

BEFORE EXAMINER CATANACH

OIL CONSERVATION DIVISION

M/W EXHIBIT NO. 1 (R8768)

CASE NO. 11996

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

IN THE MATTER OF THE HEARING
CALLED BY THE OIL CONSERVATION
DIVISION FOR THE PURPOSE OF
CONSIDERING:

CASE NO. 9420
Order No. R-8768

IN THE MATTER OF THE HEARING CALLED BY
THE OIL CONSERVATION DIVISION (OCD) ON
ITS OWN MOTION FOR POOL CREATION AND
SPECIAL POOL RULES, SAN JUAN, RIO ARRIBA,
MCKINLEY AND SANDOVAL COUNTIES, NEW MEXICO

ORDER OF THE DIVISION

BY THE DIVISION:

This cause came on for hearing at 8:30 a.m. on July 6, 1988, at Farmington, New Mexico, before Examiner David R. Catanach.

NOW, on this 17th day of October, 1988, the Division Director, having considered the testimony, the record, and the recommendations of the Examiner, and being fully advised in the premises,

FINDS THAT:

(1) Due public notice having been given as required by law, the Division has jurisdiction of this cause and the subject matter thereof.

(2) Division Case Nos. 9420 and 9421 were consolidated at the time of the hearing for the purpose of testimony.

(3) The Oil Conservation Division, hereinafter referred to as the "Division", on the recommendations of the Fruitland Coalbed Methane Committee, hereinafter referred to as the "Committee", seeks the creation of a new pool for the production of gas from coal seams within the Fruitland formation underlying the following described area in San Juan, Rio Arriba, McKinley, and Sandoval Counties, New Mexico:

CASE NO. 9420
Order No. R-8768
Page -2-

Township 19 North, Ranges 1 West through 6 West;
Township 20 North, Ranges 1 West through 8 West;
Township 21 North, Ranges 1 West through 9 West;
Township 22 North, Ranges 1 West through 11 West;
Township 23 North, Ranges 1 West through 14 West;
Township 24 North, Ranges 1 East through 16 West;
Township 25 North, Ranges 1 East through 16 West;
Township 26 North, Ranges 1 East through 16 West;
Township 27 North, Ranges 1 West through 16 West;
Township 28 North, Ranges 1 West through 16 West;
Township 29 North, Ranges 1 West through 15 West;
Township 30 North, Ranges 1 West through 15 West;
Township 31 North, Ranges 1 West through 15 West;
Township 32 North, Ranges 1 West through 13 West;

(4) The Division further seeks, also upon the recommendations of the Committee, the promulgation of special pool rules, regulations, and operating procedures for said pool including, but not limited to, provisions for 320-acre spacing and proration units, designated well locations, well density, horizontal wellbore and deviated drilling procedures, venting and flaring rules, downhole commingling, and gas well testing requirements.

(5) In companion Case No. 9421, the Division seeks to contract the vertical limits of twenty-six existing Fruitland and/or Fruitland-Pictured Cliffs Gas Pools to include only the Pictured Cliffs sandstone and/or Fruitland sandstone intervals.

(6) The Committee, which included representatives of the oil and gas industry, New Mexico Oil Conservation Division, Colorado Oil and Gas Conservation Commission, Bureau of Land Management, and Southern Ute Indian Tribe, was originally formed in 1986 for the purpose of studying and making recommendations to the Division as to the most orderly and efficient methods of developing coal seam gas within the Fruitland formation.

(7) Geologic evidence presented by the Committee indicates that the Fruitland formation, which is found within the geographic area described above, is composed of alternating layers of shales, sandstones, and coal seams.

CASE NO. 9420
Order No. R-8768
Page -3-

(8) The evidence at this time further indicates that the coal seams within the Fruitland formation are potentially productive of natural gas in substantial quantities.

