

STATE OF NEW MEXICO
ENERGY AND MINERALS DEPARTMENT
OIL CONSERVATION DIVISION
STATE LAND OFFICE BLDG.
SANTA FE, NEW MEXICO

20 November 1986

COMMISSION HEARING

IN THE MATTER OF:

The hearing called by the Oil Con- CASE
servation Division on its own motion 9015
for the adoption of new Rules 315,
413, and 903 to establish a new gas
priority production schedule.

BEFORE: Richard L. Stamets, Chairman
Ed Kelley, Commissioner

TRANSCRIPT OF HEARING

A P P E A R A N C E S

For the Division: Jeff Taylor
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inclusive.

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VICTOR T. LYON

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1
2 MR. STAMETS: The hearing will
3 please come to order.

4 Next we will resume case 9015.

5 Mr. Taylor, you have some addi-
6 tional testimony in this case?

7 MR. TAYLOR: Yes, Mr. Commis-
8 sioner. We have Mr. Vic Lyon, who testified, I believe, in
9 the first application.

10 MR. STAMETS: Whenever you're
11 ready, Mr. Taylor.

12
13 VICTOR T. LYON,
14 being previously sworn upon his oath and remaining under
15 oath, testified as follows, to-wit:

16
17 DIRECT EXAMINATION

18 BY MR. TAYLOR:

19 Q Mr. Lyon, did you previously testify in
20 Case 9015?

21 A Yes, I did.

22 Q And since that time have, in response to
23 comments and recommendations at the last hearing, have the
24 provisions of the rules involved in this case, which I be-
25 lieve are 315, 903, and is it 902B?

1 A 315 --

2 Q I don't --

3 A -- 903 --

4 Q -- 903, 315, and 413, have those revisions to those rules been redrafted or changed?

5 A Yes, they have.

6 Q Would you please explain the changes that have been made in these since the last time?

7 A Well, we rewrote the language ahead of the actual listing of the priorities.

8 There was a great deal of discussion at the last hearing about the inclusion of the paragraph -- I think it varied from (b) and (c), and so forth, in the various rules, but the paragraph wherein we quoted the language from the ratable take statute, and there didn't seem to be anybody in the middle, either. Everybody was opposed to it being in there or they were insisting that it should be there, and so we tried to accommodate both sides and changed this language so that we refer to the section of the statute and that preamble reads:

9 "When market conditions or other conditions exists whereby a gas purchaser and/or pipeline system is unable to take all gas legally produced or available from wells connected to its system, to prevent waste and to the extent permitted by Section 70-2-19 F, New Mexico Statutes

1 Annotated, 1978, such purchaser or pipeline system operator
2 shall observe the following priority production schedule:"

3 "For purposes of this rule, a system con-
4 sists of a series of interconnected gathering and trunk
5 lines under the control of a pipeline company which pur-
6 chases and transports gas to a market. Gas purchased by the
7 pipeline for resale shall be considered in a separate system
8 from gas transported in the same pipeline network for an-
9 other purchaser for resale to the same or any other market."

10 Q Okay, and on the parts (a) through (e)
11 there, for instance, (a) it says, "overproduced wells in
12 prorated gas pools and high capacity wells in unprorated gas
13 pools, shall be first restricted . . ."

14 A Yes.

15 Q In what manner is the word "restricted"
16 there used, or how is this restriction to work?

17 A Well --

18 Q Would you just briefly explain that?

19 A -- let me preface my answer to that by
20 explaining that we have expanded this list -- this priority
21 system.

22 We have five classifications now as op-
23 posed to four previously, and we have differentiated in
24 there to some extent the group of wells represented in
25 priority A in the last draft; we've divided into A and B.

1 The new A is overproduced wells in pro-
2 rated gas pools and high capacity wells in unprorated gas
3 pools and then priority B is underproduced and marginal
4 wells in prorated gas pools and lower capacity wells in un-
5 prorated gas pools.

6 In looking at these priorities, we felt
7 that there was a plausible interpretation that by restricted
8 a pipeline could say, well, I restricted priority A to 90
9 percent of the capacity, so I can move to priority B and re-
10 strict that up to 90 percent and so on up the line, and this
11 is not our interpretation.

12 Our interpretation is that all wells in
13 priority A producing into a system must be shut-in before
14 any curtailment on priority B, and furthermore, this goes on
15 up the line, that all wells in both A and B will be shut-in
16 before there's any restriction on priority C.

17 Q Okay, and it's my understanding that the
18 reference in -- in the first part of this rule to Section
19 70-2-19 F, is that the language in 70-2-19 F is the same
20 language that was in part (e) of this rule as it was origin-
21 ally drafted and presented at the last hearing.

22 A Yes.

23 Q And that language -- I don't have it spe-
24 cifically, but it's the language that nothing in this rule
25 shall be -- shall require someone to take gas for any reason

1 that it's not economic or that language --

2 A Right, and there -- there are reasons for
3 our insisting on that reference.

4 Q And that, I'm sure, is what everybody
5 wants to hear.

6 A We feel that under the decisions which
7 have been entered both in the Transco case and in the more
8 recent case in Oklahoma, where the priority system of the
9 Oklahoma Corporation Commission was struck down by the
10 court, places limitation on -- on what we can order people
11 to do, and we feel that those, those limitations must be in-
12 cluded in that statutory language, that if we do not have
13 this reference in there, and if we do not recognize and
14 operate under the mandate of the statute, that we have a
15 very seriously legally flawed rule, and in order to make it
16 enforceable, we think we need this language.

17 Q Were you around at the time that that
18 language was added in the statute and can you shed any light
19 on your understanding of any of that language when it was
20 placed in the statute and the reason why it was place there?

21 A No, I'm sorry, I was not there and I can-
22 not speak to the intent.

23 Q Okay. Since we've already presented tes-
24 timony in this case at the earlier hearing, I'm sure there's
25 a lot of comments, I think, unless you have anything else --

1 A No, I think that's all I have.

2 MR. TAYLOR: That's all we have
3 of this witness.

4
5 CROSS EXAMINATION

6 BY MR. STAMETS:

7 Q Mr. Lyon, the changes in Rule 315 and 413
8 would simply be the same one you talked about earlier, the
9 preamble relating to market conditions and legally produced
10 gas, and then the addition of the higher capacity wells ver-
11 sus the lower capacity gas wells as A and B.

12 Is that correct?

13 A Yes, that's true.

14 Q Would it be appropriate, in your view, to
15 add a sentence somewhere to these rules which would say all
16 wells in -- in higher categories shall be shut in before re-
17 striction in the next lower category shall be made, or some-
18 thing to that effect?

19 A I think it would certainly clarify the
20 situation and our interpretation of -- of the priority sche-
21 dule that we have proposed here.

22 Q Okay.

23 MR. STAMETS: Are there ques-
24 tions of Mr. Lyon?

25 MR. KENDRICK: May I ask a
question or do I need to go through counsel?

1 I could ask it on my behalf as a royalty
2 owner and a --

3 MR. STAMETS: Good, please do
4 that.

5
6 QUESTIONS BY MR. KENDRICK:

7 Q In the San Juan Basin sometimes marginal
8 wells in prorated pools are the most prolific producing
9 wells within those pools, and if marginal wells are classed
10 down in Item B behind, quote, high capacity wells un unpro-
11 rated gas pools, can high capacity marginal wells be so
12 classified?

13 A How classified?

14 Q As high capacity --

15 A As marginal?

16 Q -- wells in a nonprorated pool.

17 A Well, if they're in a prorated pool I
18 don't think that would apply.

19 What you're describing is -- seems to be
20 an anomalous situation. Can you explain why a high capacity
21 well is marginal?

22 Q Again --

23 MR. STAMETS: Excuse me,
24 gentlemen. I'm not sure that that's germane to the issue at
25 hand.

1 A That's -- I'm sorry.

2 MR. STAMETS: And I would sug-
3 gest we just move on from that unless there are additional
4 questions.

5 MR. KENDRICK: No further ques-
6 tions.

7 MR. STAMETS: Mr. Hall.

8
9 CROSS EXAMINATION

10 BY MR. HALL:

11 Q I did have one question in that regard.
12 I was was just wondering if Mr. Lyon had any sort of defin-
13 ition in mind for pipe testing at the well.

14 A Well, I'm not sure how you would define
15 that but there are some, I think, it would be obvious.
16 There are others that might take some interpretation.

17 Q Would it be possible to establish some
18 sort of cue number or test number in the rules to give to
19 this as some sort of guideline?

20 A Well, if you wanted to, I suppose we
21 could say the upper 50 percent and the lower 50 percent.

22 Q May I be allowed to inquire in further
23 matters?

24 A You certainly are allowed.

25 Q I'll ask you a question about the pre-

1 amble to the rule that says unable to take all gas legally
2 produced.

3 What's meant by the term "gas legally
4 produced"?

5 A I think that probably means the gas which
6 is authorized by the allowable.

7 Q Would that be the only definition of
8 illegal gas, gas produced without an allowable?

9 A That -- that's the way the statute reads.

10 Q All right. Again with respect to Section
11 70-2-19 F, a lot of the producers are concerned that this
12 statute might be construed broader than its original intent
13 so as to allow a de facto (not clear) the OCD regulations.

14 In your view is that statute really
15 directed towards anything other than engineering
16 impracticability?

17 MR. STAMETS: Mr. Hall, because
18 of the way you phrased that question I feel compelled to ask
19 you a question.

20 How do we know what the
21 original intent of the statute was? There's no legislative
22 history and it seems as though the statute speaks for itself
23 in its -- in its language, and it would seem to be it would
24 have to be interpreted in light of the testing conditions
25 today?

1 MR. HALL: Well, I would dis-
2 agree somewhat. I think the statute does make reference to
3 certain engineering comparisons. It references gas under a
4 quality or gas under a pressure, which may prohibit unecono-
5 mic use.

6 MR. STAMETS: But what else
7 does it say? Would you read on from that point?

8 MR. HALL: Well, it says, "...
9 such gas cannot be economically and satisfactorily..." --

10 MR. STAMETS: It seems to me
11 that you --

12 MR. HALL: -- I'm sorry.

13 MR. STAMETS: -- let out a few
14 words there. Would you please just read the whole section
15 for us?

16 MR. HALL: "Nothing in this Act
17 shall be construed or applied to require, directly or indi-
18 rectly, any person to purchase gas of a quality or under a
19 pressure or under any other conditions by reason of which
20 such gas cannot be economically and satisfactorily used by
21 such purchaser by means of his gas transportation facilities
22 then in service."

23 The question is, I guess, are
24 we considering that to, in the broad sense, to include gas
25 marketing facilities in any circumstance?

1 MR. STAMETS: Well, what does
2 "any other condition" mean?

3 MR. HALL: Do you want my in-
4 terpretation?

5 MR. STAMETS: Well, I think
6 it's unfair to ask a witness to, after he's already said he
7 wasn't at the hearings where this all was adopted, he
8 doesn't know what they may have said at that time, it seems
9 improper to ask him questions which make him speculate,
10 first off, what the original intent was.

11 MR. HALL: Well, I don't be-
12 lieve that was my question at all.

13 That question came up through
14 OCD's own (unclear). I'm simply trying to determine what
15 the present understanding of the OCD staff is with respect
16 to that.

17 MR. STAMETS: Well, let's try
18 the question again, Mr. Hall.

19 Q Well, the question is, do you understand
20 the section I've read to take into consideration any matters
21 other than engineering impracticability?

22 A I don't think it's limited to that and
23 you're asking me to speculate on what a court might decide
24 on it, and I don't think I'm qualified to do that.

25 Q Well, I think an administrative agency

1 certainly has the powers to determine the extent of its own
2 authority and jurisdiction under these statutes. That's why
3 I believe it's important to know.

4 A All right, I will answer that in view of
5 the court decisions we have seen on questions of this type,
6 I think that it would involve other things than engineering
7 considerations.

8 Q What other things?

9 A Well, it can involve a lot of things, in-
10 cluding price.

11 Q Can you point out any other reference in
12 the statute other than this particular subsection which
13 might enable the Oil Conservation Commission to consider
14 commercial impracticability? Do you know of any other?

15 A Do we need another one?

16 Q Do you know of any other?

17 A Not offhand, no.

18 Q I'd like to go to the last paragraph in
19 the first page of that rule, and that's the definition for
20 system. I'm wondering why it's necessary to define pipeline
21 system at all unless you're trying to exclude certain activ-
22 ities.

23 A Well, there have been a number of inter-
24 pretations of system and I just thought that it might be
25 well to -- to define what we consider a system to be.

1 Q Well, let me ask you your opinion of in-
2 serting in the second line after the word "purchases and" to
3 insert word "or", so it reads " control of that pipeline
4 company which purchases and/or transports gas to a market."

5 Would that be acceptable to the Division?

6 MR. STAMETS: Presumably, what
7 you're thinking about, Mr. Hall, is the apparent tendency of
8 the old line pipelines to get away from the purchasing ac-
9 tivities and more into the transportation service.

10 MR. HALL: That's right. The
11 question is whether this rule would be applicable to pure
12 carriers and likewise, I guess, to pure marketers, when
13 those activities are separate.

14 A Well, I think the second sentence there,
15 the last sentence, covers that situation, does it not?

16 Q I don't agree with you. I wonder if you
17 could elaborate on that?

18 A Well, I think that a -- where a pipeline
19 is the purchaser and he also carries gas under open access,
20 that he has one system over which he has control and the
21 other system he does not have control, all he is is the
22 transporter.

23 Q Wouldn't that still allow an exception
24 for a facility that is simply a pure transporter or carrier
25 that --

1 A Well, I --

2 Q -- does not market the gas?

3 A -- don't think that a pipeline is going
4 to carry gas for which there's no market, and to that extent
5 I don't think that a pipeline can take gas into its line and
6 put it in a hole in the ground; it's got to go somewhere.
7 If he doesn't have a market, well, a transporter can't --
8 can't take it into his line.

9 Q Let me ask you, what -- what elements
10 would the Division consider when evaluating market condi-
11 tions?

12 A Well, how many things are there to con-
13 sider? We've got to consider everything that impacts on the
14 market.

15 Q So you don't have anything in mind at
16 this point for purposes of this rule?

17 A No, we're just trying to set up a rule
18 that we feel that we can administer, and that will not be
19 subject to immediate successful challenge in the court.

20 Q Well, in that respect, if we are going to
21 be -- excuse me, if we're going to be considering market-
22 place economics, I assume that will be an on-going consider-
23 ation and in that regard will the definitions for, say, high
24 capacity and low capacity wells also be subject to change?

