr.  
3 Jennings, if you would care to withhold the memorandum and  
4 ask the questions from the memorandum in conversation, that  
5 would be acceptable.

6 MR. JENNINGS: Well, this is  
7 -- well, I'm must trying to -- I don't want to be here all  
8 day and it's pretty lengthy. I just wanted her to point  
9 out what -- if the notes I made were fine, that's all I  
10 wanted to know, but if they're not correct, she can point  
11 them out. That's the reason I was doing it this way was so  
12 I wouldn't have to ask a specific question on each thing.

13 Now I can go through that and  
14 do it, but I just think it would be pertinent. You can  
15 take this and you don't want to consider it, why, that's  
16 your business. If I show you that and she denies of the  
17 statements I put down there, I just want her to point them  
18 out to you.

19 Unfortunately I was a party to  
20 the location at that time and I don't want to be in a  
21 position to come up here and testify.

22 MR. BROSTUEN: What is the --  
23 I guess I fail to see the direction we're going with this,  
24 Mr. Jennings, for her to concur with that statement or --

25 MR. JENNINGS: Well, just I

1 told her to read it and point out anything that wasn't  
2 correct and then I want to show it to you, or I'll be glad  
3 to show it to you or we can get copies that would expedite  
4 it, but maybe you wouldn't want to do that.

5 I'm just trying to save a lot  
6 of time.

7 MR. BROSTUEN: Well, I've  
8 sustained Mr. Padilla's objection and I will continue to,  
9 so I think we should move on to something else.

10 If you want to present your --  
11 this as evidence and present yourself as a witness, that  
12 would be acceptable (not clearly audible) --

13 MR. JENNINGS: Well, do you  
14 want me to ask her about all these things?

15 MR. BROSTUEN: What purpose  
16 would it serve, Mr. Jennings?

17 MR. JENNINGS: Well, I wanted  
18 to show the absurdity of her going to get Oppermann to deal  
19 with Red Bluff and put another 5 percent on this lease,  
20 when I originally -- in this document it shows that I  
21 contacted her I believe it was in August of 1987 after I  
22 noticed the notice of intention to drill.

23 And I advised her and she was  
24 aware of it and she sent somebody, Mr. -- that man at the  
25 BLM in Roswell -- Armando Lopez, had advised her to go

1 ahead -- they'd made -- they'd made this location for the  
2 well, and he gave her this advice to go ahead and drill.

3                   And I told her about the Red  
4 Bluff position and that Red Bluff, I indicated that Red  
5 Bluff was trying to get a lease and would get the lease,  
6 and I indicated therein and we discussed a farmout, and  
7 things like that in there, and then there was a later deal  
8 when I talked to her and pointed out other things. And I  
9 just want to show that -- if this is not correct, I just  
10 want her to tell me that.

11                   MR. BROSTUEN: Mr. Jennings,  
12 is this -- has this been presented in previous hearings or  
13 --

14                   MR. JENNINGS: No. It's just  
15 -- it's just a memorandum on yellow paper --

16                   MR. BROSTUEN: At this time --

17                   MR. JENNINGS: -- that I made  
18 after my conversations with this lady about our -- the  
19 nature of our discussion, discussions, because I couldn't  
20 remember them, and this ties down the times and everything.

21                   MR. BROSTUEN: I think at this  
22 time we'll proceed with the -- with the next witness and at  
23 the end of the -- at the end of the hearing, Mr. Jennings,  
24 then we may consider your request.

25                   The witness is excused.

1 Mr. Padilla.  
2 MR. PADILLA: Mr. Chairman,  
3 I'll call Mr. Oppermann.  
4

5 L. E. OPPERMANN,  
6 being called as a witness and being duly sworn upon his  
7 oath, testified as follows, to-wit:  
8

9 DIRECT EXAMINATION

10 BY MR. PADILLA:

11 Q Mr. Oppermann, would you for the record  
12 please state your full name and where you reside?

13 A L. E. Oppermann, Midland, Texas.

14 Q Mr. Oppermann, were you a witness at the  
15 Division hearing in this matter?

16 A Yes.

17 Q And have you previously testified before  
18 the Oil Conservation Division as a petroleum landman?

19 A Yes.

20 Q And your credentials have been accepted  
21 as a matter of record?

22 A Yes.

23 Q You were involved in the negotiations  
24 over obtaining a joinder or some other agreement with Red  
25 Bluff?

1           A           Yes, sir.

2                           MR. PADILLA: Mr. Chairman, we  
3 tender Mr. Oppermann as a petroleum landman.

4                           MR. BROSTUEN: His qualifica-  
5 tions are acceptable.

6           Q           Mr. Oppermann, let me ask you to detail  
7 the -- in general, the negotiations that you had with Red  
8 Bluff and in so doing I would ask you to start on the very  
9 first time that you contacted Red Bluff concerning (not  
10 clearly understood.)

11           A           Well, first of all, we may go back a  
12 little further in 1983 when we put the deal together we  
13 were aware of the 200+ acres that were outstanding in the  
14 Amoco lease when we received the farmout.

15                           We made inquiries about it and then we  
16 finally limited it to where -- where Red Bluff had the op-  
17 tion as a right-of-way owner to acquire the lease.

18                           So I talked on the telephone in March of  
19 April, probably in April of 1988 with Mr. John Hayes and on  
20 May the 24th, 1988 I met with Doug Fuller and John Hayes in  
21 Pecos about the lease after it had been issued.

22           Q           Mr. Hayes is the gentleman that is de-  
23 ceased at this time.

24           A           Yes, sir.

25           Q           At that time you were dealing with Mr.

1 Fuller's well, is that correct?

2 A I had met with Mr. Fuller personally on  
3 May the 24th. I was dealing with Mr. Hayes.

4 Q You mentioned that as far back as 1983  
5 you were trying to buy this acreage. Was that trying to  
6 acquire it on behalf of Mallon or on behalf of yourself, or  
7 how was this --

8 A On behalf of myself and Worth Petroleum  
9 Company.

10 Q Now, did you acquire that interest?

11 A No.

12 Q You mentioned 200 acres. Does that mean  
13 200 acres that is not under the Red Bluff acreage or what  
14 -- what --

15 A It's a 207.something acres that's  
16 excepted out of the Amoco lease where the wells have been  
17 drilled on.

18 Q And that is the Red Bluff acreage?

19 A That is the Red Bluff acreage.

20 Q Okay, now tell us, why were you trying  
21 to acquire this acreage?

22 A Because we saw after we drilled the  
23 first couple of wells, we had some producing oil wells and  
24 we were trying to tie up the whole and trying to figure out  
25 a way, what to do, and I first contacted Joe Shultz of

1 Shultz Abstract here in Santa Fe and he did the initial  
2 investigation and everything lead to a deadend.

3 Q Why did it lead to a deadend?

4 A Because nobody -- it was unique situa-  
5 tion and nobody at BLM knew actually what to do. So we  
6 tried to get it put up as a bid with directional drilling  
7 stipulation on the lake itself, just like any other BLM,  
8 but we were told by statute it was set aside in a differ-  
9 ent category. This is back, to the best of my memory here,  
10 in '83 or '84.

11 Q Well, what happened after that? This,  
12 well, how did this lease -- do you know how this lease be-  
13 came an addition to Red Bluff?

14 A Not the details, no, sir, but I know it  
15 was issued and it took a long time before the lease was  
16 actually issued. I think Mr. Jennings had a lot to do with  
17 getting the lease issued to Red Bluff, and I knew Red Bluff  
18 was getting the lease and it probably took about six months  
19 to a year before the lease was actually issued after they  
20 advised that they were getting a lease on the -- on the  
21 acreage.

22 Q Approximately what time did you start  
23 negotiating with Red Bluff?

24 A Well, I wrote them a letter in '87. At  
25 that time I was assuming that they were getting a lease

1 with a 12-1/2 percent burden and I sent them a letter. I  
2 think a copy is there enclosed, where I was asking them to  
3 furnish me an assignment retaining an override being the  
4 difference between current burdens on the lease and 80 per-  
5 cent.

6 Q Mr. Oppermann, I've handed you what we  
7 have marked as Exhibit Number Seven and ask you to identify  
8 that for the Commission, please.

9 Yes, that's a letter of April 22nd from  
10 myself to John Hayes at Red Bluff; a letter dated June the  
11 7th, 1988, from myself to Red Bluff; and a letter dated  
12 September 9th, 1988, from myself to Karen McClintock, fur-  
13 nishing copies of these letters showing my actual offers to  
14 Red Bluff.

15 Q Why did Mallon contact you to acquire  
16 this acreage?

17 A Back in 1983 when this deal was sold to  
18 Worth Petroleum, an area of mutual interest was formed,  
19 which included all of that township. I think that's Town-  
20 ship 26 South, Range 29 East, and under the terms of the  
21 agreement with Worth, which was later acquired by Mallon, I  
22 was to do the land work and to acquire leases for the Fed-  
23 eral accounts in this area.

24 Q As a result of the assignment from Worth  
25 or the transfer, Mallon was under the basic contract --

1           A           Right.

2           Q           -- for you to do the land work.

3           A           Yes, sir.   Mallon assumed position in  
4 the agreement.

5           Q           And that was by virtue of an area of  
6 mutual interest.

7           A           Yes, sir.

8           Q           That you had with Worth.

9           A           Right.

10          Q           Okay, now tell us what -- further about  
11 your efforts to -- and meetings to acquire this interest  
12 for Red Bluff.

