

**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. 13598
ORDER NO. R-12581**

APPLICATION OF HUDSON OIL COMPANY OF TEXAS, WILLIAM A. HUDSON, AND EDWARD R. HUDSON FOR COMPULSORY POOLING, EDDY COUNTY, NEW MEXICO.

ORDER OF THE DIVISION

BY THE DIVISION:

This case came on for hearing at 8:15 a.m. on June 8, 2006 at Santa Fe, New Mexico, before Examiner William V. Jones.

NOW, on this 6th day of July, 2006, the Division Director, having considered the testimony, the record, and the recommendations of the Examiner,

FINDS THAT:

(1) Due public notice has been given, and the Division has jurisdiction of this case and of the subject matter.

(2) Hudson Oil Company of Texas, William A. Hudson, and Edward R. Hudson ("Hudson" or "applicant") seeks an order pooling all uncommitted mineral interests from the base of the San Andres formation to the base of the Morrow formation underlying the N/2 of Section 12, Township 17 South, Range 31 East, NMPM, Eddy County, New Mexico, in the following manner:

the N/2 to form a standard 320-acre spacing and proration unit for all formations and/or pools developed on 320-acre spacing within that vertical extent, which presently include but are not necessarily limited to the Undesignated Fren-Morrow Gas Pool (96663);

the NW/4 to form a standard 160-acre spacing and proration unit for all formations and/or pools developed on 160-acre spacing within that vertical extent; and

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the NW/4 NW/4 to form a standard 40-acre spacing and proration unit for all formations and/or pools developed on 40-acre spacing within that vertical extent, which presently include but are not necessarily limited to the **Undesignated** East Fren-Paddock Pool (97213);

(3) The above-described units (the "Units") are to be dedicated to the applicant's Francotte Federal Well No. 1 (API No. 30-015-34388) to be drilled at a location 660 feet from the North line and 660 feet from the West line (Unit D) of Section 12 to a vertical depth of approximately 12,500 feet to test any and all formations from the base of the San Andres formation to the base of the Morrow formation.

(4) Two or more separately owned tracts are embraced within the Units, and/or there are royalty interests and/or undivided interests in oil and gas minerals in one or more tracts included in the Units that are separately owned.

(5) Ard Oil, Ltd. and the Ard Energy Group, Ltd. ("the Ards") as parties to be pooled, entered an appearance and presented testimony at the hearing in opposition to this application.

(6) No other party entered an appearance in this case.

(7) Hudson presented the following testimony:

a) Hudson's geologist and owners proposed this well after examining records on surrounding Morrow wells. In particular, the active and prolific Morrow wells in the NW/4 of Section 11 and in the SE/4 of Section 2 were cited as analogous targets. No seismic data was used to locate this prospect.

b) Due to an agreement with Yates Petroleum Corporation ("Yates"), Hudson needs to spud the well by mid-August.

c) Hudson Oil Company of Texas functions as an operating company owned by William A. Hudson and Edward R. Hudson. The company is licensed and bonded as an operator in New Mexico. William A. Hudson and Edward R. Hudson own an interest in the proposed well. Hudson Oil Company of Texas does not own a direct working interest in this well.

d) Hudson obtained a verbal commitment from Marbob to drill this well because Marbob has better access to drilling rigs, Marbob also supplied the detailed drill cost estimate, which contains casing details. Production operations of the well would then revert to Hudson Oil Company of Texas. To date, there is formal contract with a drilling

contractor. No drilling prognosis was prepared.

e) Hudson provided an AFE and a JOA to prospective partners in this well.

f) Hudson Oil Company of Texas obtained a compulsory pooling order covering the S/2 of Section 12. The well did not produce from the 320-acre spaced Morrow formation and has been completed as a producer in the 40-acre spaced Yeso (Paddock) formation.

(8) The Ards presented testimony from a long-time business consultant as follows:

a) The Ards normally request additional information prior to agreeing to participate in wells in which costs to the Ards will be substantial. In this instance, a letter requesting additional information was mailed to Hudson in October of 2005. Normally these letters generate additional information, which is useful in a business sense. The Ards never received a satisfactory response from Hudson.

b) The Ards agree with Hudson that this original AFE is completely outdated and drilling costs have gone up tremendously since it was written.

c) The subpoena asking for information and the Ards appearing at this hearing are both attempts to increase the Ards' understanding of the reason to participate in the drilling of this well.

d) The Ards have concerns about Hudson's financial ability to fulfill financial requirements regarding Hudson's wells currently in operation and also concerns about Hudson's ability to prudently administer the Ards' portion of the costs for this well.

e) The Ards maintain that Hudson did not attempt to negotiate in good faith with the Ards and did not treat the Ards in an equitable manner as compared with other potential partners in this well.

