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\*NEW MEXICO BOARD OF LEGAL SPECIALIZATION  
RECOGNIZED SPECIALIST IN THE AREA OF  
NATURAL RESOURCES-OIL AND GAS LAW

JASON KELLAHIN (RETIRED 1991)

April 22, 2002

**HAND DELIVERED**

Ms. Lori Wrotenbery, Director  
Oil Conservation Division  
1220 South Saint Francis Drive  
Santa Fe, New Mexico 87505

**KEY FAMILY GROUP'S REPLY  
IN SUPPORT OF ITS MOTION TO DISMISS**

Re: Case 12845  
Application of EnerQuest Resources, LLC  
for statutory unitization, Lea County, New Mexico

Re: Case 12846  
Application of EnerQuest Resources, LLC  
for approval of a waterflood project,  
Lea County, New Mexico

12 APR 22 PM 2:51  
OIL CONSERVATION DIVISION

Dear Ms. Wrotenbery:

On behalf of the Key Family Group, please find enclosed our reply to EnerQuest's response to our motion to dismiss EnerQuest's application. The reference cases have been continued to the Examiner's docket for May 2, 2002.

Very truly yours,



W. Thomas Kellahin

cc: David K. Brooks,  
Division Attorney  
David R. Catanach, Examiner  
James Bruce, Esq.,  
Attorney for Lynx  
William F. Carr, Esq.  
Attorney for Enerquest Resources, LLC  
T. Scott Hickman

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

**IN THE MATTER OF THE APPLICATION  
OF ENERQUEST RESOURCES, LLC  
FOR STATUTORY UNITIZATION  
LEA COUNTY, NEW MEXICO**

**CASE NO. 12845**

**IN THE MATTER OF THE APPLICATION  
OF ENERQUEST RESOURCES, LLC  
FOR A WATERFLOOD PROJECT  
LEA COUNTY, NEW MEXICO**

**CASE NO. 12846**

**KEY FAMILY GROUP'S  
REPLY TO  
ENERQUEST'S RESPONSE  
TO KEY FAMILY GROUP'S  
MOTION TO DISMISS THE ENERQUEST'S APPLICATION**

Comes now Hugh B. Key, II, Julie Ann Hopkins Trust, Mark Collver Hopkins Trust, Anne Key Davis, Kite Royalty Co., LLC, White Star Royalty, LLC. ("Key Family Group"), by its attorneys, Kellahin and Kellahin, and replies to EnerQuest Resources, LLC. ("EnerQuest") response to the Key Family Group's motion to dismiss EnerQuest application.

And in support states:

**GOOD FAITH STANDARD**

The Key Family Group contends that contrary to the custom and practice before the Division and in violation of NMSA (1979) Section 70-7-6(5), EnerQuest has instituted action to obtain a Statutory Unitization Order without first making a "good faith" effort to form a voluntary unit. NMSA (1979) Section 70-2-6(5) is very specific in its requirement that as a "matter to be found by the Division precedent to issuance of unitization order" the applicant must demonstrate:

"(5) that the operator has made a good faith effort to secure voluntary unitization within the pool or the portion thereof directly affected;"

EnerQuest, in this response, argues that counsel for the Key Family Group has created "good faith" standards for Statutory Unitization Cases which are not found in either statute or rule. Counsel for EnerQuest is too modest. He not only authors the "New Mexico Statutory Unitization Act" which requires the "good faith" standard, he has also established the standard of proof required to satisfy that standard.<sup>1</sup>

As with compulsory pooling case, the Division in Statutory Unitization Case has not adopted rules concerning "good faith." Instead, the Division as determine what is "good faith" on a case-by case basis and in doing so has established the "good faith" standard set forth in the Motion to Dismiss.

On a case by case basis, counsel for EnerQuest is largely responsible for developing the elements of proof for the "Good Faith" Standard. The following are example of how he did this:

(1) Case 12331, February 17, 2002, (Order R-11375) Falcon Creek Resources, Statutory Unitization of 1,320 acres. From November 1998 to February 17, 2000, applicant tried to obtain voluntary agreement. Transcript pages 6, 16, 17

(2) Case 12417, September 7, 2000 (Order R-11640) Saga Petroleum, LLC, Statutory Unitization of 800 acres. Applicant spent the better part of two year in negotiations process before filing application (provide chronology) Mr. Carr's letter dated March 14, 2001 to Division. Transcript page 57

(3) Case 12112, February 4, 1999 (Order R-11207) GP II Energy, Inc., Statutory unitization of 6,155 acres. Applicant spent from September, 1998 to February 1999 in negotiations process. Transcript page 53-61

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<sup>1</sup> William F. Carr, Esq. help author the New Mexico Statutory Unitization Act and thereafter has represented more applicant appearing before the Division seeking Statutory Unitization orders than any other New Mexico attorney.