13          A           I first met with -- I mean talked with  
14 Mr. Hayes on the telephone several times and finally agreed  
15 to -- I knew, personally, I knew Dub Fuller, who was  
16 President, I think is his title, of Red Bluff. I had  
17 dealings with him before on the Texas side when I worked  
18 for Exxon. I bought leases from Red Bluff and I met him.

19                        So I made arrangements to meet with Mr.  
20 Fuller and Mr. Hayes on May the 24th in their office in  
21 Pecos.

22                        We met. We discussed all the possibili-  
23 ties and I left Pecos that afternoon with the assumption  
24 that I felt like we had a deal on this present location,  
25 being the Mallon Red Bluff No. 1, with a 5 percent over-

1 ride on it and possibly the same deal on the No. 14, which  
2 was an offset to the 13, which is the most recent well  
3 drilled in the area, and I left there with the feeling that  
4 we had a deal at 5 percent.

5 Q What -- what happened after that?

6 A I contacted Ms. McClintock at Mallon,  
7 told her I felt like we had a successful visit; we had a  
8 deal, and they had to bring it up at the board and they  
9 were meeting, I think their meeting is on the first Monday  
10 or Tuesday in each month, so it would be probably two weeks  
11 and they would come back.

12 I was wrong in my assumption and Mr.  
13 Hayes come back and said that the 5 percent was not a sat-  
14 isfactory deal.

15 Q Did he make -- did he give you an ex-  
16 planation why 5 percent was not acceptable?

17 A Not that I can recall. He was asking  
18 for a lot bigger override, I understand that.

19 Q Now you mentioned before that you had  
20 dealt with Red Bluff on prior occasions in Texas. Can you  
21 tell us about that?

22 A Yes. I was working for Exxon and they  
23 had some acreage that we were interested in acquiring and  
24 they had to go through the statute in Texas by advertising  
25 it three weeks in the Pecos paper and I think two neighbor-

1 ing papers, and after that the lease was issued on a bid-  
2 type bid being on bonus money, royalty and term.

3 Q About how many leases did you transact  
4 with Red Bluff?

5 A I'd say roughly five to ten.

6 Q Well, did you consider the people you  
7 dealt with as novices in the oil business?

8 A No, sir.

9 Q How recent did you have any communica-  
10 tions from Red Bluff?

11 A After, say, about the middle of June, I  
12 talked to them one or two times after they --

13 Q In what year?

14 A June of 1988, after they turned down the  
15 offer which was a 5 percent offer that was made on the  
16 visit of May 24th.

17 After that I furnished them with num-  
18 erous production records and other information which I  
19 think is stated in the letter. That was the last letter  
20 whereby I justified our overriding offer of 5 percent.

21 And I've contacted, I've talked to Mr.  
22 Hayes one or two times after that.

23 Q And I take it you failed to reach any  
24 agreement.

25 A Right. I reported to Ms. McClintock

1 that my 5 percent override was not accepted.

2 MR. PADILLA: Mr. Chairman, I  
3 believe that's all I have of this witness.

4 I will offer Exhibit Number  
5 Seven.

6 MR. BROSTUEN: Any objection,  
7 Mr. Jennings?

8 MR. JENNINGS: No.

9 MR. HUMPHRIES: I have a ques-  
10 tion. I think it's just a misstatement. My letter says  
11 September the 6th and Mr. Oppermann said September 9th.  
12 Are we in fact looking at the same letter?

13 A Maybe I just looked at the wrong date. I  
14 know --

15 MR. HUMPHRIES: You read it  
16 upside down.

17 A Yeah, it is 6.

18 MR. HUMPHRIES: All right, I  
19 just wanted to make sure I had the same letter.

20 A I'm sorry.

21 MR. HUMPHRIES: Thank you.

22 MR. BROSTUEN: Mr. Jennings?

23

24

CROSS EXAMINATION

25 BY MR. JENNINGS:

1           Q           You said that offer was not -- Red Bluff  
2 finally advised you that that offer was not acceptable.

3           A           The offer of the 5 percent override?

4           Q           Yes, sir.

5           A           No, sir.

6           Q           Did they tell you why?

7           A           Yes, they told me why. They wanted a  
8 higher override. They felt that the 5 percent was too low.

9           Q           But if you had -- they had of accepted  
10 that offer, then you would have -- in addition to the 5  
11 percent that they would get, you would have gotten 5 per-  
12 cent, too.

13          A           Yes, sir.

14          Q           Did -- and when did -- I believe you  
15 stated you had these discussions in March and May, April  
16 and May --

17          A           April and May, yes.

18          Q           -- of 1988.

19          A           Yes, sir.

20          Q           And you hadn't talked to Red Bluff about  
21 this particular figure before that date.

22          A           Yes, sir, there's a letter in there  
23 where I talked to them in '87 and I talked to them in '86.  
24 I probably talked to them every year since '83.

25          Q           And did they advise you after the --

1 that's part of Exhibit Seven, is it not?

2 A Yes, sir.

3 Q And you wrote them in April of 1987?

4 A Yes, sir.

5 Q Were you working for yourself at that  
6 time or for Mallon?

7 A I was working for myself in behalf of  
8 Mallon, due to our area of mutual interest.

9 Q And at all times you felt that since  
10 Mallon acquires this lease and even though they acquire it  
11 direct, that you would be entitled to 5 percent?

12 A Yes, sir, that's part of the letter  
13 agreement and the area of mutual interest.

14 Q So notwithstanding anything else, you're  
15 entitled to 5 percent on this lease. If we force pooled it,  
16 would you be entitled to 5 percent, too?

17 A No, sir.

18 Q So it's only if --

19 A Only if the lease is acquired.

20 Q By them?

21 A By them or me. If it's --

22 Q Well, are they forbidden under the  
23 letter agreement from trying to acquire a lease directly  
24 during the time that you were acquiring?

25 A They could acquire a lease but my over-

1 ride and my partner's override was still binding. In the  
2 same light, if I acquired it, I had to offer that to them  
3 first in that township before I could offer it to any other  
4 party.

5 Q What was the term of that letter, did it  
6 go forever, or what?

7 A There was no limitation on the term of  
8 it.

9 Q Was this a letter dated February 23rd,  
10 1983?

11 A Yes, sir, I think that is the letter,  
12 agreement --

13 Q This letter?

14 A -- of mutual interest. Yes, sir.

15 Q To expedite matters, I think that was  
16 Exhibit One in the -- Red Bluff Exhibit One -- that's the  
17 first hearing. I'm sorry I confused you. This --

18

19 (Thereupon a discussion was had off the record.)

20

21 MR. PADILLA; To clarify the  
22 record, that was Exhibit One at the division hearing, Red  
23 Bluff Exhibit Number One.

24 Q Would you point out to me on Exhibit  
25 Two, Red Bluff Exhibit Two, the language which gives you a

1 -- make that interest applicable to Red Bluff's acreage?

2 A You want me to read the whole thing or  
3 just --

4 Q No, just to point out.

5 A "If Bettis, et al, is successful in ac-  
6 quiring a farmout and/or leases in the AMI, Bettis --"

7 MR. BROSTUEN: What paragraph  
8 is that?

9 A That is paragraph 4. "-- Bettis, et al,  
10 shall retain a 2 percent of 8/8 override in any acreage  
11 having a 75 [percent] net revenue interest or less and a 5  
12 percent of 8/8 override in any acreage having a 77  
13 [percent] net revenue interest or greater."

14 You want me to continue reading?

15 Q Well, whatever -- whatever it says. If  
16 that's all it says, that's fine.

17 A "Worth shall pay 100 percent of all cost  
18 in securing said additional acreage. Said override shall  
19 apply to all rights acquired and shall not be limited to  
20 depth. Worth shall pay L. E. Oppermann \$200 per diem plus  
21 expenses to handle all landwork in the AMI. Said landwork  
22 shall include acquiring farmouts, purchasing leases, curing  
23 titles, ordering abstracts, and any other related work  
24 which Worth may require. Worth shall pay to Harry M.  
25 Bettis, Jr., \$200 per diem plus expenses to handle all

1 geologic work which Worth may require in the AMI. If Bettis  
2 et al shall acquire any additional acreage in the AMI,  
3 Worth shall have the right to acquire said acreage on the  
4 terms set out above. If Worth does not wish to acquire the  
5 acreage, Worth shall have ten days after -- after the  
6 acreage is presented to advise Bettis et al in writing that  
7 it does not wish to acquire the acreage. Bettis et al  
8 shall have the right to retain the acreage for its own  
9 account or assign the acreage to a third party."

10 Q Were you ever able to acquire a lease  
11 from Red Bluff?

12 A Who?

13 Q Red Bluff.

14 A No.

15 Q Now this letter was dated 19 -- February  
16 23rd, 1983.

17 A Yes, sir.

18 Q How many leases did you acquire under  
19 the terms of this agreement after 1983?

20 A I acquired a farmout from Gulf Oil  
21 Company, which is now Chevron.

22 I acquired a lease from Holly Energy,  
23 which is now Enron.

24 I acquired a farmout from Exxon.

25 I think that's the extent of it.

1 Q When were those acquired?

2 A They were acquired in '83, '84 and '85.

3 Q After '85 you didn't acquire any more?

4 A No, sir.

5 Q And I believe you've already testified

6 you weren't able to complete a deal with Mr. Hayes and Mr.

