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Wednesday, May 15, 2002

To: David Catanach
Oil Conservation Division

Fax : 476-3471
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From: William F. Carr

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Message:

Attached is a copy of the Response to Key Family Group's Motion to Dismiss.

☒ No Confirmation Copy

Number of pages including cover sheet: 9

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Attorney Number: 5101

Client/Matter Number: 44495.0002

Time Deadline:

Operator Initials:

Date Transmitted:

Time:

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

**APPLICATION OF ENERQUEST RESOURCES, LLC.
FOR STATUTORY UNITIZATION, LEA COUNTY,
NEW MEXICO.**

CASE NO. 12845

**APPLICATION OF ENERQUEST RESOURCES, LLC.
FOR APPROVAL OF A WATERFLOOD PROJECT
AND QUALIFICATION OF THE PROJECT FOR
THE RECOVERED OIL TAX RATE PURSUANT
TO THE ENHANCED OIL RECOVERY ACT,
LEA COUNTY, NEW MEXICO.**

CASE NO. 12846

OIL CONSERVATION DIV
02 APR 17 AM 8:00

**ENERQUEST RESOURCES, LLC.'S
RESPONSE TO KEY FAMILY GROUP'S MOTION TO DISMISS**

The Key Family Group, through its attorney, asks the Division to Dismiss the applications of EnerQuest Resources, L.L.C. ("EnerQuest") for statutory unitization based on its contention that EnerQuest has violated the Statutory Unitization Act. The facts as represented by the Key Family Group are either incomplete or untrue. The standards and procedures which the Group contends apply to this matter are the creation of their counsel and not found in either statute or rule. The Motion to Dismiss must be denied.

RELEVANT FACTS

1. To determine the most prudent course of action for developing the remaining reserves in the San Andres formation in the East Hobbs San Andres Pool, EnerQuest prepared a Unit Waterflood Feasibility Study in the fall of 2000. This study concludes that the most effective way to recover the remaining reserves in this pool is through unitization and waterflood operations. Affidavit of Tim M. Dunn, paragraph 3.

2. Because of the advanced state of depletion of the East Hobbs-San Andres Pool and the fact that substantial drainage was occurring from properties in the proposed unit area to a tract operated by Lynx Operating Co., Inc. (especially the Laney and Laney A leases in which the Key Family Group own working interest), EnerQuest

decided in early 2002 to unitize 920 acres in Lea County, New Mexico and implement a waterflood project on the unitized lands. Affidavit of Tim M. Dunn, paragraph 4.

3. On February 7, 2002, EnerQuest wrote the Key Family Group and others and sought their voluntary participation in the proposed East Hobbs (San Andres) Unit and waterflood project. EnerQuest offered to respond to any questions and to provide information concerning this proposal. Affidavit of Tim M. Dunn, paragraph 5.

4. On February 22 White Star Royalty LLC ("White Star") contacted EnerQuest and advised EnerQuest that it represented the Key Family Group. It requested information on the proposed unit and waterflood project. On that date, EnerQuest provided White Star with the Unit Waterflood Feasibility Study and offered to meet with White Star to discuss the proposed unit and waterflood. Affidavit of Tim M. Dunn, paragraph 6.

5. On February 22, 2002 EnerQuest sent an AFE to the Key Family Group for the proposed waterflood. Affidavit of Tim M. Dunn, paragraph 7.

6. On March 11, 2002 EnerQuest filed the applications which are the subject of the above-referenced cases. Affidavit of Tim M. Dunn, paragraph 8.

7. In mid-March 2002, EnerQuest was contacted by T. Scott Hickman, consulting petroleum engineer, concerning the proposed statutory unitization and waterflood project. Mr. Hickman advised EnerQuest that he represented the Key Family Group. Affidavit of Tim M. Dunn, paragraph 9

8. On March 26, 2002, representatives of EnerQuest met with Mr. Hickman for approximately two hours and reviewed the Unit Waterflood Feasibility Study with him and responded to questions concerning the proposed statutory unitization and waterflood project. EnerQuest provided additional data to Mr. Hickman on that date and offered to meet again to discuss and to consider any other matter, including the proposed unit participation formula, proposed by the Key Family Group. Affidavit of Tim M. Dunn, paragraph 10.

9. At the March 26, 2002 meeting, Mr. Hickman requested additional information on the proposed unit and waterflood project. This information was delivered to Mr. Hickman's office, by EnerQuest. Affidavit of Tim M. Dunn, paragraph 11.

10. The legal counsel for EnerQuest has agreed to request the Division schedule this matter for hearing on a special hearing date after a reasonable time for review of the data and preparation for hearing.