(9) The examiner concludes that these two parties have not agreed to participate together in this venture. Hudson did supply an AFE and a JOA to the Ards and to all other parties owning an interest in these Units implying parties were likely treated equitably in regards to basic information.

(10) Both Hudson and the Ards agree that costs have dramatically gone up and the supplied AFE is too low, but neither knew how much. In order to allow for prudent

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business and planning decisions by all owners in the Units and after the date of this order, Hudson should be required to obtain a recent AFE and supply this to all parties owning an interest in these Units. The person preparing this AFE and that person's business affiliation should be identified in a cover letter sent along with this AFE.

(11) The applicant is an owner of an oil and gas working interest within the Units. Applicant has the right to drill and proposes to drill its Francotte Federal Well No. 1 at the above-described location.

(12) There are interest owners in the proposed Units who have not agreed to pool their interests.

(13) To avoid the drilling of unnecessary wells, protect correlative rights, prevent waste, and afford to the owner of each interest in the Units the opportunity to recover or receive without unnecessary expense its just and fair share of hydrocarbons, this application should be approved by pooling all uncommitted interests, whatever they may be, in the oil and gas within the Units.

(14) Hudson Oil Company of Texas should be designated the operator of the subject well and of the Units.

(15) Any pooled working interest owner who does not pay its share of estimated well costs should have withheld from production its share of reasonable well costs plus an additional 200% (pursuant to Rule 35.A) thereof as a reasonable charge for the risk involved in drilling the well,

(16) Reasonable charges for supervision (combined fixed rates) should be fixed at \$5500 per month while drilling and \$550 per month while producing, provided that these rates should be adjusted annually pursuant to Section III.1.A.3. of the COPAS form titled "*Accounting Procedure-Joint Operations*."

IT IS THEREFORE ORDERED THAT :

(1) Pursuant to the application of Hudson Oil Company of Texas, William A. Hudson, and Edward R. Hudson, all uncommitted mineral interests in all formations from the base of the San Andres formation to the base of the Morrow formation underlying the N/2 of Section 12, Township 17 South, Range 31 East, NMPM, Eddy County, New Mexico, are hereby pooled in the following manner:

the N/2 to form a standard 320-acre spacing and proration unit for all formations and/or pools developed on 320-acre spacing within that vertical extent, which presently include but are not necessarily limited to the Undesignated Fren-Morrow Gas Pool (96663);

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the NW/4 to form a standard 160-acre spacing and proration unit for all formations and/or pools developed on 160-acre spacing within that vertical extent; and

the NW/4 NW/4 to form a standard 40-acre spacing and proration unit for all formations and/or pools developed on 40-acre spacing within that vertical extent, which presently include but are not necessarily limited to the Undesignated East Fren-Paddock Pool (97213);

The above-described units (the "Units") shall be dedicated to the applicant's Francotte Federal Well No. 1 (API No. 30-015-34388) to be drilled at a location 660 feet from the North line and 660 feet from the West line (Unit D) of Section 12, to a vertical depth of approximately 12,500 feet to test any and all formations from the base of the San Andres formation to the base of the Morrow formation.

(2) Hudson Oil Company of Texas is hereby designated the operator of the subject well and of the Units.

(3) The operator of the Units shall commence drilling the proposed well on or before October 31, 2006 and shall thereafter continue drilling the well with due diligence to test the Morrow formation.

(4) In the event the operator does not commence drilling the proposed well on or before October 31, 2006, Ordering Paragraph (1) shall be of no effect, unless the operator obtains a time extension from the Division Director for good cause.

(5) Should the subject well not be drilled and completed within 120 days after commencement thereof, Ordering Paragraph (1) shall be of no further effect, and the Units created by this Order shall terminate unless the operator appears before the Division Director and obtains an extension of time to complete the well for good cause demonstrated by satisfactory evidence.

(6) Upon final plugging and abandonment of the subject well, the pooled Units created by this Order shall terminate, unless this order has been amended to authorize further operations.