(4) Case 10515, July 23, 1992, (Order R-9710) Texaco Exploration and Production Inc. Statutory unitization for 2,778 acres. Applicant call working interest owner meeting, review of technical committee report (1990) Transcript. page 24, 35,.

(5) Case 12207, August 5, 1999, (Order R-11255) St. Mary Land & Exploration Company. Opposed by Mr. Carr for Intoil, Inc. who dispute the participation formula. Case involved numerous meetings and discussion for more than one year before hearing. See St. Mary Exhibit 10 (chronology).

Counsel for Key Family Group is just attempting to have EnerQuest conform to the standards established by their own attorney.

### **UNDISPUTED FACTS**

EnerQuest take exception to the Key Family Group's statement of facts but in doing so concedes that the following facts are not in disputed:

(1) EnerQuest's waterflood plan involve 920 acres consisting of 13 tracts. **See Exhibit "A"**

(2) In November, 2000, Chris N. Bezner, for EnerQuest, prepared a waterflood feasibility report for the East Hobbs San Andres Field which forecast the following:

(a) A Full Scale waterflood project involving 17 injection wells for the possible recovery of 3,467,663 barrels of additional oil; **See Exhibit "B"** and

(b) A Phase I waterflood development plan involving 9 injection wells for the possible recovery of 1,825.804 barrels of additional oil. **See Exhibit "C"**

(3) On February 22, 2002, EnerQuest, substantially reduced its waterflood plan to 4 injection wells. Enerquest Resources did not provide any data to justify this proposed change of plans or change in cost. **See Exhibit "D"**

- (4) On February 26, 2002, EnerQuest filed an application for statutory unitization.
- (5) Prior to contacting the Key Family Group EnerQuest obtained the agreement of 81.37% of the other working interest owners.
- (6) On February 7, 2002, EnerQuest send to the Key Family Group a proposed unit agreement, operating agreement and ratification form.
- (7) At no time prior to February 7, 2002, did EnerQuest advise the Key Family Group of its waterflood development plans.
- (8) Some 15 months after preparing the Feasibility Report, EnerQuest on February 22, 2002 send a copy to the Key Family Group.
- (9) Four days before filing its application, on February 22, 2002, EnerQuest send the Key Family Group an AFE and advised that EnerQuest had altered its plan. **See Exhibits "E" and "F"**
- (10) At no time prior to filing its application did EnerQuest provide the Key Family Group with the data to support EnerQuest's plan of reduce its 17 injection well project by a 4 injection wells project.
- (11) At no time prior to filing the application did Enerquest call a working interest owners meeting.

### CONCLUSION

Counsel for EnerQuest argues that "good faith" is a two-way street. To the contrary, it is a one-way street with the burden of proof solely on the applicant who must demonstrate that it has take all reasonable action to obtain voluntary agreement before it can filing an application asking the State of New Mexico to exercise is police powers and compel the involuntary participation in the unit.

"Good Faith" is not achieved by waiting more than 15 months to share your plans for a waterflood protect with the working interest owners.

"Good Faith" is not satisfied when a major change in the proposed operating plan is announced by sending a AFE for a 4 injection well waterflood project to a working interest owners 4 days before filing a statutory unitization application.

"Good Faith" is not demonstrate by an applicant withholding technical data to support charging the plan from a 17 injection wells to a 4 well injection waterflood project four days before filing its application.

"Good Faith" is not defined as an opportunity for the applicant to play hide and seek with its plan or its data.

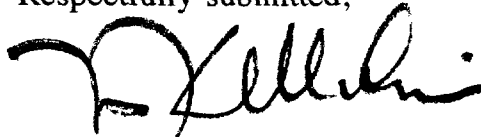
What appears to be happening is the applicant has already obtained the necessary 75 % agreement of the working interest owner and royalty owners and now is trying to get the Division to involuntarily compel the remaining owners into the unit with as little effort as possible.