11. Although EnerQuest voluntarily produced all requested information and documents to Mr. Hickman, and although EnerQuest had expressed its willingness to engage in further meetings and/or discussions as might be useful to Mr. Hickman

concerning this project, the only response from the Key Family Group was the Subpoena Duces Tecum Dated April 3, 2002. This subpoena sought much of the data that had already been produced to Mr. Hickman. Additional data has been produced pursuant to this Subpoena. Affidavit of Tim M. Dunn, paragraph 12.

ARGUMENT

Before a unit can be formed pursuant to the Statutory Unitization Act, the operator must make "a good faith effort to secure voluntary unitization within the pool or portion thereof directly affected." NMSA 1978, Section 70-7-6 (1975). Contrary to the assertions of the Key Family Group, EnerQuest has made a good faith effort to secure their voluntary participation in the proposed East Hobbs (San Andres) Unit.

The Key Family Group announces certain specific requirements that must be met to "demonstrate a good faith effort." These requirements are not found in any statute or rule. Instead, they have been crafted by the legal for the counsel for the Key Family Group for the purposes of this argument.

The Statutory Unitization Act and the rules of the Division are silent on what is required to meet the test of good faith because what is required is dependant on the particular facts and circumstances surrounding the individual unit. What EnerQuest has done in its good faith effort to obtain the voluntary participation of the Keys Family Group and others is set out above. EnerQuest provided the Keys Family Group with the Unit Agreement, an AFE, the Unit Waterflood Feasibility Study, met with their consulting petroleum engineer to review the study and answer questions, supplied additional data on March 26, 2002, and additional data was supplied thereafter at his request. EnerQuest has also produced additional data pursuant to the Subpoena obtained from the Division. EnerQuest has repeatedly made offers to meet and consider whatever the Keys Family Group would like to propose. This is "a good faith effort to secure voluntary unitization within the pool or portion thereof directly affected."

This proposal is not like the large units where there are hundreds of interest owners to be contacted. Here, through EnerQuest's efforts, 81.37% of the working interest has been voluntarily committed to the proposed unit and waterflood project. Only the Keys Family Group who stand to reap substantial benefit from the unit and waterflood and Lynx Operating Co. which is draining reserves from offsetting owners - including the Keys Family Group -- are still in opposition to the plan. Their concerns will not be addressed until there is a hearing on the merits and an order is issued pursuant to the Statutory Unitization Act.

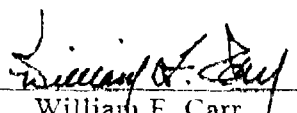
Good faith is a two-way street. This Motion to Dismiss and the Subpoena previously issued on the request of the Keys Family Group are not attempts to gain additional time to review and discuss the merits of the proposals or to obtain more data. They have only one purpose, that is to avoid a prompt resolution of the issues by the Division through frivolous procedural maneuverings

For example, the Keys Family Group lists what it contends is required to demonstrate a good faith effort and states that these things were not done by EnerQuest. The Key Family Group is simply wrong. They say EnerQuest did not prepare a feasibility study and did not provide one to the working interest owners. These statements are not only incorrect, it is inconsistent with other portions of their Motion to Dismiss (In Page 2, paragraph 7 the Keys Family Group admits that it received the Feasibility Study). The Keys Family Group working interest owners were not allowed time to study the feasibility study. In their Motion to Dismiss the Keys forget the study was presented to them on February 22nd and fail to disclose that this study was reviewed with their consulting petroleum engineer by EnerQuest on March 26th and that there have been no questions to EnerQuest from their expert since the March 26th meeting. They overlook the agreement to approach the Division for a special hearing date after there has been a reasonable time to review the data and prepare for hearing.

Perhaps, the Key Family Group should talk to their engineer and lawyer and compare notes. If they would, they would discover that studies and supporting data have been provided by EnerQuest, that meetings have occurred, additional data voluntarily shared, and additional time allowed to evaluate this proposed project. Maybe they would discover what was really going on, they would also find that EnerQuest has made a good faith effort to obtain their voluntary participation in this unit.

EnerQuest requests that the Oil Conservation Division deny the Motion to Dismiss of the Key Family Group and in so doing find that, in the context of this particular proposed unit, EnerQuest has met the good faith standard of the Statutory Unitization Act by (1) preparing and providing to the Key Family Group the Unit Waterflood Feasibility Study, (2) meeting with the representative of the Key Family Group to review the report, answer questions about the proposed unit and waterflood project, (3) voluntarily providing data on the unit and proposed waterflood on at least five occasions, and (4) agreeing to select a special hearing date after a reasonable time has passed to review all data and prepare for the hearing.