7 Fuller in the spring of 19 --

8 A Yes, sir.

9 Q Now, you're a qualified landman, Mr. Op-

10 permann. Do you have any idea as to the value of acreage

11 in this area?

12 A Are you talking about straight lease?

13 Q Yes.

14 A I would say probably between \$50 and

15 \$100.

16 Q And did you -- have you acquired leases

17 in this township other than by farmout?

18 A No. Yes, we bought a lease from Holly

19 Energy Company and I don't recall the price. That was back

20 in 1984 and the price of oil was \$28.00.

21 Q Do you remember what overrides or bur-

22 dens were placed on the other farmouts that you acquired

23 from various major companies that you mentioned?

24 A Yes. They were usually 75 percent. I

25 think the Gulf was 77 and back to 75 after payout.

1                   The Holly lease was 80-some percent, I  
2 think. I think that's right, 81, or something.

3                   Q           And all these -- you had to drill to  
4 earn them. They were all farmouts.

5                   A           Not the Holly lease.

6                   Q           Holly, that was not.

7                   A           Yes, sir, that was a straight --

8                   Q           And you don't remember the consideration  
9 for that?

10                  A           It was 200 acres. I think the consider-  
11 ation was -- I think somewhere around \$10,000, which would  
12 make it \$50 an acre, but I -- somewhere in that range.

13                  Q           Well, where was -- where was that lease?

14                  A           It was in the section to the north.

15                  Q           It have a short term?

16                  A           It had a short term.

17                  Q           And has it now since expired?

18                  A           No. It has four drilling wells -- four  
19 producing wells on it.

20                  Q           Those Mallon wells?

21                  A           Those are other wells.

22                  Q           Mallon didn't take that lease, that  
23 acreage.

24                  A           Well, Worth petroleum did. This was be-  
25 fore Mallon acquired Worth or their position in the acre-

1 age.

2 Q Well, what is a customary burden (not  
3 clearly understood) the customary net revenue interest (not  
4 understood) --

5 MR. PADILLA: For what area?

6 A I don't understand the question.

7 Q Well, what -- what -- on a farmout what  
8 in this area, what do you generally -- what net revenue  
9 interest do you generally earn?

10 A Generally, at that time, when the price  
11 of oil was \$28.00, I'd say it was 75. Now I don't think  
12 anybody would drill it unless it's about 78 to 80.

13 Q And if Mallon in this deal would get 81  
14 percent net revenue interest it would be a good deal in  
15 your opinion, wouldn't it?

16 A Well, in my opinion if they would take  
17 that it would be a 76, it wouldn't be 81, because my part-  
18 ner and myself would be then entitled to a 5 percent over-  
19 ride.

20 Q Even if they assign it.

21 A Right.

22 Q So that makes this lease uneconomic, I  
23 guess, the lease that was issued later, long since later,  
24 to Red Bluff.

25 A I don't think I'm qualified to say it's

1 uneconomical or not.

2 MR. JENNINGS: I believe  
3 that's all.

4 MR. PADILLA: I have no  
5 further questions, Mr. Chairman.

6 MR. JENNINGS: Oh, let me -- I  
7 forgot to offer -- I will offer Red Bluff Exhibit Two and  
8 once again I don't have any copies, but it's a letter dated  
9 February 23.

10 MR. BROSTUEN: Without objec-  
11 tion it will be admitted.

12 Mr. Padilla.

13 MR. PADILLA: I would like to  
14 all Mr. Cox at this time.

15 MR. BROSTUEN: Okay, if there  
16 are no -- are there any further questions of Mr. -- I  
17 thought you were going to redirect, I'm sorry. Any further  
18 questions?

19 If not, he'll be excused.

20 Mr. Padilla?

21 MR. PADILLA: Yes, sir.

22 MR. BROSTUEN: How long do you  
23 think we're going to be --

24 MR. PADILLA: Well, judging  
25 from the -- I think we'll be probably an hour, to be safe.

1 MR. BROSTUEN: We have a  
2 problem, at quarter to Mr. Humphries has to leave and we  
3 require a quorum for the hearing. What is your pleasure?  
4 Do you want to continue after lunch? Take a break till  
5 1:30? We could perhaps take a recess at this time and  
6 perhaps have a long, leisurely lunch.

7 MR. PADILLA: I'm just advised  
8 that they all have planes at 2:20 but I think if Mr. Oppermann  
9 is excused he can leave at this point.

10 MR. BROSTUEN: Do you have any  
11 other questions, Mr. Jennings, recalling Mr. Oppermann?

12  
13 (There followed a discussion off the record and the noon  
14 recess was taken.)

15  
16 MR. BROSTUEN: We'll get this  
17 hearing back to order here.

18 MR. PADILLA: Mr. Chairman,  
19 I'll call Joe Cox at this time.

20  
21 JOE H. COX, JR.,  
22 being called as a witness and being duly sworn upon his  
23 oath, testified as follows, to-wit:

24  
25

## DIRECT EXAMINATION

1  
2 BY MR. PADILLA:

3 Q Mr. Cox, for the record would you please  
4 state your name and by whom you're employed?

5 A Yes. My name is Joe H. Cox, Jr., and I'm  
6 with Mallon Oil Company.

7 Q What are your duties as -- for Mallon?

8 A I'm an engineer and I do engineering  
9 work and development geology work.

10 Q Have you previously been qualified as a  
11 geologist and as an engineer before the Division?

12 A Yes.

13 MR. PADILLA: We're going to  
14 stipulate his qualifications, Mr. Chairman.

15 MR. JENNINGS: (Unclear).

16 MR. BROSTUEN: Nevertheless, I  
17 will accept the qualifications, Mr. Jennings.

18 MR. PADILLA; As a geologist  
19 and an engineer.

20 MR. BROSTUEN: As a geologist  
21 and an engineer.

22 Q Mr. Cox, what has been your involvement  
23 in trying to make a deal with Red Bluff in this case?

24 A Well, I got involved with this when a --  
25 oh, I guess it was back in early part of '88 when we were

1 negotiating with them, trying to help explain our economic  
2 situation in drilling wells out there to Mr. Hayes and Mr.  
3 --

4 Q I'd like for you to refer to Exhibit  
5 Eight, which we have marked, and have you tell the Commis-  
6 sion what that is and what it contains.

7 A It's a collection of letters, corres-  
8 pondence between myself and John Hayes, some of which were  
9 carbons to Mr. Jennings, I believe.

10 Q What do they say?

11 A The first ones were -- we sent an AFE  
12 (not clearly understood) this was after we negotiated for  
13 some time and decided that forced pooling was the only al-  
14 ternative.

15 Q Was the AFE signed?

16 A No, they did not respond to that.

17 Q Is that AFE reasonable for that area?

18 A It -- it's with our actual costs on it.

19 Q Have the drilling costs changed in any  
20 way from then to now?

21 A There hasn't been any substantial change  
22 in any of the costs, no.

23 Q Are the figures on that AFE still valid?

24 A Yes.

25 Q And reasonable?



1 that by starting from the section corner which is described  
2 in the survey and forcing closure with what they describe  
3 in our papers as limits.

4 Q Did you ask the Bureau of Land Manage-  
5 ment as to the reasonableness of the second plat?

6 A Yes. In a letter received from them  
7 that, well, in confirmed our position and in this letter  
8 they said this is probably the best approach to solving it,  
9 since they'd have to stay with their original reserve esti-  
10 mate.

11 Q And is that in the form of Exhibit  
12 Eleven?

13 A Yes. It's a letter John Gumert of the  
14 BLM.

15 Q Now what are exhibits -- what is Exhibit  
16 Ten?

17 A Okay, it's a letter to the BLM request-  
18 ing their assessment of this plat.

19 Q And does the BLM letter indicate that  
20 the second plat is reasonably accurate for purposes of  
21 pooling?

22 A Yes, Gumert states that in his letter.

23 Q Do you have anything further concerning  
24 Exhibits Nine, Ten and Eleven?

25 A I don't believe so. The problem

1 basically is something that, according to the BLM, could  
2 not be resolved in any other way than some form of reason-  
3 able agreement such as this.

4 They would not re-survey it, in other  
5 words.

6 Q Let's go on now to what we have marked  
7 as Exhibit Number Twelve and have you identify that for the  
8 Commission, please.

9 A Yes. This is just a xeroxed shot of a  
10 topographic map, USGS base, with the Amoco Federal Lease  
11 outlined in orange, excluding the -- the 40-acre tract  
12 there in Section 27 and the 120 acres down in the lower  
13 Part of Section 27, and excluding the Red Bluff right-of-  
14 way acreage.

15 Q The only acreage you don't control is  
16 that 40-acre tract and the Red Bluff property shown on this  
17 labeled Red Bluff Reservoir, is that correct?

18 A That's right.

19 Q And I notice there are some other num-  
20 bers in there. Are those the wells that are operated by  
21 Mallon on the righthand side of that within the orange?

22 A That's correct, those are Mallon oper-  
23 ated wells.

24 Q Okay.

25 A I might add that the pink outline is the

1 Red Bluff outline, the acreage was originally surveyed on  
2 an elevation datum that was -- it will not be the spillway  
3 elevation on the dam (unclear).