(9) The gas originating from the coal seams within the Fruitland formation is composed predominantly of methane and carbon dioxide and varies significantly from the composition of the gas currently being produced from the sandstone intervals, and as such, represents a separate common source of supply.

(10) A new pool for gas production from coal seams within the Fruitland formation should be created and designated the Basin-Fruitland Coal Gas Pool with vertical limits comprising all coal seams within the equivalent of the stratigraphic interval from a depth of approximately 2450 feet to 2880 feet as shown on the Gamma Ray/Bulk Density log from Amoco Production Company's Schneider Gas Com "B" Well No. 1 located 1110 feet from the South line and 1185 feet from the West line of Section 28, Township 32 North, Range 10 West, NMPM, San Juan County, New Mexico.

(11) The proposed horizontal pool boundary, which represents the geographic area encompassed by the Fruitland formation, contains within it, an area previously defined as the Cedar Hill-Fruitland Basal Coal Gas Pool (created by Division Order No. R-7588 effective February 1, 1984); said area currently comprises Sections 3 through 6 of Township 31 North, Range 10 West, and Sections 19 through 22 and 27 through 34 of Township 32 North, Range 10 West, NMPM, San Juan County, New Mexico.

(12) The proposed horizontal boundary of the Basin-Fruitland Coal Gas Pool should be amended to exclude that acreage currently defined as the Cedar Hill-Fruitland Coal Gas Pool described in Finding No. (11) above.

(13) The Committee has recommended the promulgation of special rules and regulations for the Basin-Fruitland Coal Gas Pool including a provision for 320-acre spacing and proration units, and in support thereof presented pressure

CASE NO. 9420
Order No. R-8768
Page -4-

interference data obtained from producing and pressure observation wells located within the Cedar Hill-Fruitland Coal Gas Pool, which indicates definite pressure communication between wells located 2,180 feet apart (radius of drainage of a 320-acre proration unit = 2,106 feet).

(14) Further testimony and evidence indicates that due to the unique producing characteristics of coal seams (i.e. initial inclining production rates), engineering methods such as decline curve analysis and volumetric calculations traditionally used to aid in the determination of proper well spacing, cannot be utilized.

(15) The Committee further recommended the adoption of a provision in the proposed pool rules allowing for the drilling of a second well on a standard 320-acre proration unit in order to give an operator flexibility when addressing regional geologic trends.

(16) Dugan Production Corporation, Merrion Oil and Gas Corporation, Hixon Development Company, Robert L. Bayless, and Jerome P. McHugh and Associates, hereinafter referred to as the "Dugan Group", appeared at the hearing and presented geologic and engineering evidence and testimony in support of a proposal which includes the following:

1. Establishment of an area within the Southern portion of the Basin-Fruitland Coal Gas Pool to be developed on 160-acre spacing and proration units.
2. Creation of a demarcation line and buffer zone separating the 320-acre spacing portion of the pool and the proposed 160-acre spacing portion of the pool.

(17) The Dugan Group owns oil and gas leasehold operating rights in the Fruitland formation in various areas of the San Juan Basin, and currently operates numerous wells producing from coal seam and sandstone intervals within the Fruitland formation.

CASE NO. 9420
Order No. R-8768
Page -5-

(18) The Dugan Group has defined the location of the proposed demarcation line and 160-acre spacing area by utilizing a preponderance of geologic factors such as coal rank, depth of burial, thermal maturation, thickness of coal, and amount of gas in place.

(19) In support of the proposed 160-acre spacing area for the subject pool, the Dugan Group presented production data obtained from four producing wells, the Nassau Well Nos. 5, 6, 7, and 8 located in Section 36, Township 27 North, Range 12 West, NMPM, San Juan County, New Mexico, which indicates that the production rate from said Nassau Well No. 5 was unaffected by initiation of 160-acre offset production in said Nassau Well Nos. 6, 7, and 8.

