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. 12276
CASE NO. 12277

IN THE MATTER OF THE APPLICATIONS OF BURLINGTON RESOURCES OIL & GAS COMPANY FOR COMPULSORY POOLING, SAN JUAN COUNTY, NEW MEXICO

BURLINGTON RESOURCES OIL & GAS COMPANY'S MEMORANDUM IN SUPPORT OF ITS FIRST AMENDED APPLICATION

Comes now BURLINGTON RESOURCES OIL & GAS COMPANY ("Burlington") by its attorneys, Kellahin & Kellahin, and requests that the New Mexico Oil Conservation Division ("NMOCD") allow it to amend its compulsory pooling applications, over the objection of Energen Resources Corporation and others (collectively the "GLA-46 Group"), to allege that in the event the Division determines that the cost limitations and carrying provisions of a November 27, 1951 farmout/operating agreement (the GLA-46 Agreement) still applies to these proposed wells, then the provisions of Section 70-2-17.E NMSA (1978) apply and Division must modify the GLA-46 Agreement to the extent necessary to prevent waste in accordance with this statutory provision of the New Mexico Oil & Gas Act and in support states:

SUMMARY OF ESSENTIAL FACTS

Division Case 12276:

(1) In Case 12276, Burlington Resources Oil & Gas Company, in accordance with Section 70-2-17.C NMSA (1978), or in the alternative in accordance with Section 70-2-17.E NMSA (1978), seeks an order pooling all uncommitted owners of mineral interests in the Mesaverde formation and the Chacra formation underlying the following described acreage within Section 36, T27N, R8W, NMPM, San Juan County, New Mexico, in the following manner:

(i) a 320-acre gas spacing unit consisting of the W/2 of this section for gas production from the Blanco-Mesaverde Gas Pool to be dedicated to the proposed Brookhaven Com Well No. 8 to be located in the NW/4 and to the Brookhaven Com Well No. 8A to be located in the SW/4 of this section;

(ii) for a standard 160-acre gas spacing unit consisting of the NW/4 of this section for gas production from the Otero-Chacra Gas Pool to be dedicated to the Brookhaven Com Well No. 8; and

(iii) for a standard 160-acre gas spacing unit consisting of the SW/4 of this section for gas production from the Otero-Chacra Gas Pool to be dedicated to the Brookhaven Com Well No. 8A.

(2) On July 30, 1998, Burlington proposed to the other working interest owners in this spacing unit the drilling of the Brookhaven Com Well No. 8 as a Mesaverde/Chacra dual completion at an estimated well cost of $427,630.00 to be governed by the parties signing a new joint operating agreement instead of adopting the cost limitations and carrying provisions of the GLA-46 Agreement.

(3) On September 15, 1999, Burlington proposed to the other working interest owners in this spacing unit the drilling of a second well in this same spacing unit (the "Brookhaven Com Well No. 8A" and identified in Burlington's proposal as the Brookhaven Com Well No. 9.) as a Mesaverde/Chacra dual completion at an estimated well cost of $427,630.00 to be governed by the parties signing a new joint operating agreement instead of adopting the GLA-46 Agreement.

(4) The GLA-46 Group admits that Burlington's AFE estimate of $427,630.00 for each of these wells represents a fair and reasonable estimate of the costs of such wells as of July 30, 1998.

In Case 12277:

(5) In Case 12277, Burlington Resources Oil & Gas Company, in accordance with Section 70-2-17.C NMSA (1978), or in the alternative in accordance with Section 70-2-17.E NMSA (1978), seeks an order pooling all uncommitted owners of mineral interests in the Mesaverde formation underlying the E/2 of Section 16, T31N, R11W, NMPM, San Juan County, New Mexico, for a 320-acre gas spacing unit consisting of this half section for gas production from the Blanco-Mesaverde Gas Pool to be dedicated to the proposed Brookhaven Com B Well No. 3B to be located within the NE/4SE/4 of this section.

(6) On December 14, 1998 and again on September 15, 1999, Burlington proposed to the other working interest owners in this spacing unit the drilling of the Brookhaven Com B Well No. 3B as a Mesaverde formation completion at an estimated well cost of $386,488.00 to be governed by the parties signing a new joint operating agreement instead of adopting the cost limitations and carrying provisions of the GLA-46 Agreement.

(7) The GLA-46 Group admits that Burlington's AFE estimate of $386,488.00 for this well represents a fair and reasonable estimate of the costs as of October 22, 1998.

GLA-46 GROUP'S POSITION

(8) The GLA-46 Group contends that the Division cannot enter a compulsory pooling order for these wells because on November 27, 1951, the original parties contracted for a well development plan which provided for certain cost limitations and carrying provisions which are still in effect.