4 Q And is that a metes and bounds descrip-  
5 tion?

6 A Right, that's that metes and bounds 1938  
7 survey.

8 Q Let's go on to what we have marked as  
9 Exhibit Number Thirteen.

10 A Okay, this is just some support data for  
11 the lease operating expenses we used in the -- in the  
12 economic assessment of a typical well drilled on a lease,  
13 and that leaves about \$2200 a month (not clearly under-  
14 stood) and that works out with this group of wells that was  
15 in this exhibit.

16 Q What -- what does this show in relation  
17 to the drilling of the proposed well?

18 A Well, it just -- in arriving at econo-  
19 ics that we calculate for a well, it gives us a basis for  
20 what we can expect to spend to operate that well after we  
21 complete it, and the numbers that go into this sheet are  
22 actual expenditures from the wells.

23 Q Where is the bottom line of this exhi-  
24 bit, let me -- let me ask that question?

25 A Well, each -- each well has its own

1 figure. There's a line lefthand title there that says  
2 "Total Operating Expenses" and then they have the respec-  
3 tive months and a 6-month total and a year to date total,  
4 and averaging the months is where we came up with our \$2200  
5 a month cost.

6 Q Now, then looking at -- does each page,  
7 does each page apply to a different well?

8 A Yes. I think this covers all wells  
9 in the lease.

10 Q Okay, the bottom line is your profit, I  
11 take it, is that what that is?

12 A Yes. It's not -- that is not a very  
13 accurate figure because it doesn't take the royalties into  
14 account, so it's -- you'd have to go back in there and down  
15 for royalties paid.

16 Q And this is merely an expense itemiza-  
17 tion, is that correct?

18 A Right, it's just an amortization of ex-  
19 penses for the, but the useful information is really in the  
20 lease operating expenses part.

21 Q Let me take that bottom figure on the  
22 first page of 1499.29 and there's a minus sign after that.  
23 What does that mean?

24 A What page?

25 Q On the first page.

1           A           Okay, that's for the month of January.  
2 Well, I think that month we must have done some work. In  
3 fact there was a refrac done on that well, so that's not a  
4 very representative number but it does show that we lost  
5 \$15,000 on it, on the well that month.

6           Q           Is that in hundreds, Mr. --

7           A           \$1500, excuse me.

8           Q           \$1500. In March you also lost money on  
9 that well, is that correct?

10          A           That's correct, and that was a more typ-  
11 ical operating month.

12          Q           In February you made \$73.79?

13          A           Right. Again, these bottom line figures  
14 are 8/8ths revenue figures, so they're not -- we're not  
15 taking out the 30 percent royalty burden on these leases.  
16 That bottom line is not a very useful number.

17          Q           If we go through the rest of the exhibit  
18 and look at the bottom line, you get to see what kind of  
19 money you're making, is that correct, without considering  
20 the royalty burden on the lease?

21          A           That's correct.

22          Q           Mr. Cox, which is the best well that you  
23 have in the area? Why don't you tell us which is the best  
24 and which is the worst well that you have?

25          A           Well, right now probably No. 13 or No. 5

1 would be the best. No. 5 is in kind of sweet spot in the  
2 lease and it's been -- it's got the highest cum, projected  
3 to be the highest cum well, and the 13 is one -- is one of  
4 the newer wells and it's still relatively early in its  
5 decline, so it's showing a little higher revenue, too. In  
6 fact it was quite a bit higher.

7 Q Mr. Cox, in your opinion are these wells  
8 making a lot of money?

9 A Not -- not really. As far as the daily  
10 operating revenue they're operating profitably, but as far  
11 as the drilling wells, it's a -- pretty much of a break  
12 even situation on the last four wells we've drilled.

13 Q What's the average payout for these  
14 wells, for the wells that you have drilled out there?

15 A Well, --

16 Q The length of time?

17 A Oh, I imagine, of the wells that do pay  
18 out, they probably are paying out in about five years.  
19 Some of the wells that we've drilled will not pay out, how-  
20 ever.

21 Q Let's go on to Exhibit Number Fourteen  
22 and tell us what that is.

23 A Okay, this is just a group of the drill-  
24 ing and completion cost records from the last four or five  
25 wells drilled out there. I guess there's three wells, four

1 wells.

2 Q Does this exhibit support the data con-  
3 tained in your AFE?

4 A Yeah. The -- out of these wells, the  
5 No. 14, the first well listed, the second page of the exhi-  
6 bit shows its cumulative cost at \$352,682. That well was  
7 drilled to 6200 feet, as was No. 11, which is not included  
8 in there. So of the four wells group 14 is the only one  
9 that went as deep as the Amoco Federal -- Red Bluff Federal  
10 No. 1 is supposed to go, and it also included the building  
11 of a tank battery we're going to have to -- we're going to  
12 need for that well, so it's the most closely representa-  
13 tive.

14 Q Do you have anything further concerning  
15 Exhibit Fourteen, Mr. Cox?

16 A I believe so. It shows that we've  
17 brought the drilling costs down a little bit from previous  
18 operators wells.

19 Q Mr. Cox, let's go on now to Exhibit Num-  
20 ber Fifteen and have you identify that for the Commission  
21 and tell us what that is.

22 A Okay, this is the economics done on the  
23 -- using Michael Smith and Associates profit program. It's  
24 just using certain parameters for economic assumptions. It  
25 is a projection of economic life of the typical well out

1 there, and we input the same decline curve for both wells  
2 and the different royalty rates in the two different cases.

3 Q What -- what's the value of oil that you  
4 used in this exhibit?

5 A We used a flat \$15.00 a barrel price.

6 Q Why did you use \$15.00 per barrel?

7 A It's just based on about what the aver-  
8 age has been for the last two years, and the same with gas,  
9 about the average price for gas down there.

10 Q Mr. Cox, you used this same exhibit at  
11 -- during your testimony in October at the first hearing.  
12 Has the price of oil changed to an extent to where you  
13 would consider changing the \$15.00 per barrel price?

14 A Well, actually since this time there are  
15 a couple of changes. There was a downturned price and now  
16 there's been an upturned price. Those are fairly short  
17 term fluctuations and so until there's some basis to think  
18 otherwise, I'm inclined to stay with this pricing.

19 Q Mr. Cox, Mr. Jennings this morning re-  
20 ferred to the price of oil being at \$18.00 per barrel cur-  
21 rently. What's your opinion with regard to using the  
22 \$18.00 per barrel -- \$18.00 per barrel current price?

23 A I think for a prudent business decision  
24 that would be probably wholly optimistic. We've reached an  
25 \$18.00 oil within the last couple years but it hasn't

1 stayed there for very long, so it's -- I guess in the in-  
2 terest of conservatism \$15.00 seems like a lot more reas-  
3 onable number to me.

4 Q Is there any indication that you have  
5 with regard to whether or not this price of oil is going to  
6 remain at \$18.00 per barrel?

7 A I think that's always a question we ask  
8 on writing these things, but I would say that there is no  
9 new developments in the world oil market that make us think  
10 that it is bound to stay there.

11 Q Are you familiar with any -- anything in  
12 the futures market that would indicate that possibly your  
13 \$15.00 per barrel would be more accurate?

14 A Well, this \$19.40 (unclear) price for  
15 February was followed by decreasing prices for March,  
16 April, May, which indicates that the prudent speculators  
17 don't feel like the price is going to hold up.

18 That is probably as good an indication  
19 as any, what the consensus is.

20 Q Mr. Cox, at this point I'd like for you  
21 to explain this Exhibit Number Fifteen to the Commission in  
22 terms of the profitability of the proposed well.

23 A Okay. Well, the first sheet presents a  
24 70 percent net revenue interest on the Amoco Federal Lease  
25 and it's using \$15.00 flat pricing, the lease operating ex-

1 penses coming from the history, and then everything else is  
2 pretty much given. That shows with the actual drilling and  
3 completion expenses of \$315,000 that that well would not  
4 pay out. It would be -- on a discounted basis it would be  
5 \$13,000 short of pay out.

6 Q What's on the second page of that exhi-  
7 bit?

8 A That's just the input parameters for --  
9 for the -- it gives the decline rate, gas/oil ratio, and  
10 price of oil and severance tax, and what not.

11 Q Is the decline rate based upon the ex-  
12 perience in the other wells in the field?

13 A That and particularly the western wells  
14 in the field.

15 Q Okay, let's go on now to the third page  
16 and have you tell us what that is.

17 A Okay, this is a -- at the time I ran  
18 these we were looking into finding relief from excess roy-  
19 alty burden. That would have been anything above and be-  
20 yond the original reservoir's burden in the Federal royalty  
21 82 percent, 82.5 percent, and everything else is the same  
22 except for the royalty and it does give us a profitable  
23 situation and we've since learned that that's probably not  
24 feasible for us to get relief from those burdens at the  
25 present time.

1 Q Why is that?

2 A What we have is the legal exposure to us  
3 of being sued by the present royalty owners is just too  
4 great to take the risk, and we weren't sure after we inves-  
5 tigated that we really had the basis for filing.