25 A Now, say that again.

1 Q Well, if we are going to be considering
2 market conditions in establishing priority takes, I assume
3 that the market is always going to be in a state of flux or
4 a state of change; likewise, that would require revision to
5 any definitions of capacities of such wells, i. e. high cap-
6 acity wells and low capacity wells.

7 A Hopefully, when the -- when the market
8 gets straightened out we can -- we can forget about all this
9 and everybody will be producing all the gas that he can --
10 he can sell all the gas he can produce.

11 But we -- I certainly am not saying that
12 we won't have to revise our rules again as the situation
13 changes. We're in a new world just about every day. We're
14 trying to be flexible enough that people can operate under
15 the rules and we can still do the job that the statute says
16 we must do.

17 Q Well, in that regard, are we going to al-
18 low marketplace consideration to outweigh considerations of
19 preventing waste?

20 A Well, our primary responsibility is to
21 prevent waste and in doing so, to protect correlative
22 rights.

23 In doing this we've got to recognize the
24 situations that exist in the industry and to accomplish our
25 ends as best we can under those circumstances.

1 One final question. I'd like to get your
2 opinion on this proposed change to the preamble to the rule.
3 if we were simply to delete the words "when market
4 conditions or other conditions exist whereby" and then
5 insert in lieu thereof "wherever", so the preamble starts
6 with the word "wherever".

7 A You -- you would say -- you would just
8 start and say wherever or whenever --

9 Q Yes, -- I'm sorry.

10 A -- a gas purchaser and/or pipeline system
11 is unable to take ...". I think it could be workable that
12 way, yes.

13 Q One final, final question. Are marketers
14 going to be subject to this rule?

15 A Who do you include in marketers?

16 Q Just speaking of a pure marketer, a
17 marketer without its own pipeline system facility.

18 A I don't think it applies to the marketer.
19 I think it applies to the transporter and the producer.

20 Q Thank you, Mr. Lyon.

21 MR. STAMETS: Are there other
22 questions of the witness? Mr. Kellahin.

23

24

25

CROSS EXAMINATION

BY MR. KELLAHIN:

Q Mr. Lyon, for purposes of my question, let's assume the proposed rule is adopted with the following changes that do utilize Mr. Hall's suggestion of deleting the market condition language.

Let's further assume that the reference to Subsection F of that statutory citation is also deleted, and that is the Rule F.

In discharging its obligations under the statutes the Commission is obligated to prevent waste of hydrocarbons. In what specific ways does that rule, then, help to prevent waste within categories and among wells in relation to those categories?

A Well, in the first place, the priorities give high priority, the highest priority, to hardship gas wells which, if they do not continue to produce, are subject to loss or damage to the wells and reduction of recoverable reserves, which certainly is waste.

The next highest priority goes to casinghead gas and casinghead gas is produced with oil. If you restrict casinghead gas, you restrict oil production, and if there isn't physical waste, there certainly is an economic hardship on the operators in the State of New Mexico and also it would require that we import more crude oil in order

1 to -- to replace the oil that otherwise would have been pro-
2 duced.

3 So I think that it is obvious that
4 casinghead gas should have a high priority.

5 MR. STAMETS: While you're at
6 that point, Mr. Lyon, wouldn't another alternative for cas-
7 inghead gas be to allow the gas to be flared in the field in
8 order to keep the well production up?

9 A That is another option but the flaring of
10 gas is declared in the statute to be waste.

11 Q You've answered each of the categories
12 with regards to justifying it solely on the waste concept.
13 Can you make that justification as you continue on up
14 through the rest of the categories?

15 A I think that there is a question of waste
16 in the downhole commingled wells, where a gas zone and an
17 oil zone, or more of each, are commingled such that there
18 could be a drowning of one reservoir, commingling of fluids
19 where required under the statute to see that the fluids in
20 each formation are -- are produced separately or not com-
21 mingled in ground.

22 So the waste consideration goes to that
23 point.

24 The next category, the underproduced
25 wells, the marginal wells, are handicapped as it is by their

1 lack of ability to compete with their neighbors. If they
2 are unduly restricted there's a possibility that those could
3 be unecoomical and plugged and those reserves lost. So I
4 think that the waste goes to that category, too.

5 Q So the rule, as I suggested it to you,
6 can stand alone as a representation of the exercise by the
7 Commission of its mandate to prevent waste, totally irre-
8 spective of correlative rights concepts.

9 A Yes, I think so.

10 Q Now if we add in the phrase in the sub-
11 section under the statute, the Subsection F, when does that
12 add or subtract from the rule?

13 A It merely calls to the -- the operators
14 and purchasers, transporters, the fact that that statute ex-
15 ists.

16 MR. KELLAHIN: Thank you, Mr.
17 Chairman.

18 MR. STAMETS: Are there other
19 questions of Mr. Lyon?

20 Mr. Padilla.

21

22

CROSS EXAMINATION

23 BY MR. PADILLA:

24 Q Mr. Lyon, as I understand the question
25 posed by Mr. Hall, you don't have a problem with deleting

1 that language (not clearly understood) that language if you
2 insert the word "whenever" in front of "a gas purchaser"?

3 A I don't think it's essential. I think it
4 is consistent with our times and may give some -- some indi-
5 cation of the need to change the rule at all.

6 Well, this is being added. This is being
7 placed in the rule as opposed to being on the authority of a
8 memorandum.

9 Q Certainly I don't know whether you would
10 agree with me or not, but it seems to me that by deleting
11 that language you would be more consistent with the adver-
12 tisement of this case.

13 The advertisement contains no language
14 with regard to market conditions and other conditions.

15 Do you agree with me on the advertisement
16 of the case?

17 A I'm sorry, I really -- I'd have to com-
18 pare it with the advertisement, but I don't think that --
19 that language is essential to the -- the rule being effec-
20 tive.

21 Q During the last hearing our objection was
22 to what we believed was an expansion to the ratable take
23 statute. We did not have an objection to the insertion of
24 the statute there but we did have an objection to what we
25 call expansion of the statutory language.

1 Let me ask you also, sir, with regard to
2 the last paragraph of -- or the second paragraph of where
3 you define pipeline system. By that language you're not
4 trying to prioritize what system a pipeline should have
5 priority -- what gas has priority under any system.

6 A No.

7 Q You're simply trying to define a pipeline
8 system.

9 A Well, the language up above says such
10 purchaser or pipeline system operator shall observe the fol-
11 lowing priority production schedule.

12 Q But what I'm asking you is that you're
13 not trying to say that gas for resale or gas being
14 transported has any priority under this ruling as (not
15 understood.)

16 Is that in the rule --

17 A As opposed to what?

18 Q You said in the rule that you have one
19 system which is gas for resale and gas that the pipeline is
20 controlling as two separate systems.

21 This rule does not attempt to prioritize
22 gas under either of those two systems, does it?

23 A No, I don't think there's anything in
24 there that says that it does.

25 Q Just wanted to make sure.

1 MR. STAMETS: You will recall,
2 when we had this hearing last month I advised everybody that
3 anyone representing other than himself, as Mr. Kendrick did
4 today as a royalty interest owner, or individuals who have
5 their own business, would have to go through an attorney.
6 That's in accordance with an Attorney General's opinion that
7 goes back many, many years, but if there are any of those of
8 you out there who are royalty interest owners who have some
9 questions, certainly we'll allow you to ask those.

10 Mr. Blackwood.

11 MR. BLACKWOOD: I would --
12 we've had a partial answer for this question Mr. Hall asked
13 on my behalf, but I'm still concerned with how this high ca-
14 pacity wells and low capacity wells would be workable. I
15 would -- you've given us the higher 50 percent and the lower
16 50 percent, but I think for me to understand on a monthly
17 basis what these priorities really are, the Commission would
18 need to say every month high capacity wells in unprorated
19 fields are those wells with a Q or a D of X, you know, 1000
20 Mcf per day or 800 or 200, whatever the number is.

21 A You mean for each reservoir?

22 Q I don't know. That's what I'm -- I don't
23 know if it's statewide, I don't know what it is.

24 What I'm saying is for me to understand
25 your system, I'm going to need the help of the State in each

1 month defining what a high capacity well in an unprorated
2 pool is or what a low capacity well in an unprorated pool
3 is, and we need that additional help in order to understand
4 what you're doing here.

5 A Well, Mr. Blackwood.

6 Q Yes.

7 A Why do you need this each month?

8 Q Well, aren't these -- aren't these rules
9 going to be put on -- maybe I only need them annually, but I
10 need to know what they are all the time.

11 A Well, you may or may not recognize that
12 this is the first time that we have included in our priority
13 schedule any mention of unprorated wells.

14 Q Well, I do. I think I -- I greatly ap-
15 preciate and think you have a much better rule here this
16 month than you had last month.

17 A Thank you.

18 Q But there is still an area that I don't
19 understand and that if I want to -- if I want to know, if my
20 purchaser tells me, we're going to buy gas from these wells
21 and not these wells, in order for me to check up on the cor-
22 rectness of his advice to me, I have to have a definition of
23 these categories, if you see what I mean, for me to have any
24 check, and that's what I'm asking for. I think -- I think
25 that that -- and I don't know if you make that definition on

1 an annual basis, a quarterly basis, but there has to be a
2 definition of what that means for me to have any understand-
3 ing of whether or not I'm being -- my wells are being al-
4 lowed to be turned on that are supposed to be turned on or
5 not supposed to be turned on.

6 A I understand your concern, Mr. Blackwood,
7 and I appreciate your -- your comment. I think it's a valid
8 comment.

9 The problem is that we don't have all the
10 information on unprorated wells that we do on prorated
11 wells, and it -- it might give us a little problem as to --
12 for instance, if we said the upper 50 percent and the lower
13 50 percent, I'm not sure that we have the deliverability
14 data on those wells to draw that line.

15 Q But, Mr. Lyon, say, boy, if you don't
16 have it, how in the world I would get it.

17 A Well, don't you operate in the field?

18 Q Yes.

19 A Don't you know when --

20 Q Am I allowed to write my definition? Am
21 I allowed to -- if I am, I'll write one, but --

22 A I appreciate your suggestion.

23 Q Okay. I think the rule is unworkable
24 without an explanation of what those are.

25 A I think we could probably do some im-

1 provement.

2 MR. STAMETS: Are there other
3 questions of Mr. Lyon?

4 Would you identify yourself for
5 the record, please?

6 MR. BRATTON: My name is Don
7 Bratton and I own a working interest owner of producing oil
8 and gas wells in southeastern New Mexico.

9
10 QUESTIONS BY MR. BRATTON:

11
12 Q I have a question with regard to the in-
13 tent for separating the systems with regard to the statement
14 of the last sentence of the last paragraph. As it's indi-
15 cated it's (unclear.)

16 Can you clarify why there's a need for
17 separate systems? My view of this, it appears to me that
18 there's an opportunity here for, by subdividing into differ-
19 ent systems, for one producer to say, well, I'm in compli-
20 ance, I don't have any casinghead gas wells, therefore I can
21 produce all the dry gas that's available to my system, while
22 in another system a marketer may have casinghead gas wells
23 and he's not allowed to produce that or he's not allowed to
24 produce dry gas because he has casinghead gas that this pre-
25 cludes him from producing it.

1 I guess I'm confused as to why we have to
2 subdivide and separate into various systems. It appears to
3 me that it's the intent of the State and this regulatory
4 agency is to insure that there's not waste within the State,
5 thereby applying these rules consistently across the state,
6 and I think the only way you can look at that is on a total
7 system basis rather than subdividing into different systems.

8 Can you clarify that?

9 A Well, these systems are pipeline systems.

10 Q I understand that but you're saying here
11 gas purchased by the pipeline for resale shall be considered
12 in a separate system from gas transferred in the same pipe-
13 line network for another purchaser for resale.

14 Now is that other purchaser that's re-
15 selling that gas and it's being transporter through that
16 system, he's going to be required to follow this priority
17 schedule apart from the pipeline company that purchases and
18 resells for their own benefit and they're a separate system
19 and they follow the priority schedule.

20 Is that my understanding?

21 A I think that's right, if I heard you cor-
22 rectly.

23 MR. STAMETS: Let me -- let me
24 see if I can clarify this for everybody.

25 Let's go to a very simple case

1 where we've got a pipeline A and they -- and they have al-
2 lowed gas purchaser B to transport gas over their line and B
3 signs up nothing but high capacity gas wells. They have no
4 downhole commingled wells. They have no casinghead gas. So
5 they could, purchaser B could then take all of their con-
6 tracted gas from these high capacity gas wells, while other
7 wells on that pipeline system not selling to purchaser B
8 could be shut in.

9 MR. BRATTON: That's my under-
10 standing when I read it the way it's written now.

11 A That isn't the way we intended it to
12 state. I don't think it states that. I think it says that
13 pipeline A can consider those wells that he purchases from
14 and resells as a system but all other wells producing into
15 his system, into his pipeline system, is another one system,
16 not defined by purchaser but by pipeline for -- pipeline gas
17 for resale, pipeline gas transported.

18 Q Well, for purposes of the rule, why is it
19 necessary to separate the two systems, I guess is my ques-
20 tion?

21 A Well, because they felt that there were
22 different circumstances involved.

23 Q Can you give me an example of the circum-
24 stances that would require the separation?

25 A Well, as you know, most of our gas goes

1 out to California and they have out there what they call
2 core gas and non-core gas, and the core gas is the gas which
3 is transported under a contract where the pipeline company
4 purchases the gas and sells it to the utility -- well, to
5 the utilities out there at the California border.

6 And this is gas that they don't just
7 merely transport, and they have a separate call on that gas
8 out there for that market. The rest of the gas is kind of
9 in limbo. It's stock market or whatever, and a lot of --
10 more and more it's becoming the gas which is merely trans-
11 ported by virtue of a contract directly between the producer
12 and the consumer.

13 I feel that there is a difference in the
14 amount of control a pipeline has over his purchases in those
15 two situations.

16 Q Well, I find it very difficult to see in
17 my mind how the State is going to be able to regulate and
18 insure the prevention or the protection of correlative
19 rights in insuring that everyone has equal access to the
20 market by subdividing and classifying gas in the various
21 systems.

22 It appears to me that the opportunity,
23 like Mr. Stamets pointed out, would be there for one pur-
24 chaser who only contracts high capacity dry gas, and as a
25 result be able to produce all of that gas into the market

1 while in another system casinghead gas or hardship wells may
2 be shut in or curtailed because of their -- their require-
3 ment to comply with -- with this priority production sche-
4 dule.