(9) The GLA-46 Group contends it can adopt and participate in the Brookhaven Wells under the terms of the GLA-46 Agreement which are very favorable to GLA-46 Group and, if adopted, include the right for the GLA-46 Group to be a "carried interest" so that as to the GLA-46 acreage within a spacing unit:

(a) Burlington pays for the total cost of the well, including casing;

(b) then from 25% of the production, Burlington recoups 50% of the costs of a Mesaverde well or a Chacra well (excluding casing);

(c) the total costs (excluding casing) of a Mesaverde well cannot exceed $90,000.00 of which Brookhaven's share is not more than $45,000.00 and cannot exceed $28,500.00 for a Chacra well of which Brookhaven's share is not more than $14,275.00;

(d) the GLA-46 Group keeps its share of 25% of the production until payout of the recoverable costs and then keeps its share of 50% of the production.

BURLINGTON'S POSITION

(10) If the NMOCD believes that the cost limitations and carrying provisions of the GLA-46 Agreement still apply, the Burlington contends that the NMOCD has the authority to issue compulsory pooling orders in these cases thereby modifying the original parties' plan for the costs of the development set forth in the 1951 GLA-46 Agreement so that these wells can be drilled because:

(a) these wells are necessary in order to recover Mesaverde and Chacra reserves which will not otherwise be recovered;

(b) the cost limitations and the carrying provision of GLA-46 Agreement preclude the economic drilling of these wells;

(c) waste will occur in the event the Division fails to modify the GLA-46 Agreement because it is uneconomic for Burlington to drill these marginal wells under the economic limitations imposed by the GLA-46 Agreement and the reserves which could have been produced by these wells will be left unrecovered in the reservoirs;

(d) the provisions of Section 70-2-17.E NMSA (1978) apply and Division should modify the GLA-46 Agreement to the extent necessary to prevent waste in accordance with this statutory provision of the New Mexico Oil & Gas Act; and

(e) Pursuant to Section 70-2-17.E NMSA (1978) and in order to obtain its just and equitable share of production from these wells and these spacing units, the Division should pool the described spacing units and described mineral interests involved.

(11) In support of its claim Burlington introduced evidence which demonstrates that:

(a) these wells are necessary in order to recover Mesaverde and Chacra reserves which will not otherwise be recovered;

(b) both the Mesaverde and Chacra wells will be marginal wells;

(c) if Burlington is not subject to the cost limitations and carrying provisions of the GLA-46 Agreement, then Burlington will spend $247,000 to realize an expected profit of $185,000 on the Brookhaven 8 well; will spend $294,000 to realize an expected profit of $232,000 on the Brookhaven 8A well; and will spend $196,000 to realize an expected profit of $158,000 on the Brookhaven Com B Well No 3B;

(d) however, if Burlington is subject to the cost limitations and carrying provisions of the GLA-46 Agreement, then Burlington will spend $427,000 but realize a profit of only $93,000 on the Brookhaven 8 well; will spend $427,000 but realize a profit of only $163,000 on the Brookhaven 8A well; and will spend $386,000 but realize a profit of only $53,000 on the Brookhaven Com B Well No. 3B;

(e) if Burlington is subject to the cost limitations and carrying provisions of the GLA-46 Agreement, then Burlington will recover its investment in 3.26 years on the Brookhaven 8 well and in 2.27 years on the Brookhaven 8-A well;

(f) correspondingly, if the GLA-46 Group enjoys the cost limitations and carrying provisions of the GLA-46 Agreement then for no investment is expected to enjoy a profit of $236,000 on the Brookhaven 8 well; a profit of $166,000 on the Brookhaven 8A well; and a profit of $259,000 on the Brookhaven Com B Well No. 3B;

(g) however, if the GLA-46 Group's interest is not subject to the cost limitations and carrying provisions of the GLA-46 Agreement then the GLA-46 Group will invest $180,000 and enjoy an estimated profit of $144,000 on the Brookhaven 8

well; invest $133,000 to enjoy an estimated profit of $100,000 on the Brookhaven 8A well; and invest $190,000 to enjoy an estimated profit of $153,000 on the Brookhaven Com B Well No. 3B;

(h) waste will occur because it is uneconomic for Burlington to drill these marginal wells under the economic limitations imposed by the GLA-46 Agreement and the reserves which could have been produced by these wells will be left unrecovered in the reservoirs.

BURLINGTON'S CITATION OF AUTHORITY

Burlington's position is supported by decisions of the New Mexico Supreme Court, the New Mexico Oil & Gas Act, by a prior decision of the Division, and by the GLA-46 Agreement.

Court cases:

In 1963, the New Mexico Supreme Court in Sims v. Mechem, 72 N.M. 186, 382 P.2d 183 (NM 1963) considered the compulsory pooling powers of the Commission in a case in which the appellant specifically challenged the Commission's authority to enter a pooling order which "violated" the written agreement of the parties. Although reversed on other grounds, the Court upheld the Commission's action on this point and ruled that any agreement between owners may be modified by the Commission:

> "Unquestionably the commission is authorized to require pooling of property when such pooling has not been agreed upon by the parties (citing to what is now 70-2-17.C NMSA 1978), and it is clear that the pooling of the entire west half of Section 25 had not been agreed upon. It is also clear from sub-section (e) of the same section (citing to what is now 70-2-17.E) that any agreement between owners and lease-holders may be modified by the commission. [emphasis added] But the authority of the commission to pool property or to modify existing agreements relating to production within a pool under either of these sub-sections must be predicted on the prevention of waste."