(7) After pooling, uncommitted working interest owners are referred to as pooled working interest owners. ("Pooled working interest owners" are owners of working interests in the Units, including unleased mineral interests, who are not parties to an operating agreement governing the Units.)

(8) After the effective date of this order, the operator shall furnish the Division and each known pooled working interest owner in the Units an itemized

schedule of estimated costs of drilling, completing and equipping the subject well ("well costs"). The well costs estimate must be dated and no older than two months. The operator shall include with these well costs the name and business affiliation of the person creating the estimate.

(9) Within 30 days from the date the schedule of estimated well costs is furnished, any pooled working interest owner shall have the right to pay its share of estimated well costs to the operator in lieu of paying its share of reasonable well costs out of production as hereinafter provided, and any such owner who pays its share of estimated well costs as provided above shall remain liable for operating costs but shall not be liable for risk charges. Pooled working interest owners who elect not to pay their share of estimated well costs as provided in this paragraph shall thereafter be referred to as "non-consenting working interest owners."

(10) The operator shall furnish the Division and each known pooled working interest owner (including non-consenting working interest owners) an itemized schedule of actual well costs within 90 days following completion of the proposed well. If no objection to the actual well costs is received by the Division, and the Division has not objected within 45 days following receipt of the schedule, the actual well costs shall be deemed to be the reasonable well costs. If there is an objection to actual well costs within the 45-day period, the Division will determine reasonable well costs after public notice and hearing.

(11) Within 60 days following determination of reasonable well costs, any pooled working interest owner who has paid its share of estimated costs in advance as provided above shall pay to the operator its share of the amount that reasonable well costs exceed estimated well costs and shall receive from the operator the amount, if any, that the estimated well costs it has paid exceed its share of reasonable well costs.

(12) The operator is hereby authorized to withhold the following costs and charges from production:

- (a) the proportionate share of reasonable well costs attributable to each non-consenting working interest owner; and
- (b) as a charge for the risk involved in drilling the well, 200% of the above costs.

(13) The operator shall distribute the costs and charges withheld from production, proportionately, to the parties who advanced the well costs.

(14) Reasonable charges for supervision (combined fixed rates) are hereby fixed at \$5500 per month while drilling and \$550 per month while producing, provided

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that these rates shall be adjusted annually pursuant to Section III.1.A.3. of the COPAS form titled "*Accounting Procedure-Joint Operations*." The operator is authorized to withhold from production the proportionate share of both the supervision charges and the actual expenditures required for operating the well, not in excess of what are reasonable, attributable to pooled working interest owners.

(15) Except as provided in Ordering Paragraphs (12) and (14) above, all proceeds from production from the well that are not disbursed for any reason shall be placed in escrow in Eddy County, New Mexico, to be paid to the true owner thereof upon demand and proof of ownership. The operator shall notify the Division of the name and address of the escrow agent within 30 days from the date of first deposit with the escrow agent.

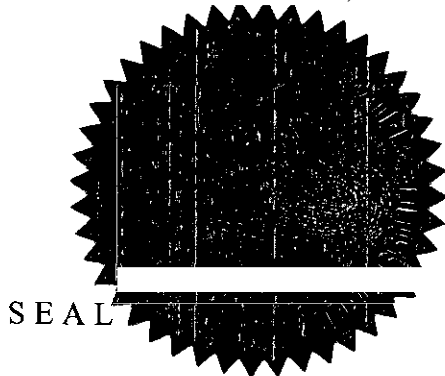
(16) Any unleased mineral interest shall be considered a seven-eighths (7/8) working interest and a one-eighth (1/8) royalty interest for the purpose of allocating costs and charges under this order. Any well costs or charges that are to be paid out of production shall be withheld only from the working interests' share of production, and no costs or charges shall be withheld from production attributable to royalty interests.

(17) Should all the parties to this compulsory pooling order reach voluntary agreement subsequent to entry of this order, this order shall thereafter be of no further effect.

(18) The operator of the well and the Units shall notify the Division in writing of the subsequent voluntary agreement of all parties subject to the forced pooling provisions of this order.

(19) Jurisdiction of this case is retained for the entry of such further orders as the Commission may deem necessary.

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



STATE OF NEW MEXICO
OIL CONSERVATION DIVISION

MARK E. FESMIRE, P.E.
Director