5 MR. STAMETS: Let me make an
6 observation here.

7 I'm -- that the gas business
8 today is sort of like standing at the end of a railway tun-
9 nel looking where you can't see any light. Now you can cer-
10 tainly imagine how things are down in this dark, dark tun-
11 nel, but you don't really know.

12 We're in the midst of tremen-
13 dous transitions in the gas business and we've getting away
14 from the old standard where the pipe line was the purchaser
15 of the gas, the transporter of the gas, and delivered at the
16 other end to the local distributing company, to a situation
17 where free competition is being encouraged and it's not un-
18 reasonable to expect that there'll be a multiplicity of pur-
19 chasers in the future; where maybe El Paso is the only pur-
20 chaser now, maybe on El Paso's pipeline there will a dozen
21 purchasers out of any particular pool.

22 The Oil and Gas Act, the common
23 purchaser section speaks of the purchaser as opposed to the
24 pipeline company, and a purchaser is only required to take
25 ratably in a pool. It would seem as though if a purchaser

1 comes in, as I understand from reading the paper yesterday,
2 SoCal Gas is going to be asking new marketers, and I'm not
3 certain if a marketer is a purchaser, they're asking new
4 marketers to get up to 350-million a day of gas which El
5 Paso Gas Marketing formerly supplied to them, and that's
6 going to mean that we're going to have people jumping all
7 over New Mexico here trying to find enough gas, and if those
8 are purchasers, and I'm not sure who the purchaser is, if
9 they're the purchaser or SoCal Gas is the purchaser, but if
10 those purchasers purchase, the only place that we could re-
11 quire them to take ratably would be in the pools in which to
12 purchase, and that would clearly be a case where we'd be
13 talking about a separate system, I would think, in that if
14 Joe Blow, gas marketer, buys gas from you in this pool, and
15 that's a gas pool, then they don't have any casinghead gas
16 that they can take, and there's nothing in our law which
17 would require them to take gas in any other pool, other than
18 the one that they are purchasing in, if they're a purchaser,
19 and is that clear?

20 MR. BRATTON: I understand what
21 you're saying, but I want to go on the record as saying I
22 think the way it's written by subdividing into these dif-
23 ferent systems, I think, is creating the opportunity for a
24 lot of things.

25 A I'd like to observe that you probably

1 have not heard some of the definitions of system that I've
2 heard. This is probably the most stringent definition of a
3 system that anybody has come up with.

4 MR. STAMETS: Other questions?
5 Mr. Currens.

6
7 CROSS EXAMINATION

8 BY MR. CURRENS:

9 Q Mr. Lyon, did I understand your response
10 awhile ago having to do with how many parts there were to a
11 pipeline, that there couldn't be more than two, if I under-
12 stood correctly your answer awhile ago, you said that with
13 respect to a system, one who -- I'm going to call it an in-
14 terconnected series of pipes so that we don't give it a sys-
15 tem title, -- with respect to a system, one who owned and
16 operated that system, bought gas, and transported it through
17 that system and delivered it to customers -- or
18 interconnected series of pipes -- that was a system, and
19 then that all of the people that he simply transported for
20 through that interconnected series of pipes became one
21 system between them and not each individual that he would
22 transport it for?

23 A Now that's -- that's my interpretation,
24 yes.

25 Q Thank you.

1 MR. STAMETS: Mr. Hall.

2
3 RECROSS EXAMINATION

4 BY MR. HALL:

5 Q You commented previously that it was your
6 opinion that this proposed rule would not apply to
7 marketers, but I think if you'll poll the audience, the
8 producers here, a lot of them had the same understanding
9 that this -- that this gentleman had, that you allow what is
10 in effect a dual designation for a single physical pipeline,
11 the Oil Commission is in fact exceeding its jurisdiction by
12 leaving the ratable take factor to the marketing entities.

13 A Well, I don't quite agree with you. The
14 -- I think we could have gone a lot further that way and
15 initially I had -- had not put that last part on there, but
16 I felt under the circumstances as we see it unfolding today,
17 that there probably was a need to -- to have a separate
18 system.

19 Q Is it your opinion that the rule couldn't
20 be effective if that last paragraph were simply stricken
21 entirely?

22 A Well, then aren't you back to a system
23 being defined by anybody who wants to define it?

24 Q Isn't it defined now by somebody who is
25 supporting that purchaser (unclear)?

A Yeah, one or the other, so you've got in

--

1 -- in one pipeline you can have two systems but not more
2 than two systems.

3 Under what you're proposing you could
4 have any number of systems and it depends on who -- who de-
5 fines the system.

6 A pipeline can define it one way and the
7 producer could define it another, and somebody else define
8 it still another way.

9 MR. STAMETS: Mr. Strand.

10

11

CROSS EXAMINATION

12 BY MR. STRAND:

13 Q Mr. Lyon, would you consider a pipeline
14 and a marketing affiliate to constitute two systems -- and a
15 marketing affiliate that a pipeline had set up, would you
16 consider those to be separate systems under this last sen-
17 tence you were talking about?

18 A Is this a -- is the marketing affiliate
19 buying the gas?

20 Q Yeah, let's get down to the same thing,
21 El Paso and El Paso Gas Marketing.

22 A I can -- I can -- if -- if El Paso Mar-
23 keting is buying the gas from the purchaser for resale at
24 the other end of the pipeline, then I think it's a single
25 system.

1 Q Okay, and then aren't they going to do
2 exactly what Mr. Stamets pointed out in his example, manipu-
3 late this system so that they can buy and sell that they
4 want to sell at a particular price on a spot market, or
5 whatever, and then utilize the priority system on the tradi-
6 tional market to shut-in wells?

7 A Isn't that what they're doing now?

8 Q It certainly is.

9 A I think with this definition of system
10 they're -- they would -- they would be more subject to
11 being called in to explain unratable taking.

12 MR. STAMETS: Other questions
13 of the witness?

14 Mr. Kendrick.

15

16 QUESTIONS BY MR. KENDRICK:

17 Q Mr. Lyon, I'm having a lot of difficulty
18 understanding just what you're saying.

19 What I understood you to say was that a
20 pipeline owner as a purchaser constitutes one system.

21 A contract carrier shipping gas along a
22 pipeline system -- excuse me, all the contract carriers
23 shipping gas along that same pipeline system constitutes the
24 second system.

25 If that is true and there are multiple

1 marketers shipping along that line, you're forcing some of
2 those people to take gas from wells they do not have a con-
3 tract with.

4 A How's that?

5 Q If -- if marketer B has contracted from
6 some wells and marketer C has contracted from wells and mar-
7 keter D has contracted from wells, and they all have to be
8 grouped into one system and follow this schedule of produc-
9 tion, if more than one class under this schedule are con-
10 nected to one or more of those systems, you're going to
11 force some marketers to take gas from wells from which they
12 have no contracts.

13 A I don't see that follows.

14 Q If they're supplying gas to purchaser B
15 and he's contracted only for high gas -- high gas -- high
16 volume gas wells, but that system has to curtail high volume
17 gas wells or overproduced wells, then he has to take gas
18 from a well from which he has no contract.

19 A I don't see that's necessarily true.

20 Q How's he going to get his gas if the
21 system requires all of the Schedule A wells to be shut-in
22 and that's all he has contracts --

23 A Are you -- are you telling me that there
24 is not gas that he can contract?

25 A No, I'm telling you that that's what he

1 has contracted and he -- and the pipeline owner has agreed
2 to transport the gas, but under his classification in the
3 system, separate from being the pipeline owner, Schedule A
4 wells all have to be shut-in.

5 MR. STAMETS: Gentlemen, let's
6 -- I think this is a good time to break for lunch and I --
7 and I would wish that all of those who are interested in
8 pursuing this line of examination meet Vic down here and go
9 to lunch and see if you can't get it figured out, and we'll
10 resume the hearing in -- at 1:15.

11

12 (Thereupon the noon recess was taken.)

13

14 MR. STAMETS: The hearing will
15 please come to order.

16

17 At the break I was advised that
18 the witness who will be representing the committee in Case
19 9018 had an obligation to leave this evening, and much as I
20 hate to, I think we're going to have to break this case and
21 hear the testimony of that witness, assuming we've got an
22 attorney. Anybody know where Mr. Taylor is?

23

24 In any event, I think we're
25 going to have to take Mr. Fields and let me suggest that
while we are doing this anyone who's interested might meet
at the back of the room with Vic Lyon and see if there is a

1 need for some sort of a longer continuance in Case 9015. If
2 anyone thinks that we could benefit by any further delay in
3 action in that case, so that we would be willing to consider
4 formation of a little further study committee and action on
5 that later.

6 With that in mind, regretfully
7 we'll have a short continuance in Case 9015.

8
9 (Thereupon this hearing was continued until
10 a later time on the same docket.)
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1 MR. STAMETS: Which leaves us
2 then with Case 9015.

3 Is there a sense that you all
4 would like to come back tomorrow and try and work some more
5 on the priority schedule or there a sense that you would
6 like to try and work on this in a committee and plan on com-
7 ing back in January and hoping that we're here?

8 Mr. Kellahin.

9 MR. KELLAHIN: Mr. Chairman, as
10 at your suggestion we met earlier today with Mr. Lyon and
11 tried formulating an additional study committee. If you de-
12 sire to continue to work on that priority schedule, Mr.
13 Stovall and I have agreed to participate.

14 Bob Strand was here earlier and
15 he's agreed to participate, and there were some others that
16 we are hopeful we could resolve our differences with some
17 further committee action, and we would request now on behalf
18 of my clients to continue that case to a January hearing and
19 allow Mr. Lyon the opportunity to work with us to see if we
20 could come to an agreement on that.

21 MR. STAMETS: Is there any par-
22 ty with a different opinion?

23 Based upon that, then, we will
24 be continuing Case 9015 to January the 8th.

25

(Hearing concluded.)

C E R T I F I C A T E

I, SALLY W. BOYD, C.S.R., DO HEREBY CERTIFY 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 this portion of the hearing, prepared by me to the best of my ability.

Sally W. Boyd CSR

STATE OF NEW MEXICO
ENERGY AND MINERALS DEPARTMENT
OIL CONSERVATION DIVISION
STATE LAND OFFICE BLDG.
SANTA FE, NEW MEXICO

5 March, 1987

COMMISSION HEARING

IN THE MATTER OF:

The hearing called by the Oil Con- CASE
servation Division on its own motion 9015
for the adoption of new Rules 315,
413 and 903 to establish a gas pro-
duction schedule.

BEFORE: William J. LeMay, Chairman
Erling A. Brostuen, Commissioner

TRANSCRIPT OF HEARING

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MR. LEMAY: The hearing will
come to order.

4

5

The Oil Conservation Commis-
sion, and I'd like to introduce our new commissioners.

6

7

8

9

On my right is Erling Brostuen,
who is Director of the Mining and Minerals Division of the
Energy Department, and he's also State Geologist, and he
will be one of the three commissioners.

10

11

12

Myself, Bill Lemay, I'm Direc-
tor of the Oil Conservation Division, Energy and Minerals
Department, another director -- or another commissioner.

13

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The third commissioner, Bill
Humphries, expressed his apologies. He was not able to make
the meeting today because of a prior commitment in Albuquer-
que; however, he does plan to be an active member of our
Commission and we look forward to having him join us in the
future hearings.

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I now call case 9015.

MR. TAYLOR: May it please the
Commission, I'm Jeff Taylor, Counsel for the Oil Conserva-
tion Division, and I'll enter an appearance on behalf of
the Division and we'll have one witness, I believe, in this
case.

MR. LEMAY: Okay, I'll read the

case for the record.

1 MR. TAYLOR: In the matter of
2 the hearing called by the Oil Conservation Division on its
3 own motion for the adoption of new rules -- I can't read
4 this -- 3 is it --

5 MR. LEMAY: 315, I think.

6 MR. TAYLOR: -- 413 and 903, to
7 establish a gas priority production schedule.

8 The Division seeks adoption of
9 a hierarchy of classes of gas production in times of severe-
10 ly restricted demand for gas from New Mexico wells.

11 Also to be considered will be
12 the application of such rules to purchasers with marketing
13 affiliates.

14 MR. LEMAY: We call for appear-
15 ances in Case 9015.

16 MR. NANCE: On behalf of El
17 Paso Natural Gas Company, my name is John Nance.

18 MR. LEMAY: You'll have one
19 witness or --

20 MR. NANCE: We don't anticipate
21 having a witness at this point, although we may have -- we'd
22 like to reserve the right to call a witness if we need
23 one.

24 MR. CARR: May it please the
25

1 Commission, my name is William F. Carr with the law firm
2 Campbell & Black, P. A., of Santa Fe.

3 I represent Doyle Hartman. I
4 have one witness.

5 MR. LEMAY: Any other appear-
6 ances?

7 MR. KELLAHIN: Mr. Chairman,
8 I'm Tom Kellahin of Santa Fe, New Mexico, appearing on be-
9 half of Tenneco Oil Company.

10 We also would like to reserve
11 the right to call a witness if we feel necessary.

12 MR. PEARCE: May it please the
13 Commission, I am W. Perry Pearce of the Santa Fe law firm of
14 Montgomery and Andrews.

15 I appear in the this matter on
16 behalf of Amoco Production Company.

17 MR. LEMAY: Do you have any
18 witnesses, Mr. Pearce?

19 MR. PEARCE: I do not expect to
20 have any witnesses, Mr. Chairman.

21 MR. LEMAY; You'll have a
22 statement at the end?

23 MR. PEARCE: I may very well
24 have a statement.

25 MR. DUKE: Mr. Chairman, I'm

1 Jonathan Duke of the Keleher Firm in Albuaquerque, represen
2 ting Gas Company of New Mexico.

3 We don't anticipate having a
4 witness but we would like to reserve the right to comment.

5 MR. LEMAY: Okay.

6 MR. STRAND: Mr. Chairman,
7 Robert H. Strand, of the firm of Atwood, Malone, Mann and
8 Turner, in Roswell, and I will be representing Alpha Twenty-
9 One Company, and the Independent Petroleum Association of
10 New Mexico.

11 We will not have any witnesses
12 but I would like to make a statement.

13 MR. LEMAY: I'll call for
14 statements after all the testimony.

15 Yes, in the back there.

16 MR. HALL: Mr. Commissioner,
17 Scott Hall from the Campbell & Black law firm, entering an
18 appearance on behalf of Blackwood and Nichols Operating Com-
19 pany, UniCal Corporation, Union Texas Petroleum, and Yates
20 Petroleum.

21 MR. LEMAY: Mr. Padilla.

22 MR. PADILLA: Mr. Chairman, my
23 name is Ernest L. Padilla of the law firm of Padilla and
24 Snyder.

25 I represent John Hendrix Cor-

1 poration and Michael Klein, and we will be making a comment.

