

May 16, 2001

Rule 37 Case No. 107137
District 2

APPLICATION OF MUELLER ENGINEERING CORP., FOR AN EXCEPTION TO STATEWIDE RULE 37 TO PLUG BACK WELL NO. 1, BLOCK 71 LEASE, CLAYTON, N.E. (1100), CLAYTON, N. E. (QUEEN CITY-A), CLAYTON, N.E. (QUEEN CITY-B-), CLAYTON (SLICK 6450), CLAYTON (SLICK 6500), CLAYTON (LULING), CLAYTON (MACKHANK 1), CLAYTON (MASSIVE), CLAYTON (BLOCK 72 SAND), CLAYTON (BLOCK 75 SAND), CLAYTON (BLOCK 85 SAND), CLAYTON (WILCOX 7360), AND WILDCAT FIELDS, LIVE OAK COUNTY, TEXAS.

APPEARANCES:

FOR APPLICANT:

Eduardo Riddle, President
Michael Mulvey

APPLICANT:

Mueller Engineering Corporation
” ” ”

FOR PROTESTANTS:

James R. Wagner, Jr., President

PROTESTANT:

White Creek Energy, Inc.

PROPOSAL FOR DECISION

PROCEDURAL HISTORY

APPLICATION FILED:

October 27, 2000

NOTICE OF HEARING:

December 22, 2000

HEARING DATE :

January 17, 2001

HEARD BY:

Meredith Kawaguchi - Hearings Examiner
Thomas Richter - Technical Examiner
Mark Helmueller - Hearings Examiner
Donna Chandler - Technical Examiner

PFD PREPARED BY

TRANSCRIPT DATE:

May 14, 2001

PFD CIRCULATION DATE:

May 16, 2001

Statement of the Case

Mueller Engineering Corporation (“Applicant” or “Mueller”) has applied for an exception to Statewide Rule 37 to plug back Well No. 1 on the Block 71 Lease (“subject lease”) in the Clayton, N.E. (1100), Clayton N.E. (Queen City -A-), Clayton, N.E. (Queen City -B-), Clayton (Slick 6450), Clayton (Slick 6500), Clayton (Luling), Clayton (Mackhank 1), Clayton (Massive), Clayton (block 72 Sand), Clayton (Block 75 Sand), Clayton (Block 85 Sand), Clayton (Wilcox 7360), and Wildcat Fields, Live Oak County, Texas. The subject lease is a 20 acre parcel with no locations regular to lease lines. The well is located at the geometric center of the lease, 165 feet from the north and south lease lines and 1370 feet from the east and west lease lines. A copy of the plat filed with Applicant’s W-1 Application for Permit to Drill, Deepen, Plug Back or Re-Enter is attached.

Field rules for the Clayton, N.E. (1100), Clayton N.E. (Queen City -A-), Clayton, N.E. (Queen City -B-), Clayton (Slick 6450), Clayton (Slick 6500), Clayton (Luling), Clayton (Mackhank 1), Clayton (Massive), Clayton (Block 72 Sand), Clayton (Block 75 Sand), Clayton (Block 85 Sand), and Wildcat Fields set requirements of 467 feet minimum spacing to the nearest lease line. Field rules for the Clayton (Block 75 Sand) and the Clayton (Wilcox 7360) Fields require 933 feet minimum spacing to the nearest lease line. The application is protested by White Creek Energy, Inc. (“White Creek”), an offset operator.

Summary of Evidence and Positions of the Parties

Mueller’s application is based on both confiscation and economic waste. Mueller’s confiscation case is based on the legal subdivision exception to the rule 37 minimum spacing requirements. Mueller contends that the subject tract took its current size and shape in 1907, prior to the discovery of oil in the area. Mueller noted that the Commission previously determined that the subject lease was a legal subdivision and granted Rule 37 exceptions for all of the applied-for fields, with the exception of the Clayton (Wilcox 7360) Field.¹ The Final Order adopted a Finding of Fact that the subject lease took its present size and shape on September 12, 1907. The Final Order also adopted a Conclusion of Law that the subject lease is a legal subdivision entitled to a well to prevent confiscation. Mueller also argued that production from offsetting wells is currently draining reserves underlying its lease.

Mueller also argued that no prudent operator would drill a new well to recover the estimated reserves underlying its lease. Mueller estimated the current recoverable reserves underlying the subject lease in the primary target field, the Clayton (Wilcox 7360) Field at 225 mmcf. The estimated cost to plug back the existing well would be \$55,000.00, while the cost of drilling a new well would be \$425,000.00. Mueller claims that it is economical to drill a new well to recover the current estimated reserves, but provided no financial analysis to support its contention.

White Creek presented no evidence, but contended that it would be drained if the exception was granted. White Creek also noted that its offset wells are at regular locations.

¹ At Mueller’s request, Official Notice was taken of the Proposal for Decision and Final Order entered by the Commission in this docket on July 20, 1992.

Examiners' Opinion

Mueller seeks a permit to drill its well on a 20 acre tract which has no locations regular to the north and south lease lines. Mueller's proposed location is at the geographic center of the subject lease. Accordingly, the first issue is whether the 20 acre tract is a legal subdivision.

No new evidence was presented at this hearing addressing the legal subdivision issue. Absent any new evidence or protest, the examiners find that the tract took its current size and shape on September 12, 1907 and is a legal subdivision.