(20) The evidence presented by the Dugan Group further indicates however, that the Nassau Well Nos. 5, 6, 7, and 8 are producing from commingled coal seam and sandstone intervals within the Fruitland formation, and as such, do not conclusively demonstrate 160-acre non-interference exclusively within the coal seams.

(21) Insufficient evidence exists at the current time to justify the creation of a 160-acre spacing area and demarcation line within the Basin-Fruitland Coal Gas Pool.

(22) The best technical evidence available at this time indicates that 320-acre well spacing is the optimum spacing for the entire Basin-Fruitland Coal Gas Pool.

(23) In order to prevent the economic loss caused by the drilling of unnecessary wells, avoid the augmentation of risk arising from the drilling of an excessive number of wells, prevent reduced recovery which might result from the drilling of too few wells, and to otherwise protect correlative rights, special rules and regulations providing for 320-acre spacing units should be promulgated for the Basin-Fruitland Coal Gas Pool.

(24) The special rules and regulations should also provide for restrictive well locations in order to assure orderly development of the subject pool and protect correlative rights.

CASE NO. 9420
Order No. R-8768
Page -6-

(25) Due to the relatively large area encompassed by the Basin-Fruitland Coal Gas Pool, and the relatively small amount of reservoir data currently available, the special rules and regulations should be promulgated for a temporary period of two years in order to allow the operators in the subject pool the opportunity to gather additional reservoir data relative to the determination of permanent spacing rules for the subject pool and/or specific areas within the pool.

(26) The evidence and testimony presented at the hearing is insufficient to approve at the present time, the proposed provision allowing for the drilling of a second well on a standard 320-acre proration unit.

(27) The Committee further recommended the adoption of a provision in the Special Rules and Regulations allowing the venting or flaring of gas from a Basin-Fruitland Coal Gas Well during initial testing in an amount not to exceed a cumulative volume of 50 MMCF or a period not to exceed 30 days.

(28) The evidence presented does not justify the establishment of a specific permissible volume of gas to be vented or flared from Basin-Fruitland Coal Gas Wells at this time, however, the supervisor of the Aztec district office of the Division should have the authority to allow such venting or flaring of gas from a well upon a demonstration such flaring or venting is justified and upon written application from the operator.

(29) Evidence and testimony presented at the hearing indicates that the gas well testing requirements as contained in Division Order No. R-333-I may cause damage to a Basin Fruitland Coal Gas Well, and that special testing procedures should be established.

(30) The special rules and regulations promulgated herein should include operating procedures for determination and classification of Basin-Fruitland Coal Gas Wells, horizontal wellbore and deviated drilling procedures, and procedures and guidelines for downhole commingling.

CASE NO. 9420
Order No. R-8768
Page -7-

(31) This case should be reopened at an examiner hearing in October, 1990, at which time the operators in the subject pool should be prepared to appear and present evidence and testimony relative to the determination of permanent rules and regulations for the Basin-Fruitland Coal Gas Pool.

IT IS THEREFORE ORDERED THAT:

(1) Effective November 1, 1988, a new pool in all or parts of San Juan, Rio Arriba, McKinley, and Sandoval Counties, New Mexico, classified as a gas pool for production from Fruitland coal seams, is hereby created and designated the Basin-Fruitland Coal Gas Pool, with vertical limits comprising all coal seams within the equivalent of the stratigraphic interval from a depth of approximately 2450 feet to 2880 feet as shown on the Gamma Ray/Bulk Density log from Amoco Production Company's Schneider Gas Com "B" Well No. 1 located 1110 feet from the South line and 1185 feet from the West line of Section 28, Township 32 North, Range 10 West, NMPM, San Juan County, New Mexico.