2 MR. LEMAY: Do you have any
3 witnesses?

4 MR. PADILLA: No witnesses.

5 MR. LEMAY: Do you have any
6 witnesses, Mr. Hall?

7 MR. HALL: No, Mr. Chairman.
8 We might offer some comments towards the end of the hearing.

9 MR. DRAPER: Mr. Chairman, Del
10 Draper, representing Northwest Pipeline Corporation.

11 We'd like to reserve the right
12 to call a witness.

13 MR. LEMAY: Okay. Are there
14 any other appearances? Yes.

15 MR. MORGAN: Mr. Chairman, Den-
16 nis Morgan on behalf of Southern Union Exploration Company.

17 We have no witnesses but we
18 would like to reserve the right to call a witness at a later
19 time.

20 MR. LEMAY: Are there any other
21 appearances?

22 At this time I'd like to swear
23 in all the witnesses. Those that will give testimony please
24 stand.

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(Witnesses sworn.)

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MR. LEMAY: Mr. Taylor.

MR. TAYLOR: Mr. Chairman, I'll
call Mr. Vic Lyon.

Just for the information of the
Commission I'd like to state that this case has been heard
previously by the Commission, Case 8015, on priority
production schedule, I believe on Octobr 23rd and November
20th there was testimony on this, although because the
Commission members have changed and because, I believe, the
Committee has met and reconsidered some of the aspects of
the case, we're going to at least summarize what's gone on
to this point in time.

VICTOR T. LYON,
being called as a witness and being duly sworn upon his
oath, testified as follows, to-wit:

DIRECT EXAMINATION

BY MR. TAYLOR:

Q Would you please state your name, your
position, and your residence for the record?

A I'm Victor T. Lyon, Chief Petroleum En-
gineer for the Oil Conservation Division, located in Santa
Fe.

1 Q Mr. Lyon, just for the record, although
2 most of us know you and your qualifications, would you
3 briefly state your educational and work experience,
4 especially as it relates to natural gas production and pro-
5 rationing?

6 A I took an -- excuse me, a BS degree in
7 general engineering, University of Oklahoma, 1945, -- it's
8 been so long ago I almost forgot -- and an MBA from Eastern
9 New Mexico University in 1975.

10 I was employed by Conoco for 39-plus
11 years, working primarily in the field of oil and gas
12 regulation, conservation.

13 I began working in New Mexico in 1953 and
14 served on the original committee which wrote the first gas
15 proration rules in New Mexico, and served on committees
16 which revised those rules from time to time.

17 I was responsible for gas prorationing
18 for Conoco during most of that time and I retired from
19 Conoco and joined the OCD approximately one year ago.

20 I am a registered professional engineer
21 in New Mexico, Oklahoma, and Texas.

22 Q So I think we could safely say you've had
23 substantial experience in the area of gas prorationing and
24 production.

25 MR. TAYLOR: I would tender the

1 witness as an expert, Mr. Chairman.

2 MR. LEMAY: His qualifications
3 are considered acceptable.

4 Q Mr. Lyon, you've previously testified
5 before the Commission on this case, have you not?

6 A Yes, I have.

7 Q Could you briefly explain how -- what has
8 been presented on this case previously to the Commission?

9 A Well, there has been in existence for
10 some time a memorandum establishing priorities for the tak-
11 ing of gas in the state.

12 I previous director, Mr. Stamets, felt
13 that it might be appropriate to -- to revise that, or to
14 promote that schedule to the status of a part of the general
15 rules, and so we had proposed some rules for that. They
16 were discussed at the October and the November hearings.
17 They have been discussed by committees and following the
18 last hearing in November there was a committee which was ag-
19 gregated to study several gas issues including the priority
20 schedules and that committee met December 16th, I believe it
21 was, and reviewed the priority schedule, adopted a revised
22 priority schedule, and there was discussion at that hearing
23 as to what form the priority schedule should take, whether
24 it should be another memorandum signed by the director, or
25 an order by the Division, since certainly there have been

1 hearings and adequate record to support such an order,
2 or whether they should be adopted in the form of amended
3 general rules.

4 Q What was the -- well, first, Mr. Lyon,
5 you are a member of this committee, do you have a list or
6 could you provide us with a list with the members that
7 served us on this committee that made the recommendations?

8 A Well, it's a pretty good sized one. One
9 reason that this committee is so large is that the committee
10 for long term solutions to the gas marketing problems is
11 rolled into this and the membership is James Allen with
12 Amoco, David Boneau with Yates, William Clark with Blackwood
13 and Nichols, Warren Curtis with Northwest Pipeline, Dave
14 Dupre, Union Texas Petroleum, Bill Duncan of Exxon, Bill
15 Gallagher with Chevron, Marta Henderson with ARCO, John
16 Hendrix, H. A. Ingram with Conoco, Louis Jones with Tenneco,
17 Al Kendrick, Consultant, Babe Kendrick with El Paso, Randy
18 Lukken with Northern Natural, myself as chairman, Buster
19 Orbison with Gas Company of New Mexico, Don Read with
20 Meridian, Ernie Padilla, Larry Sanders with Phillips, Bob
21 Strand with the Atwood firm, Jeff Taylor, Darwin Vandergraaf
22 with the New Mexico Oil and Gas Association, and Bob
23 Wehmeyer with Texaco.

24 We also have some alternates in there if
25 you'd like me to read those, too.

1 Rather than have multiple members from
2 the same company, any additional people that they wished to
3 put on there, I've put on as alternates.

4 Q Okay, and was the -- when that committee
5 met, was the rule that's proposed in the -- the memorandum
6 that went out to gas producers, purchasers, and transpor-
7 ters, does that reflect the recommendations of that commit-
8 tee, the language in that memorandum?

9 A Now which memorandum is that? Yes, this
10 is the memorandum that was adopted by the committee. I mean
11 this is the priority schedule that was adopted by the com-
12 mittee.

13 Q Let's first focus on Part A of this so
14 that we can separate these and get the feelings on each part
15 of it.

16 Would you please explain Part A of the
17 proposed rule, the reason for each category having a prior-
18 ity assigned to it and how the rule is generally supposed to
19 operate?

20 A Under this memorandum it explains that it
21 was suggested that this be retained as a memorandum by the
22 Director for the time being and the following language has
23 been proposed to be included in the memorandum and/or as
24 findings in the order, should it come out in the form of an
25 order.

1 To prevent the waste of gas which might result from the
2 shutting in or curtailment of certain wells in New Mexico,
3 the Priority Production Schedule outlined below is hereby
4 established.

5 Then there is also a preamble in there
6 that says, "In order for a seller of gas to enjoy the bene-
7 fit of the priorities established herein below," -- I might
8 point out this was not discussed by our committee, this was
9 added after that committee had met.

10 Q The preamble was not discussed by the
11 committee.

12 A If my memory serves me correctly.

13 Q So there is no recommendation by the com-
14 mittee on the preamble.

15 A Yeah. "... it may be necessary to sell
16 gas at market-clearing levels or other terms mutually accep-
17 table to the purchaser and the seller. This is not to be
18 interpreted in any respect as an interference or impediment
19 to existing contractual rights or an impairment of one par-
20 ty's rights to institute or maintain litigation over alleged
21 breaches of those contractual rights.

22 Any value paid and volumes taken may have
23 the effect of mitigating damages under such alleged
24 breaches.

25 Refusal to sell gas under current market

1 conditions is regarded as a decision not to mitigate damages
2 and also should not not impair an injured party's rights to
3 pursue recovery of damages in a court of law.

4 Such matters are not within the authority
5 of the Division. The Division's role is limited to preven-
6 tion of waste and protection of correlative rights by allo-
7 cating the gas market equitable between wells in a pool, es-
8 tablishing priorities of takes within each system and taking
9 appropriate action where a purchaser or a transporter is
10 discriminating unreasonably in the taking of gas between
11 pools or between wells in a pool."

12 Do you need me to read the priority sche-
13 dule?

14 Q Sure, why don't you read it and as you go
15 through each one explain why that is given priority and what
16 purpose it serves in the place it is on the priority sche-
17 dule?

18 A "To prevent waste, every person now en-
19 gaged or hereafter engaged in the business of producing,
20 transporting, purchasing gas from gas wells or casinghead
21 gas from oil wells, shall observes the following priority
22 production schedule:

23 (1) Gas from all wells designated under
24 a hardship classification by the Division under Rules 410,
25 411, or after hearing, shall have first priority."

1 And the reason this is given the highest
2 priority is that in order to secure such a classification,
3 the producer must have convinced the Commission that there
4 is a high probability of waste occurring should that well be
5 curtailed or shut in, or shut in or curtailed below the min-
6 imum flow rate which is established by the Commission's or-
7 der.

"(2) Casinghead gas from Division approved waterflood, pressure maintenance, or certified tertiary recovery projects, shall have second priority."

11 And the reason this is given second
12 priority is that there is a serious question of waste should
13 those types of projects be curtailed.

14 And the alternative to preventing such
15 waste would -- would be to permit the flaring of gas, which
16 in itself is waste.

17 The third priority is casinghead gas and
18 the reason for this is that if casinghead gas is not taken
19 our oil wells will have to be curtailed or we will have to
20 permit the flaring of gas, which is wasteful.

21 There isn't any surplus of oil and every
22 barrel of oil that we do not produce here is going to have
23 to be imported; therefore, we -- I think that that demon-
24 strates the need to protect casinghead gas.

"(4) Gas from downhole commingled wells

1 involving one or more gas zones and one or more oil zones
2 shall have fourth priority.

3 (5) Gas from wells classified as gas
4 wells in associated pools shall have fifth priority.

5 And (6) gas from wells in non-associated
6 pools shall have sixth priority."

7 Q Just briefly, I understand that the
8 reason the gas wells in non-associated pools is last is be-
9 cause there is little chance of waste. If that's produced
10 last, what are the reasons for (4) and (5) being placed in
11 the order they are?

12 A Well, (4) and (5) involves a mixture of
13 dry gas and casinghead gas and therefore it is given a lower
14 priority than casinghead gas but a higher priority than dry
15 gas, and wells from associated pools, the allowable for
16 those wells is set by the allowable for the oil wells in the
17 same pool, and therefore there is a question of correlative
18 rights being impaired if the gas wells in there are -- are
19 not given a higher priority than dry gas.

20 Q From your testimony, then, I take it that
21 the purpose of the rule is primarily to prevent waste in
22 periods of low demand for gas.

23 A Yes, that's true.

24 Q Is it your professional opinion that pur-
25 suant to the mandates given to the Oil Conservation Commis-

1 sion to conserve oil and gas, that Section A is a reasonable
2 method by which to prevent waste and protect correlative
3 rights in times of extremely low gas demand?

4 A Yes, I certainly do.

5 Q Do you recommend adoption of Part A of
6 the rule?

7 A Yes, I do.

8 Q I guess I have some other general
9 questions but let's go on to the other parts of the rule
10 first and have you explain those.

11 Would you explain Section B of the rule
12 for us?

13 A Section B has also been added since our
14 committee met in December and it states, "Any gas transpor-
15 ter connected to a well, lease, or field facility, which
16 transporter provides transportation to the spot market shall
17 provide an affiliate or associate marketing service. Such
18 marketing service shall provide the opportunity for sale of
19 gas from wells in the above priority schedule from the
20 highest to the lowest to the extent of available demand."

21 And Section C says, "The schedule shall
22 be observed by giving all highest priority gas an opportuni-
23 ty to produce before giving gas with the next highest
24 priority the opportunity to produce, and so on throughout
25 the priority schedule until the demand for gas is met.

1 In the schedule listed above the lowest
2 priority is number (6) and the highest is number (1)."

3 Q What is the purpose of Section B?

4 A Well, the purpose of Section B is to as-
5 sist those producers who are at a disadvantage in marketing
6 their gas. I don't think that this is needed by the major
7 companies and probably most of the larger independents, but
8 we are very concerned about the small independents who have
9 low capacity wells, such that they cannot present for con-
10 sideration by a prospective purchaser a large enough package
11 to raise any interest by that purchasers, and if -- it's my
12 concern that those people are so disadvantaged that certain-
13 ly their correlative rights are likely to suffer and it may
14 cause the premature abandonment of wells if they're not
15 given this assistance.

16 Q Just to venture into dangerous territory
17 here, have you read the Transco decision?

18 A Yes, sir.

19 Q And have you considered what the impact
20 of that decision may be on the authority of the State to re-
21 quire a transporter, particularly an interstate transporter,
22 to provide an affiliate marketing service?

23 A Well, I have given consideration to that.
24 I've also given consideration to the fact that in most, if
25 not all, these cases, there is a contract between the pur

1 chaser or between the transporter and the producer, and I
2 don't think Transco changed that contract. And if I'm not
3 mistaken, that contract says that that transporter agrees to
4 purchase that gas.

5 Q Insofar as the Federal Energy Regulatory
6 Commission has also recently instituted an investigation in-
7 to affiliate transactions of affiliate companies of pipe-
8 lines, do you know if anyone has looked into the possibility
9 that a rule such as this at the State level may conflict
10 with FERC rule making at the Federal level?

11 A I have not seen any such opinion. I have
12 not heard such an opinion, but I'm sure that I probably
13 will.

14 Q Although there apparently has not been a
15 rule like this before in the Division, has there a policy or
16 other method by which the Commission has sought to prevent
17 the waste envisioned by this rule?

18 A Well, this proposed rule arises out of --
19 out of the tremendous changes that have come about in the
20 gas production and marketing, transporting business.

21 Back in the days a year or less ago we
22 didn't have to deal with a separate -- with a transporter
23 and a purchaser separately because they were the same. The
24 splintering of those functions has brought a great deal of
25 chaos to the -- to the industry and it has got to the point

1 we really don't know in most cases who the purchaser is.

2 Q Well, since we're getting into it, then,
3 let me ask you how this would -- how this rule would apply
4 to gas purchasers with affiliated companies that separately
5 purchase gas?

6 A Well, if -- if the -- if the purchaser is
7 an affiliate of the transporter, then we know who we're
8 dealing with and can act as best we can with whatever
9 authority we have to -- to enforce the priority schedule.

10 Q And in that situation would the transpor-
11 ter and the affiliate purchaser be treated as one entity for
12 purposes of considering whether or not they were complying
13 with this rule?

14 A I would think so.

15 Q Let's get into another good one here,
16 would the rule apply to the pipeline or purchaser -- let me
17 start again.

18 How would this rule apply to a transpor-
19 ter who was purchasing no gas himself but was transporting
20 on behalf of, say, twenty different purchasers?