In 1975, the New Mexico Supreme Court, again, considered the compulsory pooling authority of the Commission and in Rutter & Wilbanks Corp. v. Oil Conservation Commission, 87 N.M. 286, 532 P.2d 582 (NM 1975) held that not only did the Commission have compulsory pooling authority to pool separately owned tracts within a spacing or proration unit, it had the power to pool separately owned tracts within an oversize non-standard spacing unit. In doing so, the Court approved of the Commission's decision to compulsory pool a 409-acre spacing unit and a 407-acre spacing unit each of which had a completed well and could have been dedicated to standard 320-acre spacing units for the Washington Ranch-Morrow Gas Pool. (See OCC Order Nos. R-4353 and R-4354). The point is that when necessary to prevent waste, the Division can and did modify the agreement of sharing revenues within a spacing unit, required the inclusion of additional acreage and thereby dilute the royalty interest of Rutter & Wilbanks over its objection.

Division cases:

Similarly, the Division has previously modified an existing operating agreement when its terms precluded the drilling of a well which the Division considered necessary in order to prevent waste. On January 11, 1996, in Case 11434, the Division held a hearing on the application of Meridian Oil Company for a compulsory pooling order for a Mesaverde infill well against Doyle Hartman and Four Star Oil & Gas Company. In this case, both Four Star and Hartman contended the Division did not have the authority to authorize the compulsory pooling of a Mesaverde infill well because the original parties in the spacing unit had signed a 1953 operating agreement which contained a plan for the spacing of but one single Mesaverde well within a 320-acre spacing unit. On February 22, 1996, the Division entered Order R-10545 and decided that the Division, in accordance with Section 70-2-17.E NMSA (1978), had the authority and would exercise that authority to modify this 1953 operating agreement to the extent necessary to prevent waste and to issue a compulsory pooling order so that the infill well could be drilled.

A further review of NMOCD compulsory pooling orders, shows that on October 24, 1990, the NMOCD issued Order R-9332 which granted an application by Doyle Hartman for compulsory pooling in which he was allowed to pool his undeveloped acreage in the Eumont Gas Pool into an existing gas spacing unit already operated by Chevron and containing a existing well. Hartman was further authorized to drill a second "infill well" over Chevron's objection. The point is that when necessary to prevent waste, the Division can and did modify the existing voluntary agreement of Chevron for the operations of its existing spacing unit and its well and required the inclusion of additional acreage and additional wells over the objection of Chevron.

The GLA-46 Agreement:

In the 1951 GLA-46 Agreement, the original parties specifically agreed that their agreement would be modified to be consistent with the orders and rules of the NMOCD when they provided at page 11:

> "Unless disapproved by final administrative action by either the Federal or State government, and **until such disapproval**, this agreement shall be binding upon the parties. **In the event of any decision disapproving of this agreement or of any provision or any part thereof,** the parties agree that the intent of this contract shall prevail so that neither party shall be denied the intended rights described herein, and to that end, **they will use their best efforts to agree on the necessary modifications hereof to cure the causes for disapproval**"[emphasis added]

CONCLUSION

Conservation laws and the rules, regulations and orders promulgated thereunder have the effect of modifying the provisions of existing leases and other contracts and agreements. Without that effect, then parties could make agreements which are contrary to or inconsistent with what the NMOCD determines are appropriate rules for development of a pool, including the cost of wells, economic waste caused by drilling too many or to few wells, well locations, well density, spacing unit sizes, production allowables, and gas-oil ratios, etc.

The statutory and administrative compulsory pooling rules and orders are a proper and necessary exercise of the police powers of the State of New Mexico. The NMOCD has jurisdiction to interpret, clarify, amend and supplement is own orders and to resolve any challenges to the public issue of conservation of oil and gas.

The NMOCD is not being asked to resolve the "private rights" of the parties created under the 1951 GLA-46 Agreement. As the Division has already said in Order R-10878 when it previously compulsory pooled the GLA-46 Group's interest: "it is the Division's position that the interpretation of the GLA-46 Agreement should be deferred to the courts."

However, there is no dispute about the fact that the 1951 GLA-46 Agreement precludes the drilling of a necessary well. Burlington can recover only $45,000 from the GLA-46 Group for Mesaverde/Chacra wells which will cost more than $427,000 and for a Mesaverde well which will cost more than $386,000. and in doing so can only be paid out of 25% of the GLA-46 Group's share of that production. If the NMOCD believes that the cost limitations and carrying provisions of the GLA-46 Agreement still apply, then it is simply not possible in the year 2000 to drill new Mesaverde and Chacra wells under the economic constraints of 1973.

The Division has the authority and the responsibility to issue a compulsory pooling order in accordance with Section 70-2-17.C or Section 70-2-17.E NMSA (1978) in these cases so that these wells can be drilled under appropriate terms and conditions which will prevent waste and protect correlative rights.

RESPECTFULLY SUBMITTED:

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