(2) The horizontal limits of the Basin-Fruitland Coal Gas Pool shall comprise the following described area in all or portions of San Juan, Rio Arriba, McKinley, and Sandoval Counties, New Mexico, with the exception of Section 3 through 6 of Township 31 North, Range 10 West, and Section 19 through 22, and 27 through 34 of Township 32 North, Range 10 West, San Juan County, New Mexico, which said acreage currently comprises the Cedar Hill-Fruitland Basal Coal Gas Pool:

Township 19 North, Ranges 1 West through 6 West;
Township 20 North, Ranges 1 West through 8 West;
Township 21 North, Ranges 1 West through 9 West;
Township 22 North, Ranges 1 West through 11 West;
Township 23 North, Ranges 1 West through 14 West;
Township 24 North, Ranges 1 East through 16 West;
Township 25 North, Ranges 1 East through 16 West;
Township 26 North, Ranges 1 East through 16 West;
Township 27 North, Ranges 1 West through 16 West;
Township 28 North, Ranges 1 West through 16 West;

CASE NO. 9420
Order No. R-8768
Page -8-

Township 29 North, Ranges 1 West through 15 West;
Township 30 North, Ranges 1 West through 15 West;
Township 31 North, Ranges 1 West through 15 West;
Township 32 North, Ranges 1 West through 13 West;

(3) Temporary Special Rules and Regulations for the Basin-Fruitland Coal Gas Pool are hereby promulgated as follows:

SPECIAL RULES AND REGULATIONS
FOR THE
BASIN-FRUITLAND COAL GAS POOL

RULE 1. Each well completed or recompleted in the Basin-Fruitland Coal Gas Pool shall be spaced, drilled, operated, and produced in accordance with the Special Rules and Regulations hereinafter set forth.

RULE 2. A gas well within the Basin-Fruitland Coal Gas Pool shall be defined by the Division Director as a well that is producing from the Fruitland coal seams as demonstrated by a preponderance of data which could include the following:

- a. Electric Log Data
- b. Drilling Time
- c. Drill Cuttings or Log Cores
- d. Mud Logs
- e. Completion Data
- f. Gas Analysis
- g. Water Analysis
- h. Reservoir Performance
- i. Other evidence which may be utilized in making such determination.

RULE 3. The Division Director may require the operator of a proposed or existing Basin-Fruitland Coal Gas Well, Fruitland Sandstone Well, or Pictured Cliffs Sandstone Well, to submit certain data as described in Rule (2) above, which would otherwise not be required by Division Rules and Regulations, in order to demonstrate to the satisfaction of the Division that said well will be or is currently producing from the appropriate common source of supply.

CASE NO. 9420
Order No. R-8768
Page -9-

RULE 4. Each well completed or recompleted in the Basin-Fruitland Coal Gas Pool shall be located on a standard unit containing 320-acres, more or less, comprising any two contiguous quarter sections of a single governmental section, being a legal subdivision of the United States Public Lands Survey.

RULE 5. The Supervisor of the Aztec district office of the Division shall have the authority to approve a non-standard gas proration unit within the Basin-Fruitland Coal Gas Pool without notice and hearing when the unorthodox size or shape is necessitated by a variation in the legal subdivision of the United States Public Lands Survey and the non-standard unit is not less than 75% nor more than 125% of a standard gas proration unit. Such approval shall consist of acceptance of Division Form C-102 showing the proposed non-standard unit and the acreage contained therein.

RULE 6. The Division Director may grant an exception to the requirements of Rule (4) when the unorthodox size or shape of the gas proration unit is necessitated by a variation in the legal subdivision of the United States Public Lands Survey and the non-standard gas proration unit is less than 75% or more than 125% of a standard gas proration unit, or where the following facts exist and the following provisions are complied with:

(a) The non-standard unit consists of quarter-quarter sections or lots that are contiguous by a common bordering side.

(b) The non-standard unit lies wholly within a governmental half section.

(c) The applicant presents written consent in the form of waivers from all offset operators or owners of undrilled tracts and from all operators owning interests in the half section in which the non-standard unit is situated and which acreage is not included in said non-standard unit.