6 Q Is that because the production exceeds  
7 15 barrels per day?

8 A Yeah, that's a big part of it. That was  
9 -- I remember mentioning some of the earlier assignments by  
10 the Federal government a 15 barrel a day limit below which  
11 you -- you get relief from any lease that's not averaging  
12 less than 15 barrels a day, so that (not clearly under-  
13 stood.)

14 Q What would be the profit on this second  
15 work sheet that you would make from this well?

16 A Discounted 15 percent it's for \$65,000.

17 Q Over how long a period of time?

18 A Producing a well three months into the  
19 year 2000, so it would be 12-1/2 years -- 11-1/2 years.

20 Q Mr. Cox, let me refer you now to Exhi-  
21 bit -- is that all you have on Exhibit Number Fifteen?

22 A Yeah.

23 Q Let's go on to Exhibit Number Sixteen,  
24 please, and have you identify that exhibit.

25 A Okay, this is an iso-cumulative plot of

1 the actual barrels of oil per day from the wells across the  
2 Brushy Draw Field from the Williamson Sand, and which is  
3 the primary field pay. There isn't any other commercial  
4 pays found under it and it shows that around the northeast  
5 corner of Section 27 and northwest corner of Section 26,  
6 that area is an area of better production and decreasing in  
7 cumulative production westward and eastward.

8 Q Where is the proposed location on this  
9 exhibit?

10 A It's labeled as No. 12. It's in the  
11 northwest of the southwest of Section 27.

12 Q What does the number 12 indicate on this  
13 for the proposed well?

14 A Well, at the time, this was through  
15 December, '87, it showed that it would project to, had been  
16 producing at that time at around 10,000 barrels of cumula-  
17 tive production.

18 Q Will that pay out the well?

19 A No. Of course I might add that that's  
20 not a projected cumulative, our projected ultimate reserves  
21 in the well, but it projected additionally that these re-  
22 serves also declined in that direction, so we are in the  
23 marginal are for payout in that area.

24 Q Mr. Cox, let me show you what we have  
25 marked as Exhibit Number Seven that has been exhibited in

1 the prior hearing. We don't have this exhibit but it would  
2 be Number Seven, and just -- we don't want to introduce it  
3 at this point, since it's already part of the record, but  
4 can you briefly tell the Commission what -- what the geolo-  
5 gic characteristics are as we move towards your proposed  
6 location from east to west?

7 A Okay. This just shows moving from east  
8 to west from the Amoco No. 4 Well across to the Amoco 13  
9 Well, a general thinning of the Williamson Sand, which is  
10 recorded by orange there.

11 Q Is the Williamson Sand the proposed pro-  
12 ductive interval?

13 A Yes.

14 Q Mr. Cox, do you have a recommendation to  
15 the Commission as to what the penalty for risk factor  
16 should be in this case?

17 A Well, every time in the last three or  
18 four wells we drilled out there it's really been a decision  
19 whether we can justify drilling the wells or not, so I  
20 think that the maximum penalty for nonconsent is very just-  
21 ifiable. We're drilling -- we're drilling now to hold the  
22 farmout.

23 MR. PADILLA: Mr. Chairman, I  
24 believe that's all I have of this witness.

25 We'd offer Exhibits Eight

1 through Sixteen.

2 MR. BROSTUEN: Without ob-  
3 jection, they'll be accepted.

4 Mr. Jennings?

5

6

CROSS EXAMINATION

7

BY MR. JENNINGS:

8

Q Mr. Cox, what did you say the average  
9 life of these wells was?

10

11

A Well, I think it's probably around --  
again it would depend on the well, but I suppose the aver-  
12 age life would be around ten years.

13

14

15

16

17

Q And then as I -- I read this, your ex-  
hibit here, I believe it's Number 14, based on your pro-  
jected payout, you drill that well, this is the well you  
propose to drill and you estimate you'd lose \$13,000, is  
that right?

18

A Discounted 15 percent.

19

20

21

Q Well, how can you justify drilling a  
well that already has less than -- has that kind of a  
chance of recovering?

22

23

24

25

A That's a good question and we always  
kind of financially agonize over that decision, whether we  
want to go ahead and drill another well in the farmout or  
whether we should let it go, but we have drilled one well

1 recently that looks like it's a fairly good payout posi-  
2 tion, the No. 13 Well, and done some mapping based on its  
3 reserves and are hoping to find better reserves. In gen-  
4 eral those around it have decreasing porosity and decreas-  
5 ing pay sections.

6 Q Well, why do you contemplate another  
7 well in Section 28 if that's where section -- if that's  
8 where the 13 Well is?

9 A Right, it would be south offset to the  
10 13, hoping to find that same improved porosity, same poro-  
11 sity section that was encountered in that well.

12 Q Now, if you were to acquire the Red  
13 Bluff lease and have a 81 percent working interest under  
14 that 10 acres, 9 acres, whatever it is, wouldn't that ac-  
15 tually change and make your -- your deal a whole lot  
16 sweeter, a better deal 10 acres, 9 acres, wouldn't that  
17 substantially change this and make your deal a whole lot  
18 sweeter, better deal (unclear) a 12th of that?

19 A I haven't figured on 81. I figure on  
20 86, that's approximately 25 percent of the standard spacing  
21 on 86 percent (unclear) and the rest at 70 percent; comes  
22 out to about 74 percent net for that drainage spacing, and  
23 it would certainly improve the economics but it would put  
24 it somewhere closer to the -- to the 70 percent case here  
25 than the 82-1/2 percent case, and we'd still be looking at

1 a high risk situation from Mallon.

2 Q Well, but it would be better for Mallon,  
3 wouldn't it? I can't understand why it wouldn't be better  
4 for Mallon. Can you tell me that?

5 A Better for Mallon than what?

6 Q Than having (unclear) in there with a 70  
7 percent.

8 A Well, it's better, as far as the 70 per-  
9 cent area interest wells, the wells on a -- completely on  
10 the Amoco acreage, we've really run out of reasonable pros-  
11 pects.

12 Q Well, if you can get this other acreage  
13 either by force pooling or by assignment from Mallon,  
14 wouldn't it improve your recovery and wouldn't it sweeten  
15 up the deal?

16 A Well, as was mentioned earlier today,  
17 the deal that was made in 1983 was substantially different  
18 well pricing period, and if we had the same deal offered to  
19 us today, there's no doubt we would not take it.

20 Q Do you get many farmouts generally when  
21 you get as much as an 81 percent net revenue interest?

22 A This is the only Delaware production  
23 that Mallon operates. I really can't compare apples and  
24 apples on that.

25 Q Well, I guess you'd recommend this to

1 your management notwithstanding it looks like (not under-  
2 stood.)

3 A Well, based on our -- our Well No. 13,  
4 my recommendation is that if we can pursue similar wells as  
5 we're drilling, if we drill the sand a lot higher, the map  
6 doesn't fit the proposed channel trends, I imagine we're  
7 going to have to take a serious look at whether we'll con-  
8 tinue drilling there or not.

9 Q Well, you have one other well. You have  
10 this one you proposed, you have 70 percent interest in that  
11 14 Well, looks like --

12 A 14 has been drilled. It's on the -- in  
13 Section 28 in the southeast quarter and it was a tight well  
14 that is projected to not pay out.

15 Q But that is across the -- across the  
16 reservoir.

17 A Right.

18 Q Do you contemplate another well at this  
19 time, I don't know what number it might be, in the section  
20 northeast of 13?

21 A Southeast of 13 we have.

22 Q I see.

23 A (Unclear) prepared work on that is  
24 because of the surface situation there where we're ap-  
25 proaching Red Bluff Reservoir on the sloping topography the

1 BLM is concerned about the drill site. It will take longer  
2 than our 90 days, probably, to get to -- or most of our 90  
3 days to get a drill site approved by them.

4 Q Well, are you familiar with what has  
5 been offered as Red Bluff Exhibit Number Two, which is the  
6 letter of February 23, the area of mutual interest deal?

7 A Yeah, I've heard it discussed in the  
8 hearing here. I haven't --

9 Q You haven't read it?

10 A I don't know if I have or not. Not  
11 being in the land department I really don't have too much  
12 to do with it.

13 Q Well, it contains this language and I  
14 wish you'd explain it to me, explain to me why you are  
15 paying 5 percent overriding royalty (not understandable).  
16 This is paragraph 4 of this exhibit, it says: "If Bettis  
17 is successful in acquiring farmouts or leases in the AMI,  
18 Bettis shall retain a 2 percent of 8/8ths overriding  
19 royalty in any acreage having a 75 percent net revenue in-  
20 terest or less..."

21 A What is the date on that?

22 Q February 23rd, 1983.

23 A Okay, I think that would probably be a  
24 -- the reason that something like that would be acceptable  
25 to the parties at the time was the economic climate for oil

1 and gas was a lot different than it is now.

2 Q Well, my question to you is why, when  
3 this -- when one gets together 25 percent interest under  
4 this, gives you a 75 percent working interest, why are you  
5 paying 2 -- why are you not paying 2 percent instead of 5  
6 percent?

7 A I wasn't even employed by the company  
8 when that was negotiated so I really am not qualified to  
9 tell you why it is like that.

10 Q Well, apparently the company is still  
11 making that payment.

12 A We're honoring an agreement we made.

13 Q Well, if someone here could explain to  
14 me why that under Exhibit Number Five, Mallon's exhibit  
15 shows that the total override for both (unclear) are 70 --  
16 30 -- 30 percent results in you getting 70 percent, and  
17 when you take that (unclear) that Bettis is doing, you've  
18 only got a -- Bettis (not understandable) is 75 percent  
19 working interest.