It is impossible to have exhausted a good faith effort to reach a voluntarily agreement in less than 19 days after sending notice of its intention to form a unit. EnerQuest made no effort to inform the Key Family Group about the project. The Key Family Group are among those owners currently participating in production from in the Laney, Laney A and Laney Reese leases who would suffer a 30% or greater loss in revenue immediately upon unitization under EnerQuest's proposed participation formula. EnerQuest's action simply ignores the requirements of NMSA (1979) Section 70-2-6(5) and will encourage others to use statutory unitization as a negotiating weapon rather than as a remedy of last resort.

EnerQuest's application must be dismissed. Unless this application is dismissed the Division will be establishing a precedent which will allow applicants to avoid complying with NMSA (1979) Section 70-2-6(5).

WHEREFORE the Key Family Group requests that the Division Hearing Examiner grant this motion and dismiss Oil Conservation Division Case 12845.

Respectfully submitted,



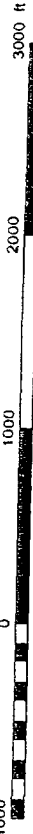
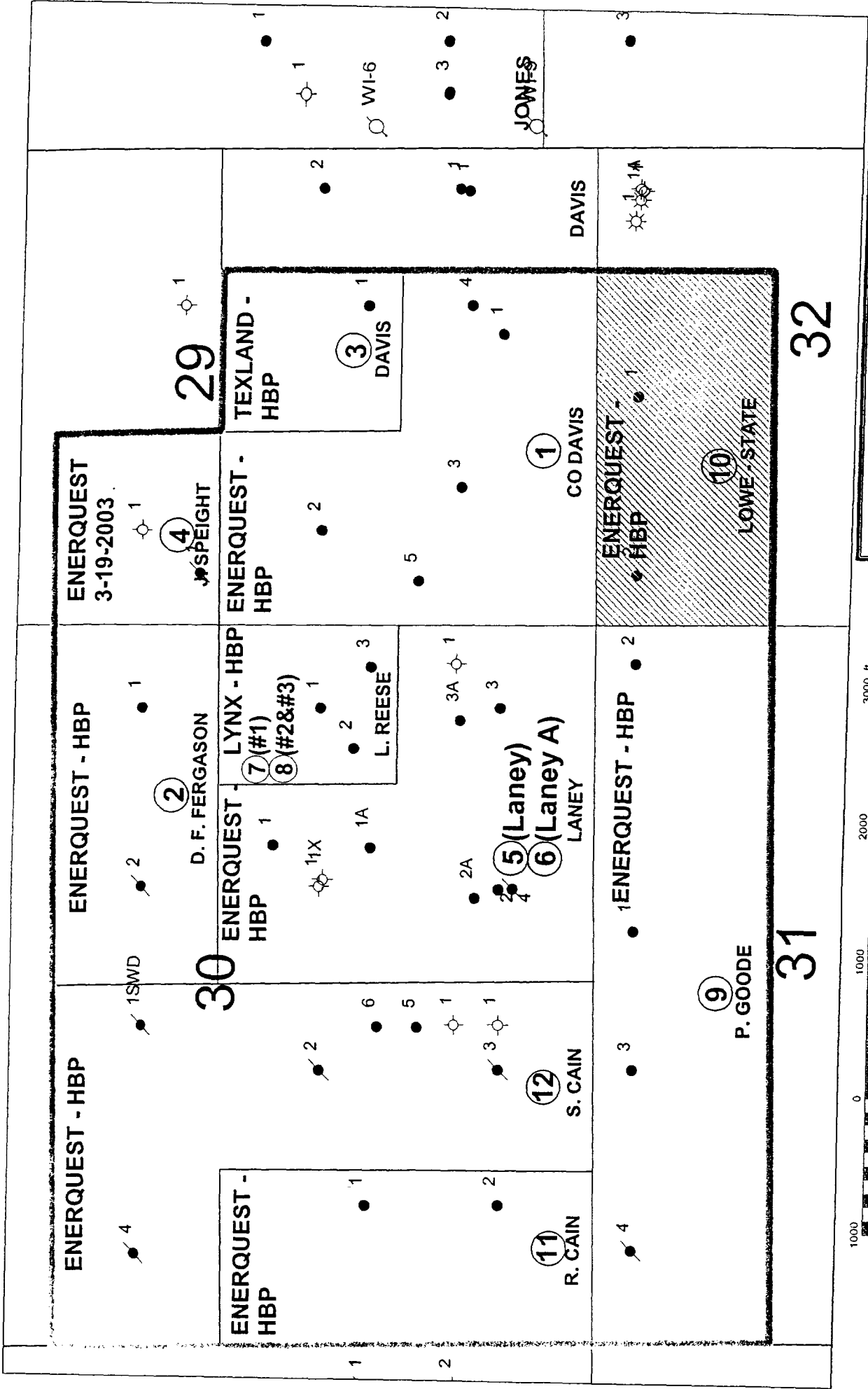
W. Thomas Kellahin  
P. O. Box 2265  
Santa Fe, New Mexico 87504