21 Would the rule apply to the pipeline or
22 the purchasers and how would the Division police purchasers,
23 say, in California? Could the Division require those pur-
24 chasers to take casinghead gas if they had contracted only
25 for high volume gas well production?

1 A I think -- I think the only control we
2 would have over purchasers in California is the control of
3 the wells themselves through the producers.

4 Q And so in a situation like that you would
5 say that the Division would control, production would come
6 down -- control would come down to producers.

7 A Right.

8 Q I assume in a situation like that the
9 Division would require the shut-in of all, say, non-casing-
10 head, non-hardship wells till they are producing and let
11 then let the other wells come on?

12 A Right. I hope it never comes to that.

13 Q Has the committee -- well, I guess the
14 committee didn't do it -- what is the purpose of the pre-
15 amble before paragraph A?

16 A Well, the purpose of that preamble before
17 paragraph A is our recognition of the law under Transco.
18 I'm sure that there has been a great deal of effort put into
19 producers to ask us to require the pipelines to take the gas
20 and honor their contract. In dealing with regulating gas,
21 gas production, gas purchases and transportation, the OCD
22 must remain price neutral, and I do not think that we
23 should, and under Transco I do not think we can, force a
24 transporter or purchaser to take gas at a specified price,
25 and so in order to make that perfectly clear, I think a pro-

1 ducer has -- has an option of producing his gas or not pro-
2 ducing his gas, and if he produces his gas he's going to
3 have to produce it and sell it at a price which is agreeable
4 to the people that take the gas.

5 Q I find this, the preamble, just a little
6 either confusing or ambiguous. Do you think it would be
7 sufficient if the language either in the rule or in the or-
8 der which stated something to the effect that the rule was
9 limited to situations where the cost of the gas ordered to
10 be taken did not exceed the pipeline's average of gas, or
11 something in there which would mitigate the requirement to
12 take high cost gas, which under the Transco case the Supreme
13 Court said the state agency can't require a pipeline to take
14 high cost gas which would increase the cost of that pipe-
15 line's gas to consumers?

16 A I think that if we put that in there it
17 would impair some of the contracts that are currently being
18 honored. I understand that -- that there are some contracts
19 that are being honored which are above their average --
20 weighted average cost of gas, and if that is a mutually
21 agreeable situation with those people, I do not intend to
22 interfere with it.

23 Q Do you then think that it might be appro-
24 priate to have no language in there regarding price require-
25 ments when the rule is being enforced?

1 Or do you recommend the adoption of the
2 preamble?

3 A I'm satisfied with it the way it is.

4 Q I think that's all the questions I have.
5 Do you have anything further to add to your testimony?

6 I guess I should ask you, you said that
7 the -- the committee that met on this did not consider the
8 preamble, so I assume that your recommendation on the pre-
9 amble is one by the Division rather than the committee that
10 met.

11 A That is correct.

12 Q What the committee met and recommended, I
13 guess, as a concensus, the adoption of paragraph A. Did
14 they also recommend the adoption of paragraphs B and C?

15 A No. Well, they -- they did recommend
16 paragraph C.

17 Q Okay, so the committee recommended the
18 adoption of paragraphs A and C and the Division is in addi-
19 tion recommending the adoptions of the preamble and para-
20 graph B?

21 A That's correct.

22 Q Do you have anything further to add to
23 your testimony?

24 A Well, the committee did not make a deci-
25 sion on the form that the priority schedule should take and

1 we agreed to leave that open pending presentation by Amoco
2 who was the one who suggested that -- that we re-issue the
3 priority schedule under a memorandum. They mention that
4 their Legal Department felt that this had virtually the same
5 weight under the law as -- as an order or general rule, and
6 I told them to show me, and so they said they would do that
7 and that's the reason we left that particular alternative
8 in.

9 Q But I take it that it's the Division's
10 recommendation that this be adopted either as an order or a
11 rule.

12 A Yes, sir.

13 Q Okay, thank you.

14 MR. LEMAY: Are there any ques-
15 tions of Mr. Lyon?

16

17 CROSS EXAMINATION

18 BY MR. LEMAY:

19 Q Mr. Lyon, I have a question concerning
20 the price issue.

21 The Division policy has always been, as I
22 take it, that the price has never been addressed as an is-
23 sue. It's always been a contractual right between purchaser
24 and seller, is that correct?

25 A Yes, that's true, although the ratable

1 take statute provides price as one of the things which we
2 should look at as far as ratable take.

3 We have been living with enforced differ-
4 ences in prices ever since 1956 because of price, prices set
5 for gas, the vintaging of gas categories since 1956, and to
6 a much greater extent in 1978 under NGPA.

7 So the price situation is so screwed up
8 there's no way that we can find any discrimination on that
9 because so much of it is mandated.

10 Q Thank you.

11 MR. LEMAY: Any other questions
12 of Mr Lyon?

13 MR. KELLAHIN: Mr. Chairman.

14 MR. LEMAY: Mr. Kellahin.

15

16 CROSS EXAMINATION

17 BY MR. KELLAHIN:

18 Q Mr. Lyon, the back of the docket page that
19 discussed the priority schedule has a list of four ques-
20 tions. Do you have a copy of that schedule?

21 A Yes, sir.

22 Q Starting with the first question, looks
23 like it calls for a legal opinion, but I've not known an en-
24 gineer yet that was reluctant to give a legal opinion, so
25 I'll ask you anyway, what is your opinion with regards to

1 whether or not the priority schedule ought to be in the form
2 of a memorandum as it exists now as opposed to making it an
3 order or a rule of the Commission?

4 A Well, Mr. Kellahin, so long as everybody
5 complies with it, it doesn't make any difference, but if
6 somebody doesn't comply with it and we try to enforce it, I
7 think it does make a difference, and I think that a memoran-
8 dum over the Director's signature does not bear the weight
9 in a court of law that an order after testimony and hearing,
10 or a general rule after testimony and evidence, would be.

11 Q Turning to the second question, what is
12 your opinion with regards to the priorities on the asso-
13 ciated pools that produce gas?

14 A I really haven't given any thought to
15 that, Mr. Kellahin.

16 Q Is this your question, then, in the memo-
17 randum, Mr. Lyon?

18 A No, it isn't.

19 Q All right. Is there any particular
20 reason to give a special priority to only certain oil and
21 gas pools that produce oil and gas as opposed to all asso-
22 ciated gas pools?

23 A I'd have to do a little research on it to
24 give you an opinion on it.

25 Offhand, I don't know of any.

1 Q I'm at a loss to understand the question,
2 I guess. What's the purpose of this question?

3 A Well, there are -- there are two pools in
4 the state which are designated oil and gas pools and I was
5 responsible for creating one of them, but it's been a long
6 time since I've looked at those rules. I just don't feel
7 like I'm qualified to give you a very intelligent answer
8 right now.

9 Q Is it your understanding that under the
10 proposed priority schedule that the Tubb and Blinbry Oil and
11 Gas Pools would in the associated gas pool category?

12 A Well, they are an associated pool but
13 they're not designated exactly as associated pools. It's
14 just oil and gas pools.

15 Q So that's part of the question, to deter-
16 mine whether or not the Tubb and Blinebry oil and gas pools
17 are going to fall within the priority for the associated gas
18 -- associated pool gas rules.

19 A Yes, sir.

20 Q The third question deals with whether or
21 not underproduced or low capacity gas wells are going to re-
22 ceive a priority and I assume that the answer is that they
23 should not, because we already have a proration formula that
24 allows the operator to determine how he would produce his
25 underproduced and overproduced wells. Is that not correct?

1 A Well, the priority schedule that the com-
2 mittee adopted was modified only slightly from a schedule
3 that was presented by Phillips and the modification was that
4 under category (6) there was a priority given to underpro-
5 duced or marginal wells.

6 When we were reviewing this, although we
7 feel that there is probably reason to give that kind of a
8 priority, there is not a question of waste involved there
9 and it was therefore recommended that we drop that priority.

10 Q And do you share that opinion or recom-
11 mendation that there should be no priority established be-
12 tween underproduced or low capacity wells versus nonmarginal
13 wells?

14 A My own personal view is that there should
15 be a priority given to underproduced and marginal wells.

16 Q The fourth question is that the -- is the
17 priority schedule in the correct order, and I assume you've
18 already answered that question, in your opinion it is?

19 A Yes.

20 Q With regards to the underproduced wells,
21 the -- is it your recollection that the consensus of the
22 study committee was that they would not make a distinction
23 between underproduced wells and normal gas wells?

24 A That's my recollection, yes, sir.

25 Q And part of the reasoning for doing that,

1 was it not, that that would be left up to the discretion of
2 the operator, how he would produce his wells?

3 A Right.

4 Q And part of that problem is addressed in
5 the prorationing rules now in terms of keeping wells in
6 balance and how far they're underproduced or overproduced.

7 A Correct.

8 Q So those were some of the reasons why we
9 -- for which that priority was not set forth in the rule.

10 A Right. Also, it was -- I think it was
11 discussed that most of the pipeline companies do give a
12 higher priority to those wells and that it wasn't necessary
13 for us to address it the -- in the order or the priority
14 schedule itself.

15 Q Do you believe that to be a reasonable
16 solution?

17 A Yes.

18 Q Thank you.

19 MR. KELLAHIN: Nothing further.

20 MR. LEMAY: Any other questions
21 of Mr. Lyon?

22

23 CROSS EXAMINATION

24 BY MR. DUKE:

25 Q Mr. Lyon, SubSection C states that the

1 schedule shall be observed by giving all highest priority
2 gas an opportunity to produce.

3 Let me ask you first of all, what does it
4 mean to give an opportunity to produce; is this an oppor-
5 tunity to --

6 A We give it an allowable.

7 Q Okay, at a spot market price or a (un-
8 clear) price?

9 A Well, we give it an allowable. We don't
10 set prices.

11 Q In your opinion do you think that any
12 consideration should be made for system constraints, for in-
13 stance, on casinghead gas that enters the system below pro-
14 cessing plants as far as compliance with these priorities?

15 A Well, I'm not sure what you're -- what
16 the constraints are.

17 Q Well, in --

18 A Certainly we've got to recognize the
19 physical facts and the infrastructure available and break-
20 downs, and that sort of thing.

21 Q Well, let me give you an example. If
22 casinghead is introduced into a gas supply system down
23 stream from processing, and could create a (not understood),
24 should that be taken into consideration?

25 A Well, if it -- if you collect liquids to

1 the point you can't run gas through there, I guess we've got
2 to recognize you can't run gas through there.

3 MR. DUKE: I don't have any
4 other questions.

5 MR. LEMAY: Any other questions
6 of Mr. Lyon?

7

8 RECROSS EXAMINATION

9 BY MR. LEMAY:

10 Q I have one, Mr. Lyon. Do you see any
11 reason why unique situations that may be unique in certain
12 fields might be the subject of an Examiner or a Commission
13 hearing in which these unique situations could be addressed?

14 And I give you an example, where there --
15 that was just mentioned, where you had a situation where a
16 purchaser could not take gas in a certain situation and it
17 was a high priority gas, if that could be the subject of a
18 hearing, or if some field is unique enough that there may be
19 a classification of casinghead gas that isn't truly casing-
20 head gas, that could be the subject of a hearing? What I
21 guess I'm asking is, because this is a general rule, would
22 we have the same -- do we have the same policy that any ex-
23 ceptions could be handled with hearings?

24 A Well, I think if a purchaser or transpor-
25 ter has -- has problems where he's prevented from abiding by

1 the priority schedule, certainly he can come in and talk to
2 us or he can ask for a hearing and exceptions, and explain
3 the situation, and also I think if we find through com-
4 plaints or through our own investigations that people are --
5 are willfully abusing the priority rules, then certainly we
6 should call those people to explain and in severe cases call
7 them to -- to a hearing to explain why this happening.

8 Q Thank you, Mr. Lyon.

9 MR. PEARCE: May I, Mr. Chair-
10 man?

11 MR. LEMAY: Mr. Pearce.

12

13 CROSS EXAMINATION

14 BY MR. PEARCE:

15 Q Mr. Lyon, I want to go back over a couple
16 of things ot make sure I understand them. I was not part of
17 the committee process and I do want to understand before I
18 get into anything else.

19 As I understand it, after the last set of
20 hearings, the committee held another meeting and recommended
21 that the priority schedule shown in paragraph A of the pro-
22 posed rule be adopted and be utilized as a memorandum and
23 not adopted as a rule, is that correct? Was that the com-
24 mittee's recommendation?

25 A No. The committee did not have a recom-

1 mendation as to what form it should take.

2 Q Okay.

3 A We had those three alternatives.

4 Q The committee established the suggested
5 priority schedule and subsequent to the committee's work the
6 preamble, the long paragraph at the front, and paragraphs B
7 and C, have been added, is that correct?

8 A That's correct.

9 Q Okay, I want to look for a minute at the
10 relationship between paragraphs A and C. Do you know what
11 the penalties for violation of Division rules or the Oil
12 Conservation Act are, the maximum penalty?

13 A As I recall, it's \$1000 a day.

14 Q And SubPart A would you're proposing be
15 adopted in a rule or set forth in an order of this Division
16 prioritizing the takes of gas, is that correct? (sic)

17 A Yes, sir.

18 Q And SubPart C of the proposed rule re-
19 quires that all of the higher priority gas be taken before
20 the next lower priority gas is taken, is that correct?

21 A Yes, sir.

22 Q Are you aware that the New Mexico Oil and
23 Gas Act in its definition of waste finds that the production
24 of natural gas in excess of reasonable market demand is
25 waste? Are you familiar with that definition?

1 A Yes. Yes.

2 Q Therefore would it be a violation of the
3 Oil and Gas Act or the Oil Conservation Division rules and
4 regulations to produce more gas than was required to meet
5 reasonable market demand?

6 A Yes, other than for storage purposes.

7 Q Therefore would production of lower
8 priority gas before production of all of the higher priority
9 gas be a violation of New Mexico Oil Conservation Division
10 and Commission rules and regulations if this rule is
11 adopted?

12 A Yes, I think that's what the rule says.

13 Q And the party could be subject to a fine
14 of \$1000 a day for that violation?

15 A Could be, yes, sir.

16 Q And I want to clarify my understanding of
17 subparagraph B.

18 As I read paragraph B it would require
19 any transporter who transports gas to the spot market to
20 provide a marketing service to all of the producers in the
21 state, is that correct?

22 A The ones that he's connected to, yes.

23 Q Whether or not they are under contract to
24 him.

25 A That's what the rule says, yes.

1 have a proration unit for the oil, a proration unit for the
2 gas, is that correct?