20 MR. PADILLA: Mr. Chairman,  
21 I'm -- I think the document speaks for itself and I'm not  
22 sure that -- that I read that the same way that Mr.  
23 Jennings does.

24 This witness has basically  
25 said he does -- really isn't familiar with this document.

1 And we're just not getting closer to a decision.

2 MR. BROSTUEN: I think we can  
3 go on to something else, Mr. Jennings. The witness is not  
4 familiar with the document and you may proceed with addi-  
5 tional questions that you may have.

6 MR. JENNINGS: I can't under-  
7 stand it. That's all.

8 Q Now I believe that you in one of your  
9 last letters, I believe it was your September 6th letter,  
10 you at that time wanted to proceed on obtaining a farmout  
11 from Red Bluff.

12 MR. PADILLA: Is that Exhibit  
13 Eight, Mr. Jennings?

14 MR. JENNINGS: Yes.

15 A Right. These negotiations went on and  
16 on and I was involved, as I mentioned before, to the extent  
17 I'm trying to -- to inform the Red Bluff people why we  
18 thought we had a limit on what we could accept for over-  
19 riding royalty burden on your lease, even though it was a  
20 lower burden than we had on the Amoco lease at the time,  
21 and we were encouraged from time to time during the discus-  
22 sions with Mr. Hayes, and with you, too, as I recall, that  
23 there was really hope for reaching an agreement. I think  
24 that's what this letter was working toward.

25 Q Have you ever made any effort to reach

1 an agreement since that time, to your knowledge?

2 A Oh, we've talked with -- I don't have a  
3 chronology of all the discussions we've had. I know as of  
4 this time it was considerably well into the period that  
5 we'd been negotiating it, we made this offer. I'm not sure  
6 (not clearly understood).

7 Q To your knowledge, then, no additional  
8 efforts have been made to make some kind of a treaty or  
9 obtain a farmout other than this (unclear).

10 A Probably from this point on Karen was  
11 more involved with negotiations than I was. I'm not really  
12 aware of them.

13 Q Do you have any idea how long it would  
14 take this lease to pay out in the event that it was force  
15 pooled and you got the maximum 200 percent?

16 A Plus cost. I would, and I told Mr.  
17 Hayes this on the phone well back in our discussions, I  
18 said I doubt that this will reach sufficient payout for Red  
19 Bluff to back into the well based on the performance of  
20 surrounding wells.

21 Q And what I'm saying, what I understand  
22 you to say, is that if the Commission should elect to force  
23 pool this acreage and put the 200 percent penalty on it,  
24 then Red Bluff would never receive anything for their  
25 acreage.

1           A           Under that assumption that would not  
2 reach that point, that's true. Of course it also points to  
3 the substantial risk that Mallon's taking in drilling it,  
4 which is the reason for (unclear) in the first place.

5           Q           Now, I assume that the Red Bluff acreage  
6 would pay out more -- much sooner than the other acreage,  
7 would it not?

8           A           If Red Bluff were to go in there and  
9 drill a well on --

10          Q           No, no, no, under the -- either if it's  
11 force pooled or they'd make an assignment, you will recover  
12 -- you will get the money back from that 10 acres a lot  
13 sooner than you will on the other 30, it's a possibility.

14          A           Not a lot sooner. I think, as I stated,  
15 that forced scenario is about 74 percent net to the working  
16 interest partners in the Amoco lease, or the participants  
17 in the well, I should say, and which would accelerate the  
18 payout, but it's not tremendously different (unclear).

19          Q           I don't understand how it's 74 percent  
20 return on investment -- 74 percent of --

21          A           74 percent net revenue interest, which  
22 would be what we (unclear) under this -- this particular  
23 40-acre drill site to the 100 percent working interest.

24          Q           You mean you would pick up 4 percent net  
25 revenue interest by force pooling, is that what you're

1 saying?

2 A That's correct.

3 Q And you pick up, if you don't force pool  
4 it, what would you pick up? Assuming the 5 percent over-  
5 riding royalty, that's 19 percent. The difference between  
6 19 and 30 is quite a bit.

7 A Yeah, I'd have to calculate that out;  
8 whatever proportion, it may be somewhat less than 74 per-  
9 cent.

10 Q It would be less than 74? It would be  
11 more than 74 percent.

12 A No, it would be less. This -- the 74  
13 percent is calculated on 25 percent of the gross spacing  
14 having a 86 percent net revenue interest and 75 percent of  
15 the gross spacing having a 70 percent (unclear) so if -- if  
16 you had to cut 5 percent off that 25 percent portion, then  
17 that would be about 73 percent net revenue interest.

18 Q Okay, but you're -- you're increasing  
19 the net revenue interest either way, whether you assign it  
20 or you get force pooled, is that right?

21 A That's true, over -- over the Amoco  
22 lease, you're saying?

23 Q Yes.

24 A That's correct.

25 Q And as I understood your testimony this

1 morning, if this is force pooled, then you will be better  
2 off, tell me if this is your understanding, because you  
3 won't have to pay Oppermann anything, is that correct?  
4 You'll be much better off because he won't get 5 percent on  
5 that.

6 A On that 25 percent of the (unclear).

7 Q So then you won't have anything on that  
8 and the only burden on that will be the 14 percent that the  
9 government gets, that will be a substantial savings.

10 MR. PADILLA: Mr. Chairman, I  
11 believe I'm going to object at this point because I believe  
12 Mr. Oppermann's testimony was that if a lease was obtained  
13 by him, either -- or -- or by Mallon, Oppermann would get 5  
14 percent; it doesn't matter who gets the lease from Red  
15 Bluff, Oppermann and Bettis would (unclear) at getting 5  
16 percent, or a total of 10 percent. That would make the  
17 lease worth -- there'd be another 10 percent royalty on  
18 this, what it really comes out to, over and above the 14  
19 percent.

20 MR. BROSTUEN: Mr. Padilla,  
21 are you saying that -- that Mr. Oppermann would participate  
22 if the well was forced pooled or if it were acquired by a  
23 farmout or --

24 MR. PADILLA: No, we're not  
25 saying that. We're saying simply that consistent with Mr.

1 Cox' testimony, that we would wind up with a lease of 86  
2 percent net revenue interest should the forced pooling  
3 occur, up until the time that Red Bluff would back in after  
4 the penalty is paid out.

5 But should a deal be made with  
6 Red Bluff for 5 percent or whatever the percent is, that  
7 the Oppermann would automatically participate with his 5  
8 percent. That has been one of the considerations and I  
9 think that was Mr. Oppermann's testimony this morning, that  
10 he would have that additional 10 percent whether or not a  
11 deal was made or not at this point.

12 Our testimony has been that  
13 that is not available any more, that we're here in a forced  
14 pooling hearing. I don't know where Mr. Jennings is going  
15 as far as this 5 percent, as to whether it's reasonable or  
16 not, we've certainly heard enough testimony concerning that  
17 from his side.

18 MR. BROSTUEN: I think that as  
19 far as this hearing is concerned, the overrides in this  
20 matter are of really no concern to this case as far as the  
21 Commission is concerned. This is something that is going  
22 to be between, probably between operators, and it simply  
23 isn't germane to the determination of this case.

24 We are here to determine  
25 whether or not the tract should be pooled, that the statute

1 was complied with insofar as efforts to -- to -- to reach a  
2 negotiation, negotiate a settlement, and if it's not been  
3 possible to do so, we see we have the -- Mallon, I think,  
4 has a deadline insofar as a drilling rig, as far as the  
5 expiration of a lease is concerned, that -- that determin-  
6 ation we have to make, not really regarding the royalty  
7 rights. I guess I'm not able to see the importance of this  
8 discussion.

9 MR. JENNINGS: Well, I think  
10 it's -- I think it's the policy of the Commission that  
11 people will make a reasonable effort through bargaining and  
12 not the policy to allow somebody to be force pooled for  
13 their benefit, (unclear) everybody would get the opportun-  
14 ity to get their fair share, and I think that it's very  
15 important because there's no reason for Mallon to negotiate  
16 and put Mr. Oppermann in for a 5 percent override, and if  
17 you will read that deal, I don't think that covers a 5 per-  
18 cent override in a situation such as this. Perhaps that's  
19 the reason for showing the Commission just what the deal  
20 is.

21 MR. BROSTUEN: I think we have  
22 to determine at this time that the testimony is getting  
23 cumulative and repetitive and I think we're plowing the  
24 same old ground. I think at this point in time we should  
25 move on to -- to other questions.

1 MR. JENNINGS: I have nothing  
2 further of this witness.

3 MR. BROSTUEN: Are there any  
4 other questions of the witness?

5

6 QUESTIONS BY MR. BROSTUEN:

7 Q Mr. Cox, I have one question. Referring  
8 to your cumulative production isopach, you're showing pro-  
9 duction through December, 1987, and that is from the ini-  
10 tial producing data in any of these wells.

11 A That's correct.

12 Q And some of them have been in production  
13 for how long? What is the --

14 A Since, I imagine over on the -- in  
15 Section 26, that is probably late '82 and then '83 on for  
16 the rest of them.