**CERTIFICATE OF SERVICE**

I certify that a copy of the foregoing pleading was transmitted by facsimile this 22th day of April, 2002 to James Bruce, attorney for Lynx et al, and to William F. Carr, attorney for EnerQuest Resources, LLC

A handwritten signature in black ink, appearing to read 'W. Thomas Kellahin', written over a horizontal line.

W. Thomas Kellahin



<div></div>	State Lands 80 acres (8.7%)
<div></div>	Patented Lands 840 acres (91.3%)

3 Tract Number Unit Outline



**ENERQUEST RESOURCES, LLC**

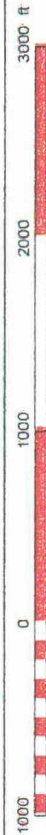
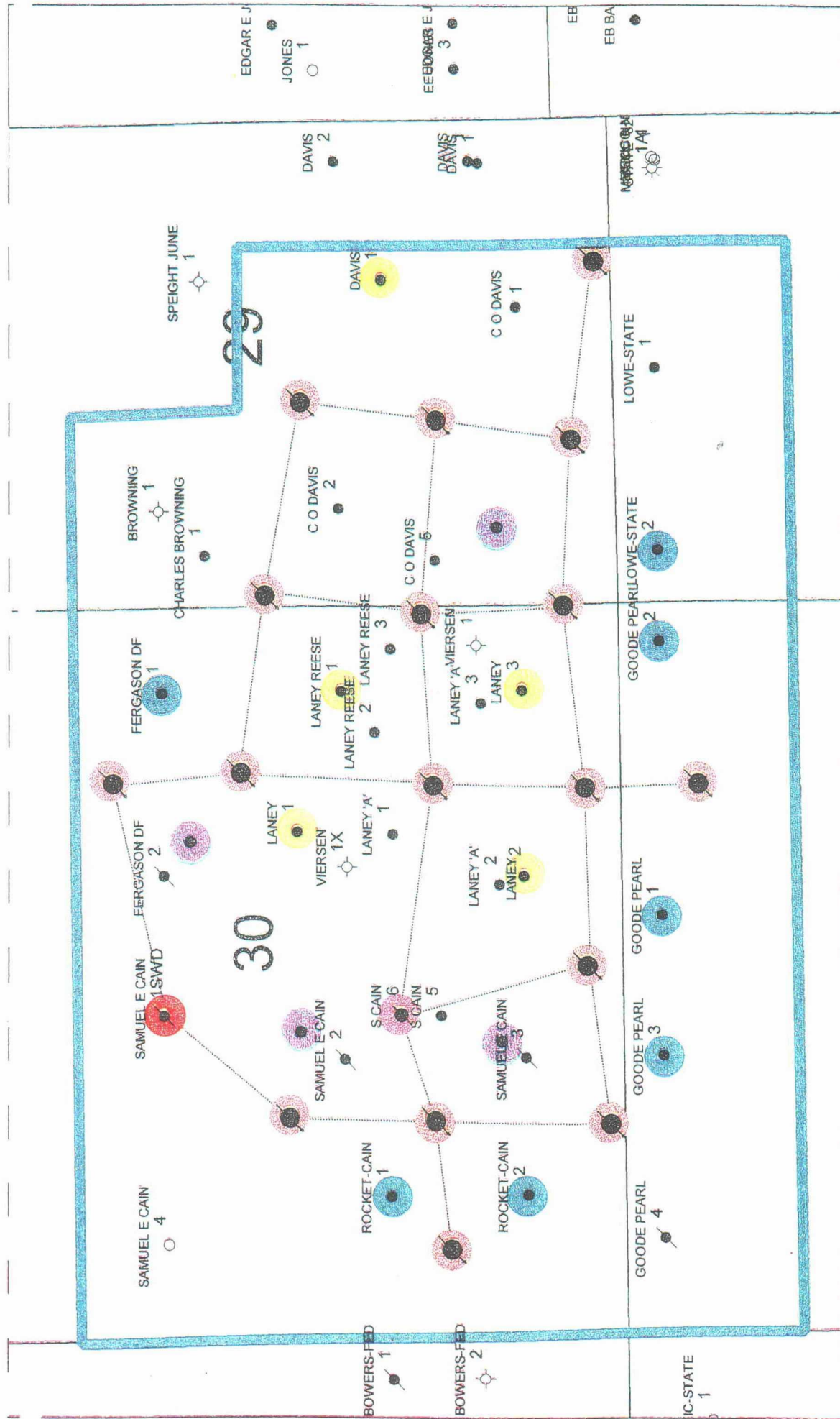
**EAST HOBBS (SAN ANDRES) UNIT**  
920 ACRES  
Lea County, New Mexico  
T18S - R39E