3 A That's right.

4 Q Now this category (5) only applies to
5 wells that are classified as gas wells and that are -- or
6 that have a proration unit for gas.

7 A Right.

8 Q It does not intend to amend or modify the
9 Division's rule on the definition of casinghead gas, is that
10 --

11 A No, the oil proration units in an asso-
12 ciated pool would be covered under the casinghead gas cate-
13 gory.

14 Q Okay.

15 A And the gas wells would come under the
16 next priority so that if push came to shove, you would have
17 to take the casinghead gas before you took the dry gas out
18 of the associated gas pool.

19 Q But assuming an associated pool calls for
20 40-acre spacing for gas and, say, 160-acre spacing for the
21 gas well, category (5) only applies to gas wells that are
22 spaced on 160 acres.

23 A Well, unless there's a nonstandard unit
24 in there, I can see that that --

25 Q Well, subject to that kind of exception.

1 A Yes.

2 MR. PADILLA: No further ques-
3 tions.

4 MR. LEMAY: Any other --

5 MR. TAYLOR: I have a clari-
6 fying question.

7

8 REDIRECT EXAMINATION

9 BY MR. TAYLOR:

10 Q I thought, Mr. Lyon, that you responded
11 to a question by Mr. Pearce that paragraphs B and C were not
12 recommendations of the committee but I thought you told me
13 that C was a recommendation.

14 Could you clarify that for me?

15 A Oh, I may have misunderstood. Yes, the
16 paragraph C was recommended by the committee.

17 Q Thank you.

18 MR. LEMAY: Any other questions
19 of the witness?

20 If not, he'll be excused.

21 MR. HALL: One comment. Mr.
22 Pearce raised a question with respect to paragraph B and its
23 possible application on a statewide basis.

24 It might not -- I wonder if it
25 might not cure the problem if we were to add at the end of

1 the first sentence of paragraph B the following language,
2 simply "in any pool served."

3 MR. LEMAY: Are you recommen-
4 ding, Mr. Hall, that that be portion of paragraph B?

5 MR. HALL: Yes.

6 MR. LEMAY: In any pool served,
7 and that would limit the purchaser from, say, ratable takes
8 within the pool only and not extending to the statewide?

9 MR. HALL: That might clarify
10 that.

11 MR. LEMAY: Okay. Yeah, we
12 could certainly look at that.

13 Any other questions of the wit-
14 ness?

15 If not, he can be excused.

16 Is it my understanding that you
17 were going to present a witness, Mr. Nance?

18 MR. NANCE: No, sir. El Paso
19 won't present a witness.

20 MR. LEMAY: Oh, not presented.

21 Are there any other witnesses?

22 I thought there was one other. Mr. Carr?

23 MR. CARR: Mr. Lemay, at this
24 time on behalf of Doyle Hartman I'd like to call Dan Nutter.

25 MR. LEMAY: Mr. Carr.

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DANIEL S. NUTTER,
being called as a witness and being duly sworn upon his
oath, testified as follows, to-wit:

DIRECT EXAMINATION

BY MR. CARR:

Q Will you state your full name for the re-
cord, please?

A Dan Nutter.

Q Mr. Nutter, by whom are you employed?

A I'm a consulting petroleum engineer em-
ployed in this particular case by Mr. Doyle Hartman, oil
operator.

Q Mr. Nutter, would you briefly summarize
for the Commission your educational background and your work
experience?

A Yes, sir. I graduated from the New Mexi-
co School of Mines in January, 1952.

Subsequent to graduation I was employed
by Phillips Petroleum Company as a staff petroleum engineer.
I stayed with Phillips until August of 1954.

Came to work for the New Mexico Oil Con-
servation Commission on September 1st, 1954 and remained
with the Commission until my retirement on December 31st,

1 1982.

2 At first with the Commission I was a
3 staff petroleum engineer. In I believe it was 1957 I was
4 appointed Chief Engineer and remaining that capacity until
5 my retirement.

6 Q Mr. Nutter, are you familiar with the
7 priority schedule set forth in Oil Conservation Commission
8 Case 9015?

9 A Yes, I am.

10 MR. CARR: Mr. Lemay, at this
11 time we'd tender Mr. Nutter as an expert witness in petro-
12 leum engineering and oil and gas regulatory matters.

13 MR. LEMAY: Mr. Nutter is so
14 qualified.

15 Q Mr. Nutter, would you briefly state the
16 purpose of your testimony here today?

17 A The purpose of my testimony is recommend
18 to the Commission that this priority production schedule not
19 be adopted as a rule in the rules and regulations of the
20 Commission.

21 Q Mr. Nutter, have you prepared certain ex-
22 hibits for introduction in this case?

23 A Yes, I have.

24 Q Would you refer to what has been marked
25 for identification as Hartman Exhibit Number One, identify

1 this, and review it for the Commission?

2 A Hartman Exhibit Number One is a memoran-
3 dum to all operators and all gas purchasers for Joe Ramey,
4 Division Director, dated February 18, 1983.

5 The subject of this memorandum is priori-
6 ties of gas production and purchases.

7 Q Would you review the priorities as set
8 forth in this memorandum?

9 A Yes, sir. The memorandum states, "During
10 periods of low demand for New Mexico gas, the following cur-
11 tailment schedule should be observed.

12 1. Overproduced nonmarginal and high
13 capacity nonprorated gas wells.

14 2. Nonmarginal gas wells.

15 3. Marginal and low capacity nonprorated
16 gas wells.

17 4. Exempt marginal gas wells.

18 5. Casinghead gas.

19 6. Gas wells which will be damaged by
20 being shut-in or will require swabbing to produce after
21 being shut-in."

22 Q Now, Mr. Nutter, in your opinion does
23 Item Number Six on Exhibit One address hardship wells?

24 A Yes, sir, that's what a hardship well is.
25 I think hardship wells were defined subsequent to this memo-

1 random, so --

2 Q And this is the original memorandum is-
3 sued by the Division Director in 1983 setting a recommended
4 priority procedure?

5 A This is the first and only priority sche-
6 dule for curtailment that has ever been issued to my know-
7 ledge by this Division or Commission.

8 Q Will you now refer to what has been mar-
9 ked as Hartman Exhibit Number Two, identify this, and review
10 it for the Commission?

11 A Exhibit Number Two is a combination of
12 several Notice to Sellers issued by El Paso Natural Gas Com-
13 pany.

14 The first one in the stack here is dated
15 May 29, 1986, a Notice to Sellers.

16 The second one in here is a Notice to
17 Sellers dated February 28, 1986. This directive was--was
18 sent by El Paso to the people that produce gas and sell gas
19 to El Paso Natural Gas Company.

20 Q Now what is your purpose in including
21 these Notices to Sellers in your presentation here today?

22 A If you'll look at page 1 of the May 29,
23 1986 notice, down there in the last three lines it says, "As
24 used in this notice" -- first of all they say that they've
25 scheduled their takes from the lowest cost swing pools after

1 taking the gas from all non-swing sources.

2 Quote, as used throughout this notice,
3 the terms 'non-swing gas' and 'non-swing sources' include:

4 (1) Hardship or emergency gas.

5 (2) Casinghead or associated gas.

6 Then it lists (3) being residue gas, (4)
7 certain downhole commingled gas, (5) gas received at central
8 points of delivery, and (6) gas taken pursuant to certain
9 contractual minimum physical take provisions.

10 The memorandum of -- or the Notice to
11 Sellers dated February 28, on page 8, the second paragraph
12 there down in the lower portion of the page, says, "Under
13 its new production scheduling procedures El Paso expects
14 that it will continue to purchase without curtailment its
15 non-swing supplies (i.e. gas produced in association with
16 oil and gas produced from hardship or emergency wells)."

17 Q Now, Mr. Nutter, in your opinion what do
18 these Notices to Sellers show?

19 A These Notices to Sellers indicate to me
20 that despite the fact that there is no rule in the rules and
21 regulations of the Division, El Paso Natural Gas Company, as
22 a major purchaser of natural gas in the State of New Mexico,
23 has observed the memorandum that's in effect since February
24 18th, 1983.

25 This further confirms in my mind the

1 opinion that no rule is necessary.

2 Q Mr. Nutter, would you refer to Hartman
3 Exhibit Number Three, identify that and review it for the
4 Commission?

5 A Exhibit Number Three is a reproduction of
6 page 28 of the Section I of the R. W. Byrum rule book. This
7 page is dated April, 1986.

8 It shows Rule 902 in the upper lefthand
9 portion of the page. Rule 902 is named Ratable Take, and
10 you will notice at the end of the first long paragraph
11 there, the provisions of this subsection shall not apply to
12 any wells or pools used for storage and withdrawal from
13 storage of natural gas originally produced not in violation
14 of the rules, regulations, or orders of the Division.

15 Two, to persons purchasing gas principal-
16 ly for use in the recovery or production of oil or gas; or
17 Three, to any well which has been designated a hardship well
18 by the Division.

19 Now, in 1983 this statute -- Paragraph A
20 of Rule 902 is taken almost verbatim from the statute on
21 ratable take. I believe it's 70-2-19, if I remember cor-
22 rectly.

23 In 1983 that rule was amended by the
24 Legislature.

25 Those exceptions, which I just read, "The

1 provisions of this subsection shall not apply...", original-
2 ly also included casinghead gas, so casinghead gas was not
3 intended to be ratable. It was exempt from being taken rat-
4 ably with gas well gas.

5 Then the Legislature, in 1983, struck
6 that exemption so casinghead gas is required now to be taken
7 ratably under the statutes.

8 Q Now, Mr. Nutter, let's go back to hard-
9 ship for a minute. What is the effect, in your opinion, of
10 the inclusion of hardship wells in Rue 902?

11 A Well, the effect -- okay, before I get to
12 that, in 1984 this rule was amended to add (3) there to the
13 -- to the exceptions. The provisions of this subsection
14 shall not apply to any well which has been designated a
15 hardship gas well by the Division.

16 All right, in rule -- in 1984 that rule
17 was amended after the definition of a hardship well and af-
18 ter the adoption of rules for obtaining hardship classifica-
19 tion, so by inference the omission of casinghead gas from
20 the exemptions for the rule, the statute, and by listing
21 hardship gas by reference in the rule itself, you have
22 covered the two major considerations that are being attemp-
23 ted to be covered by this memorandum -- this proposed --
24 this proposed rule, hardship gas and casinghead gas.

25 Q In your opinion under existing rules, the

1 rules on hardship wells and also the ratable take statute set
2 out in Rule 902, is there a priority afforded the hardship
3 wells?

4 A Yes, there is.

5 Q In your opinion does the current status
6 of Section 70-1-19 and Rule 902 also afford a priority
7 situation for casinghead takes?

8 A They do and I think that the evidence by
9 the letters, by the Notice to Sellers, shows that those are
10 being observed by the pipeline companies.

11 Q Mr. Nutter, in your work as a consulting
12 engineer have you become familiar with gas purchase
13 agreements?

14 A Yes, I have.

15 Q Do those gas purchase -- have you become
16 familiar with purchase agreements which affect takes of
17 casinghead gas?

18 A Yes, I have.

19 Q How would they interreact with the Rule
20 902?

21 A Casinghead contracts invariably require
22 that that gas be taken under all circumstances.

23 Q And then with this rule providing for
24 ratable take of casinghead, what would the effect, in your
25 opinion, be?

1 A There's no requirement for any rule, or
2 even a memorandum, as far as that goes.

3 Q Now, Mr. Nutter, you've addressed in your
4 comments so far casinghead and hardship.

5 A Right.

6 Q You haven't addressed lower priorities as
7 set out on the proposed rule.

8 A No, I haven't. They have some lower
9 priorities here.

10 Q In your opinion are they in sufficient
11 detail that in fact a rule had to be adopted in this regard?

12 A I think it's a mistake to put all gas
13 wells in Item Number (6). Gas from wells in non-associated
14 pools shall have (6) priority. I think if you're going to
15 have a memorandum that details the priorities for shut-in or
16 curtailment, that it should be a lot more detailed as far as
17 gas wells are concerned.

18 One of the questions I heard asked ear-
19 lier of Mr. Lyon was whether marginal wells and low capacity
20 wells shouldn't be addressed, and I really think they should
21 be.

22 If you're going to have a memorandum, it
23 should be more detailed with regard to the size and capacity
24 of wells.

25 Q Now, Mr. Nutter, would you refer to what

1 has been marked as Hartman Exhibit Number Four and identify
2 that?

3 A Exhibit Number Four is Page 40 and 41 --

4 Q I think Exhibit Number Four, Mr. Nutter,
5 is the Page 21, the section of proration --

6 A Okay, okay, we'll get to that first.

7 Exhibit Number Four is Page 21, 22, and
8 23 from R. W. Byrum's rule books for the State of New Mexi-
9 co, and it covers the section relating to oil proration and
10 the depth bracket allowables, and gas/oil ratio limitations.

11 Q What's the purpose of including this in
12 your presentation?

13 A Just to demonstrate what the rules are
14 and how wells are classified and what the normal gas/oil
15 ratio is and how the gas/oil ratio is determined for casing-
16 head gas.

17 Q Mr. Nutter, would you now go to Exhibit
18 Number Five. That is the Page 40 and 41 are from the
19 special pool rules for the prorated gas pools of New Mexico.

20 Page 40 has the special rules and regula-
21 tions for the Eumont Gas Pool and in there it states that
22 the -- a gas well in the Eumont shall be a well producing
23 from the vertical limits of the pool with a gas/liquid ratio
24 in excess of 100,000 cubic feet of gas per barrel of oil,
25 and the limiting ratio, gas/oil ratio for oil wells in the

1 pool shall be 10,000 cubic feet of gas per barrel.

2 Any well that's not classified as a gas
3 well is -- any well not classified as a gas well is an oil
4 well.

5 Page 41 is the same thing for the Jalmat.
6 The classification is the same, and the gas/oil ratio limi-
7 tation is the same.

8 Q Now, Mr. Nutter, would you go to what has
9 been marked Hartman Exhibit Number Six, cross section D-D'?

10 A Cross section D-D' is a cross section.
11 The first page shows the line of the cross section, commen-
12 cing in Section 36 of Township 24 South, Range 36 East,
13 going into Section 30 of that township, of the next township
14 to the east, which would be 37, and ending in township -- in
15 Section 32 of Township 24, South Range 37 East.

16 These are wells in the Jalmat Gas Pool.
17 The first well on the cross section is an oil well. The
18 next three wells are gas wells and the last two wells to the
19 right are oil wells.

20 The gas well -- the oil wells presumably
21 are producing because they're making casinghead gas.

22 The second well on the cross section at
23 the time this cross section was made, was a Burleson gas
24 well and it was producing.