17 Q So what we're seeing here is not the  
18 capability of the wells to produce but rather just the  
19 cumulative production of those wells.

20 A Right. They're somewhat misleading  
21 without having the dates of the wells on here, but the ini-  
22 tial flush production from these wells accounts for a large  
23 portion of their ultimate reserves and I think that the --  
24 if we checked ultimate reserves on these wells it would  
25 have a similar shape to it.

1 Q Thank you very much.

2 MR. BROSTUEN: Are there any  
3 other questions of the witness?

4 MR. PADILLA: I have nothing.

5 MR. BROSTUEN: He may be ex-  
6 cused.

7 Is there any further testimony  
8 in this case? Or any reason for recall? Mr. Jennings, I  
9 believe you have an exhibit here which has not been intro-  
10 duced as yet. Did you want to introduce this exhibit?

11 MR. JENNINGS: Yes, I -- as I  
12 stated, I do not have any witnesses here but I do have an  
13 exhibit that I tendered before (not clearly audible).

14 MR. BROSTUEN: I think that  
15 here again we're getting repetitive in this case, Mr.  
16 Jennings. I think that not much point would be served by  
17 that.

18 MR. JENNINGS: By considering  
19 this exhibit?

20 MR. BROSTUEN: If you -- you  
21 want to submit this exhibit?

22 MR. JENNINGS: Yes, sir,  
23 that's what I said, I want to.

24 MR. BROSTUEN: Very well, you  
25 made do that and (not clearly understood).

1 MR. JENNINGS: Well, if that's  
2 what the Commission wants, I will.

3 MR. PADILLA: Mr. Chairman, if  
4 he's going to introduce it as a part of -- well, my objec-  
5 tion still stands. With regards to if Mr. Jennings wants  
6 to take the stand, I can't really object to his introduc-  
7 tions. Presumably if he's going to (unclear) some other  
8 witness might have said, then I believe we would then look  
9 at the weight of the evidence as to whether his assessment  
10 is more correct than Ms. McClintock's.

11 I will cross examine him (not  
12 clearly audible) --

13 MR. JENNINGS: (Not clearly  
14 understood), I'll be glad to offer myself as a witness and  
15 be sworn for the offer.

16 MR. BROSTUEN: Okay, we will  
17 have you -- have Mr. Stovall administer the oath.

18 MR. STOVALL: Let me, if I  
19 may, Mr. Chairman, may we go off the record for just a  
20 moment and just --

21

22 (Thereupon a discussion was had off the record.)

23

24

(Witness sworn.)

25

1 JAMES T. JENNINGS,

2 being duly sworn upon his oath, testified as follows, to-  
3 wit:

4  
5 DIRECT TESTIMONY BY MR. JENNINGS

6  
7 MR. JENNINGS: I haven't been  
8 in this position very many times but this document which  
9 has been marked Red Bluff's Exhibit One and which is before  
10 each of you consists of a memorandum on yellow paper taken  
11 from my office file in connection with the Red Bluff nego-  
12 tiation with Mallon.

13 And the first memorandum is  
14 dated April -- or, I'm sorry, August 20, 1987, has been in  
15 my files and that's two pages and there are some handwrit-  
16 ten notes about other conversations in 1987 with Karen  
17 McClintock and they are on the page two.

18 And the other document, which  
19 is dated September 21, 1987, is also a memorandum to, mark-  
20 ed, so marked, to Red Bluff file. I initialed it and this  
21 is concerning my later confirmation -- or conversation with  
22 Ms. McClintock in September, 1987, concerning the negotia-  
23 tions and issues in the lease and things like that.

24 MR. STOVALL: Do you have any-  
25 thing further with respect to this exhibit?

1 MR. JENNINGS: No, sir.

2  
3 QUESTIONS BY MR. STOVALL:

4 Q A Are you going to move it -- I  
5 guess I'll play the advocate for you for a moment.

6 Are you going to move it's admission?

7 A I've already --

8 Q Well, you're now doing it again as an --

9 A We'll again move the -- I'll again move  
10 its admission.

11  
12 QUESTIONS BY MR. PADILLA:

13 Q Mr. Jennings, I notice that this file  
14 says to Red Bluff, your August 20th, 1987, memorandum says  
15 to Red Bluff. Was that sent -- was this memorandum sent to  
16 Red Bluff?

17 A No, This is -- this is a memorandum --  
18 all this memorandum -- I'm an old guy and I can't remember  
19 everything in the course of conversation and in 50 years of  
20 practice I've learned it's always well to make a memorandum  
21 about any conversation and put them in the file, and that's  
22 my work product.

23 Q On the memorandum dated September 21st,  
24 you refer to Danny and Gay's mineral interests.

25 A Now where is this?

1           Q           In the first paragraph of the second  
2 memorandum, there's a reference there to Gay's mineral  
3 interests.

4           A           Yes. When I filed this application to  
5 get this lease in 1985, and it was before the BLM all that  
6 time and they were -- just all kind of stuff, and it was  
7 some other acreage in the area where somebody, another  
8 party, might have had -- offset this acreage and had the  
9 right to either bid on it or to -- to bid on it or to bid  
10 -- pay compensatory royalty. The Gays had some way away  
11 from this land, but they had some fee acreage up there and  
12 they had leased it to some third party and that's -- she  
13 asked me to get this information for her so that they could  
14 determine who would be given an opportunity to bid.

15           Q           Does that have anything to do with the  
16 Red Bluff lease?

17           A           Yes.

18           Q           In that they would have an opportunity  
19 to bid, is that --

20           A           Well, the Gays, yeah, the Gays leased it  
21 to Kerr McGee, or somebody like that, and then the lease  
22 had expired and they wanted to know the status and the Gays  
23 owned the minerals because anybody -- under the Mineral  
24 Leasing Act any adjoining owner has a right to pay compen-  
25 satory royalties, the only one to get the lease is directly

1 holder to the right-of-way for this assignee and nobody  
2 else can -- it wasn't possible for Oppermann or anybody to  
3 get that lease. Red Bluff had to get it and it's not easy.

4 Q Did -- Mr. Jennings, did you file the  
5 application for Red Bluff --

6 A Yes, sir.

7 Q -- to acquire --

8 A Yes, sir.

9 Q Did you acquire any interest in the  
10 lease as a result of --

11 A No, sir.

12 Q -- that work?

13 A I was well compensated.

14 Q You don't own an interest in the Red  
15 Bluff --

16 A No, sir. I don't own an interest in Red  
17 Bluff. I guess the only way you can get one is if you're a  
18 farmer.

19 MR. PADILLA: I believe that's  
20 all I have.

21 MR. BROSTUEN: Any other  
22 questions?

23 MR. JENNINGS: Does the Com-  
24 mission have some questions? I'll be glad to --

25 MR. HUMPHRIES: Yes, I have a

1 few questions.

2

3 QUESTIONS BY MR. HUMPHRIES:

4 Q Mr. Jennings, did Red Bluff pay any  
5 bonus fees or advance rentals or advanced royalties in  
6 acquiring this lease?

7 A It had to pay the rental, the first  
8 year's rental. It's like -- just like you guys, you get  
9 the first year's rental.

10 Q And that amounted to --

11 A A Dollar an acre, as I recall.

12 Q For some 9 acres?

13 A Oh, no, no, no. The lease, I guess it's  
14 not before us but it's -- it was marked Exhibit Two in your  
15 book there, in the transcript and the lease covered, you  
16 can look at it, it's a lot a land that goes down through --  
17 that goes from Section 8 all down through the township and  
18 goes out down in the south end of Sections 33 and 34.

19 Q So their attempt was to obtain the  
20 shoreline of the lake inclusive.

21 A Well, no. They were -- their attempt  
22 was pursuant to this act of 1930 which allows the owner of  
23 the right-of-way, owner of the right-of-way, to get the  
24 lease on the right-of-way.

25 Q And that right-of-way was to be the

1 shoreline of the lake inclusive of all of that within the  
2 shoreline, or did they seek a certain buffer zone?

3 A I can't tell you.

4 Q Okay.

5 A But I think -- I think that the testi-  
6 mony that somebody stated this morning, that when you gave  
7 the right-of-way the same level as the top of the dam, so  
8 water wouldn't get any higher, shouldn't get much higher  
9 than that because it would go over the dam.

10 Q But again, this specific acreage in  
11 question is some approximately 9 acres but --

12 A Well, this is just part of a big lease.

13 Q I understand, but Red Bluff's economic  
14 exposure to this 9 acres is approximately a dollar an acre  
15 of advanced rental plus a royalty that whoever might be a  
16 successful producer would pay to the federal government.

17 A That's right, but this -- this acreage,  
18 I'm sure, with the federal government concerned, would be  
19 not assignable because it would be (unclear) offsetting  
20 production, you know. It would be competitive bidding as  
21 far as the government was concerned if it was government  
22 acreage.

23 Q But the competitive bidding was the  
24 royalty rate, not an advance (interrupted) --

25 A It was in this but it isn't on the other

1 (not clearly understood) but what -- the other thing that  
2 they did pay is -- you see, I have a file in the office  
3 about that thick, and my efforts to get the lease issued by  
4 the Bureau of Land Management is included; a number of  
5 trips to Santa Fe and getting all the documentation that  
6 they could think of. We started in April of 1985 and we  
7 got the lease in 1987, I guess, '88, '88. I'm getting  
8 behind myself.