Project:  
Area:  
Prospect:

Date: 1 Jan, 2002  
Scale: 1"=1000'  
C.I.:

Geologist:  
Geophysicist:  
Engineer:





**FIGURE 7**

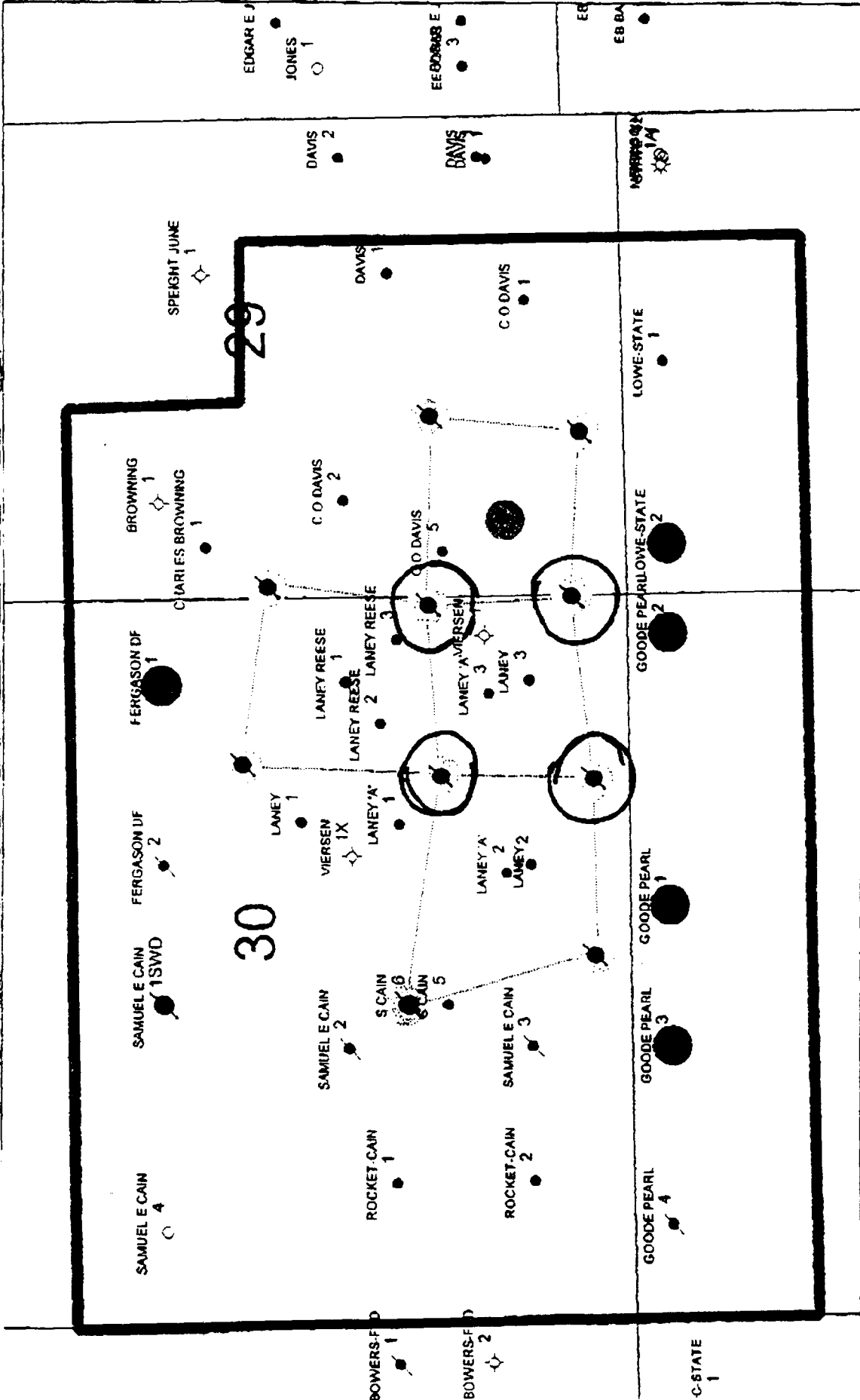
**ENERQUEST RESOURCES, LLC**

**FULL SCALE WATERFLOOD - PATTERN MAP**

**PROPOSED EAST HOBBS UNIT  
920 ACRES**

Project:	Date: 2 Nov, 2000	Geologist:	Chris Bezner
Area:	Scale: 1"=1000'	Geophysicist:	
Prospect:	C.L.:	Engineer:	





**ENERQUEST RESOURCES, LLC**

PHASE I WATERFLOOD - PATTERN MAP

PROPOSED EAST HOBBS UNIT  
920 ACRES

Project:	Date: 2 Nov. 2000	Geologist:	Chris Peters
Area:	Scale: 1"=1000'	Geophysicist:	
Proposed:	C.L.I.	Engineer:	

CONVERT FROM PRODUCER TO INJ. (1)

20 ACRE INFILL, PROD. (1)

20 ACRE INFILL, INJ. (9)

DEEPEN / RE-ENTER P1 PROD. (5)

REMAINING P1 PROD. (5)

EXHIBIT

D

# ENERQUEST

ENERQUEST OIL & GAS, LTD.

February 22, 2002

White Star Royalty Co  
P.O. Box 18693  
Oklahoma City, OK 73154


Re: East Hobbs Unit  
Lea County, New Mexico

Gentlemen:

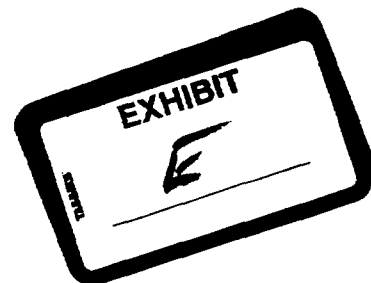
Pursuant to my telephone conversation with Mike Carr, enclosed please find a Phase I cost estimate for the above captioned unit as well as a feasibility report for the project. Please be advised that we have changed the development plans from the initial feasibility report as reflected on the reduced Phase I cost estimate.

Should you have any further questions, please let me know.

