

BLACKWOOD & NICHOLS CO., LTD.

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November 10, 1986

State of New Mexico
Oil Conservation Division
P.O. Box 2088
Santa Fe, New Mexico 87504-2088

Attn: R. L. Stamets, Director

Re: Proposed Rule Changes

Dear Mr. Stamets:

The hearing October 23, 1986 brought up several ideas for rule changes which were good. We were particularly pleased to hear that an "Allowable Bank" idea was being considered. This idea, if properly implemented, could greatly aid in protecting correlative rights between producers. It is hoped that this basic idea will be brought forth in each committee or sub-committee hearing on rules in the future.

Mr. William Clark, Blackwood & Nichols Co., Ltd., in the Durango office will be available to serve on rules committees or sub-committees. I will also be glad to offer suggestions to the various committees. Please let us know when the committees are to meet on the various proposed rule changes.

The following suggestions are offered concerning Docket numbers 9015 - 9018 heard October 23, 1986 and continued to November 20, 1986.

Docket No. 9015

Rule 315 Priorities of Production

We recommend the adoption of these priorities as printed in your memorandum dated October 1, 1986.

Rule 903 Priorities of Production

We recommend adoption of section (a). We oppose adoption of section (b). We recommend adoption of section (c), with the wording changed to read as follows:

"Should any purchaser be unable to take gas in accordance with the conditions described in paragraph (a) of this rule, such purchaser shall write the operator of the affected wells and explain the reason."

Docket No. 9017

Rule 902 Ratable Take

We oppose adding the additional paragraph proposed in the memorandum of October 1, 1986.

Docket No. 9016

Rule 414

We believe that if the conditions of Alternative Nos. 1 and 2 have been satisfied as between the Operator and the W.I. Owners of a well, then the Oil Conservation Division should allow the well to be produced and assign it a proper allowable. There would seem to be no disagreement as to property rights under these two plans.

We recommend that the Oil Conservation Division limit the amount any W.I. Owner be allowed to be overproduced to two years of their proportionate share of allowable, from any well.

The rule could be worded in such a manner to make the Operators responsible for controlling the gas deliveries and balancing.

Docket No. 9018

Rule 10 (a) should be amended in its entirety. The "Allowable Bank" idea needs to be implemented in each of the subdivisions of this rule. It is recommended that the reasons for underproduction be stated for each well and that the allowables be directly connected to the well's physical capability of producing gas. The following Rule 10 is recommended:

Rule 10 (a) (1) Underproduction, Northwest:

For the prorated gas pools of northwest New Mexico, a non-marginal GPU which has an underproduced status as of the end of a gas proration period shall be allowed to carry such underproduction forward into the next two gas proration periods and may produce such underproduction in addition to the allowable assigned during the next two succeeding periods. Any underproduction carried forward for the two gas prorative periods and remaining unproduced shall be cancelled if the reason for underproduction was the well's physical inability to produce the allowable quantities of gas.

Rule 10 (a) (2) Underproduction, Southeast:

For the prorated gas pools of southeast New Mexico, any non-marginal GPU which has an underproduced status as of the end of a gas proration period shall be allowed to carry such underproduction forward in the next gas proration period and may produce such underproduction in addition to the allowable assigned during such succeeding period. Any underproduction carried forward into a gas proration period remaining underproduced at the end of such gas proration period shall be cancelled if the reason for underproduction was the well's physical inability to produce the allowable quantities of gas.

Rule 10 (a) (3) Reasons for Underproduction:

No well's allowable will be cancelled for lack of market

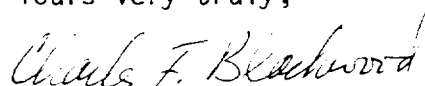
or being shut-in because of a contract dispute over price.

Allowables will only be cancelled because of a well being physically unable to produce gas in volumes sufficient to sell its allowable.

These suggestions are not intended to be "sacrosanct," but do represent what we believe to be fair to all parties involved in the production, sales, and purchases of natural gas in New Mexico.

Please let us know if you have any questions about these recommendations.