Respectfully submitted,
Holland & Hart LLP

By: 
William F. Carr

ATTORNEYS FOR ENERQUEST
RESOURCES, LLC

RESPONSE TO MOTION TO DISMISS
PAGE 4

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TO THE ENHANCED OIL RECOVERY ACT,
LEA COUNTY, NEW MEXICO.**

CASE NO. 12846

AFFIDAVIT OF TIM M. DUNN

STATE OF TEXAS)
)
COUNTY MIDLAND)

Tim M. Dunn, being first duly sworn on oath, states as follows:

1. My name is Tim M. Dunn. I reside in Midland, Texas. I am the Vice President of EnerQuest Resources, L.L.C. ("EnerQuest"). My responsibilities with EnerQuest include supervision of technical activities of this company.
2. I am responsible for supervision of the efforts of EnerQuest to unitize the East Hobbs (San Andres) Unit pursuant to the New Mexico Statutory Unitization Act.
3. To determine the most prudent course of action for developing the remaining reserves in the San Andres formation in the East Hobbs San Andres Pool, in the fall of 2000 EnerQuest prepared a Feasibility Study. This study concludes that the most effective way to recover the remaining reserves in this pool is through unitization and fieldwide waterflood operations.

4. Because of the advanced state of depletion of the East Hobbs-San Andres Pool and the fact that substantial drainage was occurring from properties in the proposed unit area to a tract operated by Lynx Operating Co., Inc. (especially the Laney and Laney A leases in which the Key Family own their working interest), it was decided in early 2002 to proceed with the formation of the proposed unit and implementation of a waterflood project on 920-acres in Lea County, New Mexico.

5. On February 7, 2002, EnerQuest wrote the Key Family Group and others and sought their voluntary participation in the proposed East Hobbs (San Andres) Unit and waterflood project. EnerQuest offered to respond to any questions and to provide information concerning this proposal.

6. On February 22, 2002, the Feasibility Study was sent to White Star Royalty, LLC which advised EnerQuest that it represented the Key Family Group in this area. EnerQuest offered on that date to provide additional information or answer questions concerning the study and our plans to unitize and implement waterflood operations in this pool.

7. On February 22, 2002, EnerQuest sent an AFE to the Key Family Group for the proposed waterflood.

8. The applications in these consolidated cases were filed on March 11, 2002.

9. In mid-March 2002, EnerQuest was contacted by T. Scott Hickman, consulting petroleum Engineer from Midland Texas, concerning the proposed statutory unitization and waterflood project. Mr. Hickman advised EnerQuest that he represented the Key Family Group.

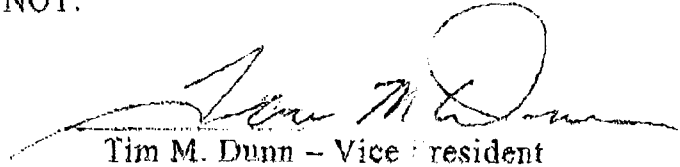
10. Chris Bezner met with Mr. Hickman for approximately two hours on March 26, 2002, reviewed the Feasibility Study with him and responded to questions about the proposed unitization and waterflood project on behalf of EnerQuest. EnerQuest provided additional data to Mr. Hickman on that date and offered to meet again to discuss and to consider any other matter, including the proposed unit participation formula, proposed by the Key Family Group.

11. At the March 26, 2002 meeting, Mr. Hickman requested additional information on the proposed unit and waterflood project. This information was delivered to Mr. Hickman's office in Midland, Texas by EnerQuest.

12. Although EnerQuest had voluntarily produced all requested information and documents to Mr. Hickman, and although on March 26, 2002,

EnerQuest had expressed its willingness to engage in further meetings and/or discussions as might be useful to Mr. Hickman concerning this project, the only response from the Key Family Group was the Subpoena Duces Tecum Dated April 3, 2002. This subpoena sought much of the data that had already been produced to Mr. Hickman. Other data has been produced pursuant to this Subpoena.

FURTHER AFFIANT SAYETH NOT.

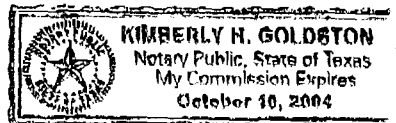

Tim M. Dunn - Vice President

SUBSCRIBED AND SWORN before me on this 16 day of April 2002.


Notary Public

My Commission Expires:

Oct. 10, 2004



CERTIFICATE OF SERVICE

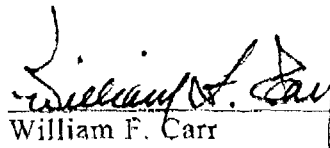
I certify that on April 17, 2002, I served a copy of the foregoing document to the following by

☐
☒
☐

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