9                   And I might also add for information,  
10 there was one bid for -- one of the offset operators bid  
11 for the -- to pay compensatory royalty and that was -- he  
12 owned Sections 3 -- or 33 and 34 which is south of this,  
13 and he was awarded the right to pay compensatory royalty on  
14 that, but he didn't do it and ultimately all the lands in  
15 the reservoir in New Mexico were included. We went back  
16 and got a lease on, on the lands that were -- they put --  
17 amended the lease to put the lands in 33 and 34 back in the  
18 lease, but it goes -- winds around all up through and this  
19 is not going to be a one shot deal because everybody --  
20 there's probably, in these two sections, 27 and 28, there's  
21 probably ten 40's that Red Bluff has some or part of.

22                   Q           Let me again, my interpretation is that  
23 in this right-of-way compensatory royalty lease, Red  
24 Bluff's first endeavor to obtain it was -- consisted of of-  
25 fering a 14 percent royalty, and subsequent to that they

1 had to pay a year's advance rental on the entire amount  
2 that was approximately equal to the acreage that would be  
3 at topographic line or the elevation line equal to the top  
4 of the dam.

5 A And I think it was -- to hold me to  
6 this, I could dig it out for you -- but I think it's in the  
7 neighborhood of 11-or-1200 acres. This lease itself, as  
8 you can see, has 300 -- it's close to 300 acres, but  
9 there's more south of there and they've got some more  
10 acreage and as the reservoir narrows down, it's just -- it  
11 goes up there where it's not as wide in the reservoir  
12 (inaudible).

13 Q But what we are dealing with out of that  
14 entire lease that they got, is the question of completing a  
15 40-acre tract that --

16 A That's right.

17 Q -- Mallon through multiple agreements,  
18 assignments and farmouts, has obtained the lease on and  
19 that remaining part belonging to Red Bluff is something ap-  
20 proximately 9 acres.

21 A It's closer to 10, I think.

22 Q So again Red Bluff's economic exposure  
23 to this particular piece of property is approximately \$9.00  
24 per year.

25 A Well, I guess they can pay the rental.

1 They have to pay the rental. I guess it would go at  
2 minimum royalty now if it gets right down to that. I think  
3 it would go in minimum royalty, and if the royalties are  
4 sufficient to pay the rental, why the rental would be paid,  
5 otherwise, they would have to pay the rental on the rest of  
6 it and maintain that.

7 If that's your question. Now I don't  
8 know whether I'm --

9 Q No, that -- you've answered it. I  
10 understood they had your legal opinion involved, and then  
11 they made no bonus bid, nor did they make an advance roy-  
12 alty payment of some undetermined amount.

13 A No, no, no, there wasn't any bonus in-  
14 volved. All they did was to bid to pay the royalty or not.  
15 The royalty on all of the rest of the acreage is at 12-1/2  
16 percent except in Section 33 and 34 you get 14 percent  
17 rather than 12-1/2.

18 Q And then my next question is, I think I  
19 heard you say this but I want to be sure, that your inter-  
20 nal problem in those, you did not send to Ms. McClintock  
21 and ask her if she concurred. These are your own personal  
22 files, your recollections --

23 A Oh, no, that's -- that was -- well, it's  
24 my recollection made at the time, you know.

25 Q You don't -- you don't have her concur-



1 very brief, Mr. Chairman.

2                   As I stated this morning and  
3 throughout the course of our arguments here today, this  
4 case started out way back a long time ago and I agree fully  
5 with your remarks awhile ago that the question of overrid-  
6 ing royalties really bears no relationship to this case.

7                   Mr. Jennings somehow is trying  
8 to say that we -- Mallon had some kind of continuing offer  
9 for 5 percent royalty. There has been no evidence whether  
10 that is reasonable or not. We have only heard Mr. Jennings  
11 testimony here because, and I insisted on that, because at  
12 least we testimony under oath and it's not a lawyer's  
13 statements as to what -- what his perceptions would be.  
14 His perceptions (not clearly understood) anyway. It's  
15 almost insignificant at this stage, at this time, because  
16 really there has been no deal made. The compulsory pooling  
17 statute is clear. If you have a nonconsenting party,  
18 that's the ballgame. We are here. We have met every con-  
19 dition of the compulsory pooling statute in order to force  
20 pool the interest of Red Bluff.

21                   Mallon is ready to drill.  
22 They have a drilling deadline. They have to get on the  
23 lease, commence drilling, and retain their override.

24                   The economics, the economic  
25 testimony, which has not been refuted, is to the same



1 doesn't do anything except subject Mallon to a breach of  
2 contract lawsuit.

3                   So in short, we feel that the  
4 Commission should issue its order and in so doing we would  
5 request it being done expeditiously so that Mallon can pro-  
6 ceed with drilling the well which is -- this hearing is  
7 about.

8                   MR. BROSTUEN: Mr. Jennings?

9                   MR. JENNINGS: Well, as far as  
10 (unclear) the Commission, I'm in a bad spot by not having  
11 witnesses to testify, but since Mr. Hayes is gone (unclear)  
12 to testify, (inaudible) and at short notice I couldn't get  
13 them up here, but whether I would have or not, I don't  
14 know.

15                   But I do know one of the  
16 things the Commission is supposed to find is some evidence  
17 that the applicant made a reasonable attempt to obtain a  
18 voluntary agreement, maybe it was a reasonable attempt but  
19 they haven't made any more and we're here, we're still here  
20 and the Commission hasn't ruled on it, so if the offer had  
21 been made at the time, we probably would have saved every-  
22 body's time today to take the 5 percent because you can't  
23 afford to be (not understood) with them or anybody else.  
24 This is not economic for Red Bluff and my purpose in try-  
25 ing to call this to your attention was just to show that if

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you do force pool, and I realize that you have -- but I think some consideration should be given to the penalty. A tract down there with wells all around it, and they're doing it and they're getting -- Red Bluff's acreage is nothing and Red Bluff never, according to the testimony of the witness there, Mr. Cox, they won't ever pay out at that rate, so they are actually being deprived of their property.

I know the Commission doesn't have any authority to allow them any overriding royalty in it, but I think it's (not clearly understood) I guess, but you get profit anyway out of the lease by this forced pooling -- I know (unclear) I don't believe they've made a good faith, reasonable effort to lease (unclear). I would appreciate it if you would read the memo. I think that you will find that some of the negotiations were a little less than reasonable and especially since they've taken the case of a deal, want to take a deal that will cost them much more, much better than the deal that we had offered. They wanted to pay another 5 percent to Mallon and you can read that two ways, you can read where he's entitled to 5 percent even if he doesn't get the lease, although I just don't see that in there, and the other thing is that he is -- he's been getting all along, they've given him 5 percent

1 when he was only entitled to 2 under his deal, and that  
2 deal was made back in 1983 when (unclear) earning interest,  
3 (unclear) the whole township, and you know how much a town-  
4 ship is, that's a lot of -- lot of acreage in a township,  
5 and then to come back and contend he gets 5 percent on this  
6 and you force pool us, they're not going to get a --  
7 they'll get a whole lot more out of than 5 percent. Of  
8 course if you force pool it he doesn't get that 5 percent,  
9 why then they stand to profit.

10 That's all.

11 MR. BROSTUEN: Thank you, Mr.  
12 Jennings.

13 If there is nothing else to be  
14 heard in this case --

15 MR. STOVALL: Mr. Examiner, I  
16 would like to check one thing -- or Mr. Chairman -- what is  
17 the deadline under which you're operating and I ask you  
18 remembering this is a Commission hearing and they cannot  
19 simply issue an order in an expedited manner as the Divi-  
20 sion can. They have to have an open meeting in order to  
21 discuss and issue an order.

22 What is your deadline in which  
23 you're --

24 MR. PADILLA: February 1st.

25 MR. STOVALL: And when -- do

1 you know when your next open meeting is scheduled?

2 MR. BROSTUEN: Normally it  
3 would be the first Thursday in the month, that is nor-  
4 mally our --

5 MR. STOVALL: That would be  
6 the 2nd of February, so we may have -- we may have an  
7 issue, you gentlemen may need to consider calling a  
8 special meeting of the Commission to discuss this order and  
9 get it out, if you wish to do so to serve the Mallon in-  
10 terest. I just was a little concerned about that date and  
11 knew that would be a problem.

12 MR. PADILLA: Well, in any  
13 event, I suppose for my clients protection we're going to  
14 have to commence some kind of building activity in order to  
15 preserve (inaudible).

16 MR. STOVALL: My biggest con-  
17 cern with a special meeting is that I don't know the notice  
18 requirements as far as conducting special meetings under  
19 the open meetings law and I'd have to -- Bridget, do you  
20 know offhand what that --

21

22 (Thereupon a discussion was held off the record.)

23

24 MR. BROSTUEN: This concludes  
25 the January 19th hearing day, and the hearing is adjourned.

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C E R T I F I C A T E

I, SALLY W. BOYD, C. S. R. DO HEREBY  
CERTIFY that the foregoing Transcript of Hearing before the  
Oil Conservation Division (Commission) was reported by me;  
that the said transcript is a full, true and correct record  
of the hearing, prepared by me to the best of my ability.

Sally W. Boyd CSR