Yours very truly,

A handwritten signature in cursive script that reads "Charles F. Blackwood".

Charles F. Blackwood

CFB:sp

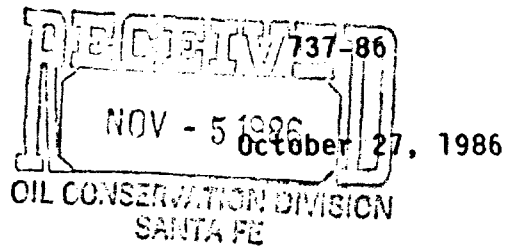
CC: Victor Lyon, Chief Engineer

F.T. Chavez, District III Supervisor

William F. Clark, Blackwood & Nichols Co., Ltd./Durango, CO.

NORTHWEST PIPELINE CORPORATION
ONE OF THE WILLIAMS COMPANIES

LAND DEPARTMENT



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State of New Mexico
Oil Conservation Commission
Attn: Richard L. Stamets
P. O. Box 2088
Santa Fe, NM 87501

Dear Dick:

At your suggestion, Northwest respectfully submits its comments to you regarding Case Nos. 9015, 9016, 9017 and 9018. We hope that by so doing, Northwest can call to the Commission's attention our concerns and suggest various proposals in a manner that will help expedite the hearings.

It is our understanding and opinion that the impetus behind the general meeting in June, the subsequently established committees and the above mentioned cases was the desire to get New Mexico Gas flowing again. Northwest strongly feels that if all industry entities were to work together, this goal can be accomplished in an expeditious and beneficial manner.

The industry seems to be changing faster than almost anyone can keep up with. These changes are challenging but can be exciting and worthwhile. One change that has occurred, which has left many confused and frustrated, is the dominant role that market forces currently play in almost every decision producers and pipelines make. It is Northwest's opinion that the market will dictate the winners and losers during the next decade. Market responsive decisions, and the institutional frameworks within which these decisions are made, are paramount for anyone to survive these tumultuous times.

It appears that many producers are unable and unwilling to accept the reality that the market will play such a dominant role in the future. Until the producers are able to accept this fact, it will be very difficult for New Mexico's natural gas to compete with competing energy sources in our traditional market areas.

Although several progressive market oriented rules were proposed at the hearings, many producers were unwilling to accept any rule that does not carry with it the implication of state enforcement of regulations requiring pipelines to accept gas into their systems for which there is no market. This attitude is counter productive for the producer and defeats the State of New Mexico's goal for increasing the production and marketing of its energy reserves. Again, the key must be to promulgate rules that will facilitate the production and flow of gas to markets.

Northwest reiterates its concern that no rule should be adopted that has the effect of shutting in gas which could be marketed.

CASE 9015

Northwest supports, with modification, the rules espoused in Rule 315, Rule 413 and Rule 903. The priority production would have the effect of preventing waste where the parties are willing to market their gas. Proposed rule 903(b) effectively reiterates a portion of the statute found in N.M.S.A. §§70-2-19(F) which in its entirety states "Nothing in the Oil and Gas Act [70-2-1 to 70-2-36 N.M.S.A. 1978] shall be construed or applied to require, directly or indirectly, any person to purchase gas of a quality or under a pressure or under any other condition by reason of which such gas cannot be economically and satisfactorily used by such purchaser by means of his gas transportation facilities then in service." Note the language states that the rule applies not just to Ratable Take language but to N.M.S.A. §§70-2-1 thru 70-2-36 which covers the full spectrum of proration, common purchaser, etc.

Not only is this a sensible statute but corresponds with the decision made recently by the United States Supreme Court in Mississippi vs. Transco case wherein the demarcation of authority between the FERC and state conservation laws was reiterated.

Thus, Northwest feels that rule 903(b) should be retained as stated to clarify the intent of rule 903.

However, Northwest feels that 903(c) is not necessary. The purchaser is in constant communication with the well operator who is responsible for turning the well on and shutting the well in as required. A requirement to notify the operator in writing that this has occurred is redundant and burdensome.