25 The middle two wells on the cross section

1 are gas wellss that are shut in, and the two oil wells to
2 the far right are presumably producing.

3 Q What are the exhibits behind the cross
4 section?

5 A These are tabulations of the production
6 from those various wells, going back a number of years.

7 Q And does this data just establish that
8 the oil wells are producing at rates in excess of the gas
9 wells?

10 A It shows that they're producing and that
11 certain gas wells are shut in, yes.

12 Q Mr. Nutter, will you go now to Exhibit
13 Number Seven and review that?

14 A Exhibit Number Seven is a similar cross
15 section. It covers four wells. The cross section starts in
16 Section -- it's in the Eumont Gas Pool. It starts in Sec-
17 tion 19 of 21 South, 36 East, with an ARCO oil well.

18 It proceeds southward to a Conoco oil
19 well in Section 30.

20 It then goes to two Hartman gas wells in
21 Section 30, and finishes up with a long oil well in Section
22 31 of Township 21 South, Range 36 East.

23 Here again we have gas wells that are
24 shut in and oil wells that are producing.

25 Q Now, Mr. Nutter, if the priority schedule

1 as proposed were adopted, the statewide rules require that
2 the oil wells continue to produce while gas wells offsetting
3 them should be shut in.

4 A That is correct.

5 Q In your opinion would adopting a state-
6 wide rule limit the flexibility the (unclear) operators
7 would have to deal with this kind of a problem on a pool by
8 pool basis?

9 A I think so. This demonstrates that there
10 is a problem and I think that by adopting a statewide rule
11 you're -- you might be relieving the producers of an oppor-
12 tunity to enforce their contracts and to stand up for their
13 rights as far as the sale and -- production and sale of gas
14 is concerned.

15 Q Now you stated that in your work as a
16 consulting engineer, you've become familiar with gas pur-
17 chase agreements.

18 A Yes.

19 Q How do these gas purchase agreements in-
20 terrelate with the state conservation rules and regula-
21 tions?

22 A Invariably they say that the gas the --
23 for the production and sale of gas it has to be in accor-
24 dance with the contract but subject to any state rules and
25 regulations.

1 Q And what in your opinion could be the ef-
2 fect of adopting a rule as that proposed here today?

3 A It provides further defense for the pipe-
4 lines to -- in their -- if there's litigation concerning the
5 abrogation of contracts by the pipelines.

6 Q Do you believe the preamble as proposed
7 by the Division and the rule proposal set forth in the doc-
8 ket would actually address that problem?

9 A No, I don't. I don't think it would at
10 all. It pretends to say, well, your contracts are still
11 there, but it would just be another defense for the pipe-
12 lines in litigation.

13 Q What do you recommend the Oil Conserva-
14 tion Commission do in regard to this proposal?

15 A Dismiss this case.

16 Q And --

17 A And just stand on the existing memoran-
18 dum.

19 Q Were Exhibits One through Seven prepared
20 by you or compiled under your direction and supervision?

21 A Yes, they were.

22 MR. CARR: At this time we
23 would offer into evidence Hartman Exhibits One through
24 Seven.

25 MR. LEMAY: So admitted.

1 MR. CARR: I have nothing fur-
2 ther on direct of Mr. Nutter.

3 MR. LEMAY: Are there any ques-
4 tions of Mr. Nutter?

5

6

CROSS EXAMINATION

7 BY MR. LEMAY:

8 Q I've got one, Mr. Nutter. Your examples
9 of Jalmat and Eumont, they, to my knowledge, are treated as
10 associated pools and yet there are classifications in there
11 of gas wells and oil wells.

12 With your history with the Commission can
13 you elaborate a little bit about those two pools as to why
14 they seem to go against the more commonly held definitions
15 of associated pools?

16 A Those pools are probably mistakes as far
17 as the Commission's regulation over the many, many years is
18 concerned.

19 They were originally developed as oil
20 pools with a few gas wells. Then in the very early fifties
21 there was an abundance of drilling, looking for gas and
22 these gas caps, really what they are, they're gas caps on
23 oil pools, and there was a lot of drilling done. There were
24 new pipelines put into the area, new connections were made ,
25 and the thing kind of got out of control a little bit, and

1 by the time they realized what was happening, it was prob-
2 ably too late because there was so much vested interest in
3 all those gas wells, and one hearing was called way back in
4 the early fifties at which time it was proposed that these
5 be declared as associated reservoirs, and that a cap be put
6 on the amount of gas, a severe cap be put on the amount of
7 gas that could be produced from the gas cap.

8 But there was quite a lot of opposition
9 because of those vested interests and the Commission sat on
10 that case for probably ten or fifteen years before it was
11 finally just dismissed.

12 But they're not associated by the defini-
13 tion of associated but they're associated pools by the -- in
14 reality.

15 Q And if we were to grant a priority sche-
16 dule, would it not be possible for operators to present a
17 case that you've made there for a reclassification of cer-
18 tain wells in that pool for priority of takes?

19 A Yeah, that's how it would have to be done
20 but those gas wells, actually the gas wells would benefit if
21 they were put on a gas/oil ratio limit like the -- you see,
22 there's -- there's oil wells in there that are producing a
23 heck of a lot more gas than the gas wells are at the present
24 time, and if it were -- if those gas allowables were removed
25 and it was all tied to the oil allowables as an associated

1 pool, the gas wells would benefit. But I just don't know if
2 the market could absorb all that gas. It would be difficult
3 for it to these days, I'm sure.

4 Q One other question. You referred to a
5 priority situation I guess versus a priority schedule, mean-
6 ing another way to express that might be a memorandum versus
7 an order.

8 A Uh-huh.

9 Q In the past we've had these memorandums
10 that you've shown us here. What weight do you see to a mem-
11 orandum versus an order? That seems to be a point of con-
12 tention at this hearing.

13 A Yes, there's two schools of thought on
14 these memorandums. I heard it expressed this morning that
15 they thought that a memorandum had the full force and effect
16 of rules and regulations, but I -- there's a school of
17 thought among attorneys, also, that a memorandum is non-en-
18 forceable and if it's an enforceable rule it certainly does
19 provide the pipelines with an additional defense for abroga-
20 tion of contracts.

21 If it's a memorandum there's a question
22 as to whether it is enforceable or not, but certainly a rule
23 has a lot more weight than a memorandum might have.

24 Q I see. Thank you.

25 MR. TAYLOR: I have a couple of

1 questions, Mr. Chairman.

2

3

CROSS EXAMINATION

4

BY MR. TAYLOR:

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Q Mr. Nutter, you seem to base a lot of your case upon the fact that El Paso is complying with the -- more or less with the rules in this memorandum.

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I've heard El Paso say a lot of times, just for an example, that they comply with ratable take, therefore would it be Doyle Hartman's argument that we should do away with ratable take and proration rules? Is that your argument?

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A Well, I'm not sure they always do comply with ratable take, so I don't think we ought to --

Q That's just what I've heard. This memorandum from Mr. Ramey, dated February 18th, 1983, listing his priorities, do you know if this memorandum was arrived at after notice and hearing?

19

20

21

22

A No, it was not.

Q No, it's not, do you know if there were any findings made that this was a reasonable method in which to regulate the takes of gas?

23

24

25

A No. I think it was just Mr. Ramey's work product after discussion of the problems with producers and staff and probably pipelines, also.

1 Q Do you know that the Commission had a
2 complaint by a producer that his casinghead gas was shut in
3 and other gas well gas was being taken. He attempted to
4 take action in the court against the producer of the -- if
5 the court would differentiate between a rule that had been
6 made after hearing and notice or a memorandum that had been
7 sent out by the Director?

8 A I don't know if there had been any such
9 incident at that particular time. I know it has occurred
10 from time to time over the last 35 years, that oil wells,
11 producers of oil wells had to resort to some kind of plea
12 with the Commission to try to get their casinghead gas con-
13 nected.

14 Q You stated that one of the reasons that
15 Mr. Hartman didn't like a rule like this was because it
16 would be a defense to the pipelines.

17 Have you -- are you aware of a case in
18 the United States District Court for the Western District of
19 Oklahoma, A & R Pipeline and Northwest Central Pipeline Cor-
20 poration versus the Corporation Commission of Oklahoma?

21 A No, I'm not.

22 Q Why don't you look at that, and would you
23 -- why don't you read us the first paragraph of that case,
24 just into the record?

25 MR. CARR: I think I'm going to

1 object to this line of questioning. It appears to me, one,
2 Mr. Nutter is not an attorney. He's just been given some-
3 thing he has not had an opportunity to review and although
4 he may like to play attorney from time to times, I think
5 it's inappropriate to give him a court decision he hasn't
6 seen and ask him to read selected portions of it, and I will
7 object to this line of questioning.

8 MR. TAYLOR: Well, what I'll do
9 is just say that this decision is a challenge of Oklahoma's
10 priority schedule in which they claimed that it was uncon-
11 stitutional and a violation of the interstate commerce
12 clause to enforce the priority schedule, and the court up-
13 held them in this particular case, and ruled that Oklahoma's
14 priority schedule was not appropriate for probably reasons
15 other than we're looking at one today, but I would just say
16 that if there the pipelines are challenging the statute and
17 rules in Oklahoma, settling a priority schedule, I don't
18 know that it would be such a great defense to them or else
19 they'd be in favor of it.

20 A Well, is -- let me ask you a question.
21 Is -- was that -- was that a rule or was it a memorandum?

22 MR. LEMAY: I think what we'll
23 do is include that as a statement, as a concluding statement
24 and inasmuch as we have a lawyer/engineer on the stand and
25 really don't want -- he's not qualified as a lawyer so we

1 won't ask for interpretations.

2 MR. CARR: And I'm certain Mr.
3 Hartman would be glad to have someone review that and give
4 you his opinion on it.

5 MR. LEMAY: We can get an opin-
6 ion on that from lots of lawyers. It can be part of a con-
7 cluding statement, Mr. Taylor.

8 Are there any other questions
9 of Mr. Nutter?

10 If not, I'm going to declare a
11 ten minute recess and we'll adjourn -- and we will come back
12 here at 20 minutes till 11 and accept the statements at that
13 time.

14 Mr. Nance?

15 MR. NANCE: Mr. Chairman, I do
16 not have a question of Mr. Nutter but I did have a comment
17 that I would like to make on behalf of El Paso specifically
18 with regard to his presentation.

19 If this would be an appropriate
20 time to do it, I'd like to get it in the record.

21 MR. LEMAY: Can you include
22 that comment in your closing? Are you going to make a
23 statement on behalf of El Paso?

24 MR. NANCE: Yes, I will.

25 MR. LEMAY: Could you include

1 that comment in that statement?

2 MR. NANCE: Okay.

3 MR. LEMAY: We'll accept any
4 other ocmments as well as statements at 20 minutes to 11.

5

6 (Thereupon a recess was taken.)

7

8 MR. LEMAY: We'll continue Case
9 9015 with the summary statements.

10 Mr. Nance, would you like to
11 make your comments concerning Mr. Nutter's testimony as well
12 as your summation, or your statement for the record, I mean?

13 MR. NANCE: Mr. Chairmam, I ap-
14 preciate the opportunity. Once again for the record my name
15 is John Nance on behalf of El Paso Natural Gas Company.

16 The first comment that I needed
17 to make is with respect to the inclusion of certain docu-
18 ments from El Paso with the group of exhibits that Mr. Nut-
19 ter has submitted.

20 El Paso appreciates the back-
21 handed compliment that Mr. Nutter has -- has paid us and his
22 vote of confidence in El Paso's position; however, we would
23 in fact like to disassociate ourselves from Mr. Hartman's
24 position and make it clear that those -- those Notices to
25 Sellers which -- which are included in Mr. Hartman's exhi-

1 bits may have represented a position taken by El Paso at a
2 particular point in time but should not be taken as repre-
3 sentative of our existing support or opposition to any pro-
4 posed priority of take rules, and certainly don't reflect El
5 Paso's position that the priority of take rules would some-
6 how afford us a defense in take-or-pay litigation that we
7 might not otherwise have.

8 With respect to the rules gen-
9 erally, El Paso is in support of priority of take rules --
10 of a priority of take concept, I should say. We do not spe-
11 cifically support or oppose the particular listing of prior-
12 ities that -- that are given here in Subparagraph A of the
13 proposed rule.

14 The objection that El Paso
15 would have to the rules as proposed is to paragraph B, which
16 would require any transporter of gas to provide a marketing
17 service. El Paso as an interstate pipeline does not feel
18 that it is appropriate for any sort of commission rules to
19 compel this type of service to be offered, particularly by
20 an interstate transporter. There perhaps are problems as
21 well with requiring this of intrastate, but certainly that's
22 -- that's not our concern here.

23 We do feel that although Mr.
24 Lyon had expressed his consideration of the applicability of
25 the Transco decision to this particular situation and did

1 not find a conflict with it, we feel somewhat differently,
2 and believe that to the extent that, first of all, that El
3 Paso, for example, might be required to have a marketing af-
4 filiate simply to fulfill its obligation under these rules,
5 is a step too far in the direction of regulating our inter-
6 state business, and particularly to the extent that the rule
7 might require El Paso to contract for new gas supplies that
8 we really don't feel our market would justify. This is
9 clearly in conflict with the -- the rule that Transco repre-
10 sents.

11 Mr. Chairman, thank you.

12 MR. LEMAY: Could I ask you one
13 quick question --

14 MR. NANCE: Yes, sir.

15 MR. LEMAY: -- Mr. Nance?

16 Do you support a memorandum or
17 an orders or have a preference?

18 MR. NANCE: I don't think El
19 Paso has a preference. It would be difficult, I think, for
20 El Paso to -- to represent at this point whether we feel
21 that, regardless of the form, that we would necessarily be
22 bound by any such set of priorities, anyway. We do not have
23 a position on that at this point but in fairness I think it
24 would be appropriate for us to -- to mention that as a pos-
25 sible issue that -- that might come up.

1 MR. LEMAY: Thank you.

2 Let's see, Mr. Carr, do you
3 have summation, any statement you want to make besides your
4 witness?

5 MR. CARR: No. At this time I
6 do have a very brief closing statement and I was going to
7 ask to give it last but I think in view of Mr. Nance's
8 statement, maybe it would be appropriate to go now.

9 Mr. Hartman has appeared here
10 today in opposition of reducing a priority schedule to a
11 formal rule of the Oil Conservation Division and it is bas-
12 ically our premise that such a rule is not needed.