CASE NO. 9420
Order No. R-8768
Page -10-

(d) In lieu of Paragraph (c) of this rule, the applicant may furnish proof of the fact that all of the aforesaid parties were notified by registered or certified mail of his intent to form such non-standard unit. The Division Director may approve the application if no such party has entered an objection to the formation of such non-standard unit within 30 days after the Division Director has received the application.

RULE 7. The first well drilled or recompleted on every standard or non-standard unit in the Basin-Fruitland Coal Gas Pool shall be located in the NE/4 or SW/4 of a single governmental section and shall be located no closer than 790 feet to any outer boundary of the proration unit nor closer than 130 feet to any quarter section line nor closer than 10 feet to any quarter-quarter section line or subdivision inner boundary.

RULE 8. The Division Director may grant an exception to the requirements of Rule (7) without hearing when an application has been filed for an unorthodox location necessitated by topographical conditions, the recompletion of a well previously drilled to a deeper horizon, provided said well was drilled at an orthodox or approved unorthodox location for such original horizon, or the drilling of an intentionally deviated horizontal wellbore. All operators or owners of undrilled tracts offsetting the proposed location shall be notified of the application by registered or certified mail, and the application shall state that such notice has been furnished. The Director may approve the application upon receipt of written waivers from all parties described above or if no objection to the unorthodox location has been entered within 20 days after the Director has received the application.

RULE 9(A). The Division Director shall have the authority to administratively approve an intentionally deviated well in the Basin-Fruitland Coal Gas Pool for the purpose of penetrating the coalbed seams by means of a wellbore drilled horizontally, provided the following conditions are complied with:

CASE NO. 9420
Order No. R-8768
Page -11-

(1) The surface location of the proposed well is a standard location or the applicant has obtained approval of an unorthodox surface location as provided for in Rule (8) above.

(2) The bore hole shall not enter or exit the coalbed seams outside of a drilling window which is in accordance with the setback requirements of Rule (7), provided however, that the 10 foot setback distance requirement from the quarter-quarter section line or subdivision inner boundary shall not apply to horizontally drilled wells.

(B). To obtain administrative approval to drill an intentionally deviated horizontal wellbore, the applicant shall file such application with the Santa Fe and Aztec offices of the Division and shall further provide a copy of such application to all operators or owners of undrilled tracts offsetting the proposed gas proration unit for said well by registered or certified mail, and the application shall state that such notice has been furnished. The application shall further include the following information:

- (1) A copy of Division Form C-102 identifying the proposed proration unit to be dedicated to the well.
- (2) Schematic drawings of the proposed well which fully describe the casing, tubing, perforated or open hole interval, kick-off point, and proposed trajectory of the drainhole section.

The Director may approve the application upon receipt of written waivers from all parties described above or if no objection to the intentionally deviated horizontal wellbore has been entered within 20 days after the Director has received the application. If any objection to the proposed intentionally deviated horizontal well is received within the prescribed time limit as described above, the Director shall, at the applicant's request, set said application for public hearing.

CASE NO. 9420
Order No. R-8768
Page -12-

(C). During or upon completion of drilling operations the operator shall further be required to conduct a directional survey on the vertical and lateral portions of the wellbore and shall submit a copy of said survey to the Santa Fe and Aztec offices of the Division.

(D). The Division Director, at his discretion, may set any application for intentionally deviated horizontal wellbores for public hearing.

RULE 10. Notwithstanding the provisions of Division Rule No. 404, the Supervisor of the Aztec district office of the Division shall have the authority to approve the venting or flaring of gas from a Basin-Fruitland Coal Gas Well upon a determination that said venting or flaring is necessary during completion operations, to obtain necessary well test information, or to maintain the producibility of said well. Application to flare or vent gas shall be made in writing to the Aztec district office of the Division.