Northwest recommends amending Rule 903 by striking, in its entirety, subsection (c).

CASE 9016

Northwest recognizes the fact that split stream sales exist and will continue to exist in the future. We also feel that one of the changes to our industry that will continue with us for many years to come is that at various times less than 100% of the parties in a well will be willing or able to sell their portion of the gas. This is a reality that needs to be addressed.

In analyzing the proposed alternatives, Northwest feels that Alternative #1 which requires all interest owners in a well to designate one party to sell 100% of the gas would potentially shut in gas that is marketable. Also this alternative raises serious questions concerning; first, the authority of an operator to market another interest owners gas if sold at spot sale prices,

and second, the method and responsibility for payment of taxes and royalty. Alternative #3 does not address the problem of balancing the gas and could still allow a minority interest owner to become several times out of balance in a short time period with potential injury to correlative rights.

Alternative #2 most nearly addresses the current problems. It is Northwest's opinion that a gas balancing agreement is a necessity. We also feel that no gas should be shut in for a lengthy period of time if it is marketable. Thus, Northwest proposes the following language for the suggested Rule 414:

Rule 414

Effective May 1, 1987, where there are separate owners in a well, no gas sales may commence or be made from such well unless either:

- a) Such owners have entered into a gas balancing agreement or,
- b) The Division has entered an order establishing a gas balancing agreement which has been approved by a majority of the working interest of the well.

The well operator must provide the Division with a statement attesting to such agreement or order before any allowable will be assigned or before any authorization to produce will be made.

In principle, Northwest believes that gas balancing should be regarded as any other question affecting unit or well operations. No one wants to encourage further government regulation if it stifles anyone's ability to transact business. If regulations are promulgated, keeping in mind that rules should help industry transact their business, then all parties can be benefitted. Gas needs to flow and no order should be issued that would allow a minority interest owner to tie up well production, effectively shutting in the total production and leaving gas in the ground that has a market to which it can be sold.

Northwest realizes that there may be questions as to whether the existing statute gives the Commission authority or jurisdiction to involve themselves in gas balancing. If this is a genuine issue, we recommend that the Commission work with the Legislature to enact a statute, giving the Commission authority to order forced gas balancing and then issue the above mentioned order.

CASE 9017

Please note the comments above for Case 9015. Northwest sees no reason for amending rule 902 to include subsection (d). Notice is given to operators

Richard L. Stamets
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when a well is turned on or shut in. Additional notice should not be required. Also ratable take should be measured at year end and not on a shorter period. Lastly, by requiring notice to the operator, you may not be notifying all those who are interest holders in the well.

CASE 9018

Although Northwest feels that the changes suggested to rules 10(a), 11(a) and 11(b) which extend the make up period for over or under production and increase the six times over produced rule to twelve times over produced may be helpful, Northwest questions whether the rules should be permanent.

A suggested alternative is to issue an additional rule which would state:

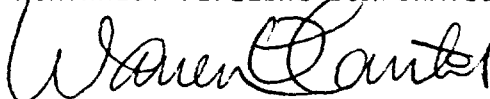
The Division Director, upon determination that changes to rules 10(a), 11(a) and 11(b) are necessary and upon statewide notice, may temporarily change rules 10(a) and 11(a) to increase the make up period, not to exceed two years, and may temporarily change rule 11(b) to increase the overproduced status requiring shut in of wells, not to exceed twelve times over produced. The Division Director will by statewide notice, indicate when conditions exists that rules 10(a), 11(a) and 11(b) would return to their standard status.

Vic Lyon's suggestion of a Gas (Allowable) Bank is very interesting and deserves further study. Northwest is willing to assist the Commission in any way we can to work out the details of such a proposal and analyze the benefits of implementing the concept.

In conclusion, Northwest encourages all aspects of the industry to work together to develop rules or procedures that will facilitate the production of natural gas in the State of New Mexico in the highly competitive environment which faces all of us.

Sincerely,

NORTHWEST PIPELINE CORPORATION



Warren O. Curtis
Manager, Land/Proration

WOC:js