13 We believe that the memo of Mr.
14 Ramey has by and large in the past been followed. El Paso,
15 I think here today, however, has really underscored the pro-
16 blem that a producer faces before you and that is that they
17 don't feel they'll be bound by whatever you do and they re-
18 mind you of Transco and the problem is, when you reduce this
19 to a rule you're simply creating something that may be cited
20 by a purchaser in disputes with producers and we see little
21 or no benefit to the producers of New Mexico in taking this
22 step and reducing it to a formal rule.

23 We therefore think that it's
24 ill advised, and we ask you not to reduce the priority
25 schedule to a formal rule.

1 MR. LEMAY: Thank you, Mr. Carr.
2 Mr. Kellahin, would you care to
3 make a statement?

4 MR. KELLAHIN: Thank you for
5 the opportunity, Mr. Chairman. We have no statement to ex-
6 press to you either for or against the adoption of the
7 priority schedule as a rule or memorandum.

8 We have participated in the
9 study groups. We think the priority schedule before you in
10 the suggested order is one that's reasonable. We can't tell
11 you whether to make it a rule or a memorandum.

12 The other questions that are
13 asked for comment in the notice, I think I answered by Mr.
14 Lyon and we have nothing further to tell you.

15 MR. LEMAY: Okay, thank you.

16 Mr. Pearce, for Amoco?

17 MR. PEARCE: Thank you, Mr.
18 Chairman, if I may do this in two parts. As I mentioned,
19 I'm appearing in this matter on behalf of Amoco Production
20 Company. I was asked to appear on their behalf this mor-
21 ning. The attorney, Mr. Dan Currens, in-house attorney for
22 Amoco was unable to get to Santa Fe because of travel com-
23 plications.

24 He had planned to come and ad-
25 dress the memorandum versus order legal point. In that re-

1 gard I would request that we be given something like a two-
2 week comment period so that Mr. Curren will have an oppor-
3 tunity to formalize those comments, and I do not know what
4 they were or the substance of those, but to contribute to
5 that record.

6 In addition, attending the
7 hearing today is Mr. Alan Wood, an engineer with Amoco in
8 Denver and with your permission I'd like for him to make a
9 closing comment on the substance of this matter.

10 MR. LEMAY: Fine.

11 MR. WOODS: Thank you, Mr.
12 Pearce.

13 Mr. Chairman, my name is Alan
14 Wood. I'm with Amoco Production Company of Denver,
15 Colorado.

16 It's our recommendation that
17 proposed rules, specifically Rules 315, 413, and 903, not be
18 adopted and instead the prioritization curtailment, if
19 required, be addressed through a memorandum from the
20 Director.

21 It's our opinion that the
22 current guidelines properly address the prioritization of --
23 for the prevention of waste.

24 The proposed provisions and
25 rules go far beyond that and for that reason we would

1 request and recommend that they not be adopted as rules.

2 Thank you.

3 MR. LEMAY: Thank you. Any
4 other comments, Mr. Pearce?

5 MR. PEARCE: No, Mr. Chairman.
6 Thank you.

7 MR. LEMAY: Yeah, thank you.

8 Mr. Duke, the Gas Company of
9 New Mexico?

10 MR. DUKE: We don't have any
11 comments.

12 MR. LEMAY; No comments. Mr.
13 Strand, for Alpha Twenty-One and IPA of New Mexico?

14 MR. STRAND: Mr. Chairman, on
15 behalf of Alpha Twenty-One Production Company and IPA of New
16 Mexico, we would simply concur in the opinions and recommen-
17 dations expressed by Mr. Nutter and in the statements of Mr.
18 Carr in his closing statement.

19 We would be very much in sup-
20 port of keeping the system the way it is right now with the
21 1983 memorandum remaining in effect. It appears that that
22 has worked well. There was no testimony presented that
23 there had been a large number of complaints over the past
24 year or two relating to priority of take problems and it ap-
25 pears the system is working and we see no reason to change

1 it at this point in time.

2 One other additional comment,
3 if the priority system is adopted as a rule or an order, we
4 think it imperative that there be some type of exception
5 procedure incorporated in that rule, as you alluded to in
6 your questions of Mr. Lyon. Mr. Lyon gave the example of
7 transporters coming in and having the right to ask for ex-
8 ceptions. I take it it goes without saying that that would
9 also apply to producers.

10 I took a quick glance at the
11 Oklahoma priority system case that Mr. Taylor had over the
12 break and it appears to me that if a priority system is un-
13 constitutional in Oklahoma, I suspect it probably is in New
14 Mexico, as well.

15 I'm also of the opinion that it
16 would run afoul of Transco. I think it's just exactly the
17 type of thing that Transco prohibits.

18 We would simply ask that it re-
19 main as it is and this particular proceeding be dismissed
20 and (not clearly understood) remain in effect.

21 Thank you.

22 MR. LEMAY: Is it fair to say
23 that Alpha Twenty-One and IPA of New Mexico support Mr.
24 Hartman pretty much on the testimony of Mr. Nutter and your
25 recommendations as you stated here?

1 MR. STRAND: Yes, that's cor-
2 rect.

3 MR. LEMAY: Okay, thank you.

4 Mr. Hall, for Blackwood and
5 Nichols, UniCal, Union Texas Petroleum, Yates Petroleum?

6 MR. HALL: Mr. Chairman, I have
7 no summary statement either for or against the proposal to
8 offer today.

9 I do have one further comment
10 on paragraph B of the proposal and I'm sorry I didn't bring
11 this up before the break.

12 Concern was expressed during
13 the break that perhaps further clarification is appropriate
14 in paragraph B. It may be appropriate to further define gas
15 transporter for someone who provides transportation to the
16 spot market.

17 A fear was expressed that as
18 written the paragraph could be construed to require someone
19 who offers mere gathering services, say a short two-mile
20 gathering line, to also provide marketing services.

21 We don't believe that what the
22 intent of the rule but perhaps because of the way it is
23 written, further clarification is in order.

24 MR. LEMAY: And if I take it
25 correct, you also made the suggestion as a comment that

1 rather than statewide you would suggest any pool in terms of
2 a connection for a transporter.

3 MR.HALL: Yes, Mr. Chairman.

4 MR. LEMAY: Thank you.

5 Mr. Padilla for Mr. Hendrix.

6 MR. PADILLA: Mr. Chairman, the
7 comments that I have in this regard are that the concerns of
8 my clients would be addressed in the priority schedule pro-
9 posed by the Committee or by the 1983 memorandum.

10 With respect to the priority
11 schedule and the preamble that was included in the Commit-
12 tee's report, or Mr. Lyon's report, we have some problems
13 with some of the language in the preamble and I would,
14 rather than argue about the specific language, I would ask
15 that it be stricken in your consideration.

16 Insofar as whether or not the
17 form of the regulations for the -- what action the Commis-
18 sion takes should be in the form of a memorandum or a pool
19 rule, we're not going to take a position on that; however, I
20 think that if you should adopt a memorandum of Mr. Ramey in
21 1983, I think that your action should reflect the incorpora-
22 tion of a 1983 memorandum and you're doing so as a result of
23 a hearing in this case.

24 MR. LEMAY: Thank you, Mr. Pad-
25 illa.

1 Mr. Draper?

2 MR. DRAPER: Northwest Pipeline
3 has no closing statement.

4 MR. LEMAY: Thank you, sir.

5 Mr. Morgan, Southern Union?

6 MR. MORGAN: Southern Union has
7 no comments, Mr. Chairman.

8 MR. LEMAY: Thank you, Mr. Mor-
9 gan.

10 Mr. Taylor, did you have any
11 summation for --

12 MR. TAYLOR: Mr. Chairman, I'd
13 just like to recommend on behalf of the Committee that the
14 recommendation in paragraph be adopted as a priority sche-
15 dule.

16 And on behalf of also the Divi-
17 sion, the Division recommends the adoption of the whole
18 rule, and I would just like to say that also on behalf of
19 the Division I think I would agree with Mr. Padilla, that if
20 they're going to return to the -- to a memorandum form, that
21 at least they declare in the form that there was notice and
22 hearing opportunity to address it before it was adopted.

23 MR. LEMAY: Do you have any
24 comment on the Oklahoma issue? Did you feel that it was un-
25 constitutional, therefore might be a factor in our consider-

1 ation?

2 MR. TAYLOR: Certainly from a
3 legal point of view, I think if you'll look at the Oklahoma
4 case, I think the judge in that case didn't consider a lot
5 of issues. He just read Transco and threw it out, but I
6 think the real issue is are you addressing production, which
7 states clearly have more authority to control or are you ad-
8 dressing transportation and taking, and I think in our case
9 our rule is just called a priority production schedule. In
10 Oklahoma they were looking more at takes and the judge in
11 that case said that the state could not control takes, al-
12 though I don't know if these are important distinctions at
13 this point or I think it will take more cases to figure that
14 out and see exactly what the emphasis in Transco was.

15 MR. LEMAY: Thank you, Mr. Tay-
16 lor.

17 Are there any other statements
18 or appearances in this case? Yes, sir.

19 MR. HOCKER: My name is R. L.
20 Hocker and I work for Cities Service Oil and Gas Corpor-
21 tion, Tulsa, Oklahoma. I'm a petroleum engineer.

22 With regard to some of the pro-
23 posals made today, I'd like to try to make a comment on
24 several of them.

25 First with regard to paragraph

1 A. Cities Service supports adoption of paragraph A, that is
2 the six priority schedule, either as a memo or as an order,
3 whichever you feel is proper. I think an order would prob-
4 ably be stronger.

5 As to paragraph C, we would
6 support paragraph C.

7 As to paragraph B, I'm a little
8 -- I'm not sure how that would be operated but I certainly
9 think that Mr. Hall's suggestion of making it apply to a
10 pool being served is certainly -- if you're going to adopt
11 it, that certainly ought to be in it. I'm not really in
12 support of B in the condition it's in right now.

13 With regard to the questions, I
14 think I've already answered number (1). I think an order
15 would probably be better.

16 With regard to number (2), I
17 don't know how to answer that and I don't think Mr. Lyon
18 (not understood.) I would say this, that I think that since
19 I like the first six priorities, I think if you want to
20 change that, perhaps those fields need to be a change asso-
21 ciated somewhere, perhaps that's the answer.

22 With regard to number (3), I
23 think yes, a well that is underproduced should have some ad-
24 ditional consideration. I think the purchaser, where pos-
25 sible, should leave it on line longer. There should be an

1 attempt to try to get that well insofar as it's able, to
2 produce its underproduction.

3 Now, whether that needs to be
4 as a sub-priority, I don't know, but -- but I think that
5 should be done.

6 Of course, number (4) is yes.

7 You asked a question of Mr.
8 Taylor that I'd like to comment on. I happen to be from Ok-
9 lahoma.

10 MR. LEMAY: Please do.

11 MR. HOCKER: I happen to have
12 been the witness in the priority case. I think that -- that
13 that hearing took took place and those rules were adopted by
14 the Commission prior to the final answer in Transco, and the
15 orders where the rules were adopted by Oklahoma Corporation
16 Commission addressed purchasers almost exclusively.

17 I would contrast that with the
18 new statewide Rule 30 and 34 in Texas, which puts an equal
19 burden upon both the producer and the purchaser. We'll see
20 how that comes out, whether that's constitutional or not,
21 but Oklahoma unfortunately was early and addressed only the
22 purchasers.

23 That's all I have. If you have
24 any questions, I'd try to answer those.

25 MR. LEMAY: I have none. We

1 appreciate your comments in the case.

2 MR. HOCKER: Thank you.

3 MR. LEMAY: Any other comments
4 or statements in Case 9015?

5 Yes, sir.

6 MR. AYCOCK: Mr. Chairman, Wil-
7 liam P. Aycock, Midland, Texas, representing myself as a
8 very small practical working interest owner in some non --
9 very few nonoperated working interests.

10 I support the position of IPA
11 of New Mexico, Alpha Twenty-One and Doyle Hartman.

12 MR. LEMAY: Thank you, sir.

13 Yes, sir, Mr. Merrion.

14 MR. MERRION: Mr. Chairman, I'm
15 Greg Merrion, President of Merrion Oil and Gas Corporation.

16 We support the position of Vic
17 Lyon and feel that this memorandum should be made an order
18 or dropped as a memorandum because it is not being followed
19 in our opinion. It was at one time followed very strictly
20 by El Paso Natural Gas Company. I don't think it's being
21 followed any more.

22 In our experience Northwest
23 Pipeline has never regarded this memorandum at all and we
24 think that the best efforts of the State would be served if
25 the effective order as in the memorandum were adopted as an

1 order.

2 MR. LEMAY: Thank you. Any
3 other comments, statements, in Case 9015?

4 Mr. Taylor.

5 MR. TAYLOR: I don't have a
6 statement but I just wanted to thank on behalf of the Com-
7 mission all the companies and individuals who participated
8 in the gas meetings and especially Bob Manning for putting
9 himself under fire here at the last hearing.

10 MR. HALL: Mr. Chairman, I need
11 to enter an appearance on the record on behalf of Exxon Com-
12 pany, USA.

13 MR. LEMAY: Yes. Your comments
14 apply to Exxon, what you had to say here?

15 MR. HALL: Yes.

16 MR. MANNING: Mr. Chairman.

17 MR. LEMAY: Yes, Mr. Manning.

18 MR. MANNING: I'd like to re-
19 spond to Mr. Taylor. I too thank him for not putting me on
20 the stand here today.

21 MR. LEMAY: Well, your -- Mr.
22 Nance had that opportunity and declined to do so.

23 Any other statements? Yes,
24 sir.

25 MR. DUKE: Mr. Chairman, I

1 apologize, do I understand there's going to be two weeks for
2 written comments?

3 MR. LEMAY: That was my -- I
4 was going to say, we are going to leave the record open two
5 weeks for written comments and -- and then it will be
6 closed, so --

7 MR. DUKE: Okay. I would also
8 ask you to take official notice of Gas Company's comments of
9 November 10th, 1986.

10 MR. LEMAY: We shall so do.

11 MR. DUKE: Thank you.

12 MR. LEMAY: Any other comments?

13 Mr. Taylor.

14 MR. TAYLOR: I guess we would
15 ask for the Commission's benefit that the records of the
16 last two meetings be incorporated into this one because
17 there was testimony developed in those hearings.

18 MR. LEMAY: Those records will
19 be part of this case, yes.

20 Any other comments?

21 If not, we'll take the case
22 under advisement.

23

24 (Hearing concluded.)

25

C E R T I F I C A T E

I, SALLY W. BOYD, C.S.R., DO HEREBY CERTIFY 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 this portion of the hearing, prepared by me to the best of my ability.

Sally W. Boyd CSR