Very truly yours,

  
M. Craig Clark

MCC/s  
Enclosure



Phase1

Costs

10/9/2001

### EAST HOBBS WATERFLOOD PHASE I COST ESTIMATE

This is a reduced Phase 1 to just include 4 inj. Wells around the Laney 3 & Laney A 3.  
Maximum water injection 2000 BWPD at 1100 psi.

Quant.	Units	Description	\$/unit	Price, \$
1	Pump	Triplex Inj Pumps, 50 HP motor w/control panel, bypass valve, safety shut-downs, etc.	\$22,800	\$22,800
2	Tank	500 bbl. FG closed top tanks with connections.	\$6,000	\$12,000
		Miscellaneous fiberglass connections 2" & 4" ID		\$2,000
1	header	Inj header, flanged, w/ misc valves, IPC, & set concrete base for injection pumps		\$5,000
4	wellhead	Inj well heads w/turbine meter & variable choke, includes labor to install.	\$2,500	\$10,000
2,700	ft	Fiberglass injection lines, 1500# WP, 2" ID, delivered	\$2.25	\$6,100
1,300	ft	Fiberglass injection lines, 1500# WP, 4" ID, delivered	\$5.70	\$7,400
4,000	ft	Ditch, lay, & bury fiberglass inj lines w/detector tape, assumes 10% rock ditching.	\$3.35	\$13,400
		Misc contingencies & labor		\$7,300
		<b>SUBTOTAL FACILITIES</b>		<b>\$86,000</b>
1	WSW	Drill or convert 1 wells to Water Supply Wells	\$105,000	\$105,000
4	Inj	D&C injectors w/ FG lined tbg & inj pkr	\$240,000	\$960,000
		<b>SUBTOTAL WELL WORK</b>		<b>\$1,065,000</b>
		<b>GRAND TOTAL PHASE 1</b>		<b>\$1,151,000</b>

EXHIBIT

F