In order to justify an exception to spacing rules, Mueller must also show that it will be denied a fair chance to recover the oil and gas in or under its land, or their equivalents in kind. Mueller is seeking the first well on this lease in the Clayton (Wilcox 7360) Field. Generally, a refusal to permit the first well on a legal subdivision is confiscation as a matter of law. The size of the tract does not matter. *Benz-Stoddard v. Aluminum Company of America*, 368 S.W.2d 94 (Tex 1963). Additionally, Mueller presented an uncontested estimate that the current recoverable reserves underlying the lease in the Clayton (Wilcox 7360) Field total 225mmcf.

Mueller must also show that the proposed location is reasonable. There are no regular locations on the subject tract. Further, the applied-for location is at the geographic center of the Block 71 Lease. This is presumably the most reasonable well location. Finally, no evidence indicated that the proposed location was less reasonable than any other location on the lease.

It is the examiners' opinion that Mueller is entitled to an exception to Rule 37 to prevent confiscation. Mueller established that this would be the only well on a legal subdivision. Additionally, Mueller showed that the proposed irregular location was reasonable due to its presence at the geographic center of the lease. Accordingly, the examiners' recommend that Mueller's application for an exception to Rule 37 to prevent confiscation should be granted.²

Conclusion

Mueller is entitled to an exception to Rule 37 to prevent confiscation of hydrocarbons underlying its lease on a legal subdivision. Mueller established that the well would be the first well in the Clayton (Wilcox 7360) Field, that there are no regular locations, and that the proposed irregular location was reasonable due to its presence at the geographic center of the lease. Accordingly, the application should be granted.

Based on the record in this Docket, the examiners recommend adoption of the following Findings of Fact and Conclusions of Law.

² Because an exception is appropriate to prevent confiscation, it is no necessary to determine whether an exception is also necessary to prevent waste.

Findings of Fact

1. Mueller Engineering Corporation (“Applicant” or “Mueller”) has applied for an exception to Statewide Rule 37 to plug back Well No. 1 on the Block 71 Lease (“subject lease”) in the Clayton, N.E. (1100), Clayton N.E. (Queen City -A-), Clayton, N.E. (Queen City - B-), Clayton (Slick 6450), Clayton (Slick 6500), Clayton (Luling), Clayton (Mackhank 1), Clayton (Massive), Clayton (Block 72 Sand), Clayton (Block 75 Sand), Clayton (Block 85 Sand), and Wildcat Fields, Live Oak County, Texas.
2. The subject lease is a 20 acre parcel with no locations regular to lease lines. The well is located at the geometric center of the lease, 165 feet from the north and south lease lines and 1370 feet from the east and west lease lines. A copy of the plat filed with Applicant’s W-1 Application for Permit to Drill, Deepen, Plug Back or Re-Enter is attached.
3. Field rules for the Clayton, N.E. (1100), Clayton N.E. (Queen City -A-), Clayton, N.E. (Queen City - B-), Clayton (Slick 6450), Clayton (Slick 6500), Clayton (Luling), Clayton (Mackhank 1), Clayton (Massive), Clayton (Block 72 Sand), Clayton (Block 85 Sand), and Wildcat Fields set requirements of 467 feet minimum spacing to the nearest lease line. Field rules for the Clayton (Block 75 Sand) and the Clayton (Wilcox 7360) Fields require 933 feet minimum spacing to the nearest lease line.
4. The well is the only well on the subject lease in the applied-for fields.
5. Mueller’s application is protested by offset operator White Creek Energy, Inc.
6. The subject lease took its current size and shape on September 12, 1907.
7. Reserves exist beneath the subject lease that the mineral interest owners will not have an opportunity to recover without an exception to the spacing requirements of Rule 37.
 - a. The estimated recoverable reserves of natural gas in the Clayton (Wilcox 7360) Field is 250 mmcf.
 - b. The well will be the first well on the subject lease in the Clayton (Wilcox 7360) Field.
 - c. The proposed location is at the geographic center of the subject lease and is reasonable.
8. The proposed location is at the geographic center of the subject lease and is reasonable.

Conclusions of Law

1. Proper notice of hearing was timely given to all persons legally entitled to notice.
2. All things have occurred to give the Commission jurisdiction to decide this matter.
3. The 20 acre Block 71 Lease is a legal subdivision.
4. A well spacing rules exception is required to give Mueller a reasonable opportunity to recover its fair share of hydrocarbons from the Clayton, N.E. (1100), Clayton N.E. (Queen City -A-), Clayton, N.E. (Queen City - B-), Clayton (Slick 6450), Clayton (Slick 6500), Clayton (Luling), Clayton (Mackhank 1), Clayton (Massive), Clayton (Block 72 Sand), Clayton (Block 75 Sand), Clayton (Block 85 Sand), and Wildcat Fields

5. A well spacing rules exception is required to give Mueller a reasonable opportunity to recover its fair share of hydrocarbons from the Clayton (Wilcox 7360) Field.
6. An exception to Statewide Rule 37 is necessary to prevent confiscation.

RECOMMENDATION

The examiners recommend that the subject application be granted in the applied-for fields in accordance with the attached final order.

Respectfully submitted,

Mark J. Helmueller
Hearings Examiner

Donna Chandler
Technical Examiner