RULE 11. Testing requirements for a Basin-Fruitland Coal Gas well hereinafter set forth may be used in lieu of the testing requirements contained in Division Order No. R-333-I. The test shall consist of a minimum twenty-four hour shut-in period, and a three hour production test. The Division Director shall have the authority to modify the testing requirements contained herein upon a showing of need for such modification. The following information from this initial production test must be reported:

1. The surface shut-in tubing and/or casing pressure and date these pressures were recorded.
2. The length of the shut-in period.
3. The final flowing casing and flowing tubing pressures and the duration and date of the flow period.

CASE NO. 9420
Order No. R-8768
Page -13-

4. The individual fluid flow rate of gas, water, and oil which must be determined by the use of a separator and measurement facilities approved by the Supervisor of the Aztec district office of the Division; and
5. The method of production, e.g. flowing, pumping, etc. and disposition of gas.

RULE 12. The Division Director shall have the authority to approve the commingling within the wellbore of gas produced from coal seams and sandstone intervals within the Fruitland and/or Pictured Cliffs formations where a finding has been made that a well is not producing entirely from either coal seams or sandstone intervals as determined by the Division. All such applications shall be submitted to the Santa Fe office of the Division and shall contain all the necessary information as described in General Rule 303 (C) of the Division Rules and Regulation, and shall meet the prerequisites described in 303 (C)(1)(b). In addition, the Division Director may require the submittal of additional well data as may be required to process such application.

RULE 13. The Division Director may approve the commingling within the wellbore of gas produced from coal seams and sandstone intervals within the Fruitland and/or Pictured Cliffs formations where a well does not meet the prerequisites as described in General Rule 303 (C)(1)(b) provided that such commingling had been accomplished prior to July 1, 1988, and provided further that the application is filed as described in Rule (12).

IT IS FURTHER ORDERED THAT:

(4) The locations of all wells presently drilling to, completed in, commingled in, or having an approved APD for the Basin-Fruitland Coal Gas Pool are hereby approved; the operator of any well having an unorthodox location shall notify the Aztec district office of the Division in writing of the name and location of the well within 30 days from the date of this order.

CASE NO. 9420
Order No. R-8768
Page -14-

(5) Pursuant to Paragraph A. of Section 70-2-18, N.M.S.A. 1978, Comp., contained in Laws of 1969, Chapter 271, existing gas wells in the Basin-Fruitland Coal Gas Pool shall have dedicated thereto 320 acres in accordance with the foregoing pool rules; or, pursuant to Paragraph C. of said Section 70-2-18, existing wells may have non-standard spacing and proration units established by the Division and dedicated thereto.

(6) In accordance with (5) above, the operator shall file a new Form C-102 dedicating 320 acres to the well or shall obtain a non-standard unit approved by the Division. The operator shall also file a new C-104 with the Aztec district office of the Division.

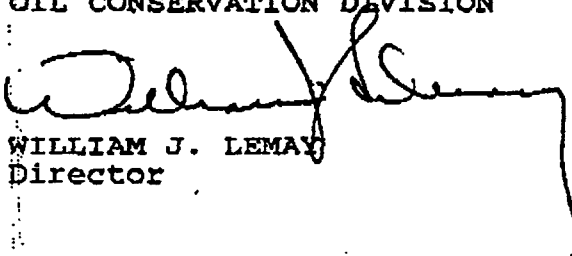
(7) Failure to comply with Paragraphs (5) and (6) above within 60 days of the date of this order shall subject the well to a shut-in order until such requirements have been met.

(8) This case shall be reopened at an examiner hearing in October, 1990 at which time the operators in the subject pool may appear and present evidence and testimony relative to the determination of permanent rules and regulations for the Basin-Fruitland Coal Gas Pool.

(9) Jurisdiction of this cause is retained for the entry of such further orders as the Division may deem necessary.

DONE at Santa Fe, New Mexico, on the day and year hereinabove designated.

STATE OF NEW MEXICO
OIL CONSERVATION DIVISION


WILLIAM J. LEMAY
Director

S E A L