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*   KEY ISSUES: Surface location = surface mine      *
*               TUMCO. Alternatives; slant drill,   *
*               mine over producing well. Unusual   *
*               condition not proven.                *
*                                                     *
*   FINAL ORDER: RULE 37 EXCEPTION DENIED          *
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Rule 37 Case No. 0200363

**APPLICATION OF VERADO ENERGY, INC. FOR AN EXCEPTION TO STATEWIDE
RULE 37 TO DRILL ITS NO. 3 WELL, ED LOCKRIDGE GAS UNIT O/A LEASE, OAK
HILL (COTTON VALLEY) FIELD, RUSK COUNTY, TEXAS**

APPLICANT: Verado Energy Inc.

FOR APPLICANT: Mr. Glenn Johnson - Attorney
Mr. Gregg Mehringer
Mr. G. Lance Binder

PROTESTANT: Exxon Corporation

FOR PROTESTANT EXXON CORPORATION:
Mr. Tim George - Attorney
Mr. Robert E. Dreyling
Mr. William C. Morris, Jr.
Mr. Tim Cotter

PROCEDURAL HISTORY

Application Filed:	November 10, 1992
Notice of Hearing:	December 4, 1992
Hearing Held:	February 2, 1993
PFD Circulated:	May 7, 1993
Heard by:	David Clarkson, Hearings Examiner Donna Chandler, Technical Examiner

STATEMENT OF THE CASE

Applicant, Verado Energy Inc., is the operator of the 669.95 acre Ed Lockridge Gas Unit O/A located in Rusk County, Texas. Applicant is seeking to drill its fourth well on the unit. Protestant, Exxon Corporation, is the operator of the Tanner Gas Unit, due north of the Verado unit. The proposed well, the Ed Lockridge Gas Unit O/A No. 3, is a vertical well with a proposed completion in the Oak Hill (Cotton Valley) Field. Field rules require 933'/1867' spacing with 640 acre spacing and optional 320 and 160 acre units. The surface location is 346 feet from the easterly west line, and 933 feet from the north line.

Applicant is seeking an exception to Statewide Rule 37 (16 TEX. ADMIN. CODE §3.37), to prevent confiscation and waste.

DISCUSSION OF THE EVIDENCE

The Ed Lockridge Gas Unit O/A Lease is in Rusk County in an area of extensive lignite deposits. Applicant seeks a Rule 37 exception based not only on the prevention of waste of hydrocarbon resources but also to meet the stated purpose of the Texas Surface Mining and Reclamation Act, TEX. REV. CIV. STAT. ANN. Art. 5920-11 (Vernon, Supp. 1993), (the Act), as stated in Sec. 2, (5)(E), which is "to assure that the coal supply essential to the state's energy requirements and to its economic and social well-being is provided, and to strike a balance between protection of the environment and agricultural productivity and the state's need for coal as an essential source of energy."

Applicants' proposed surface location is in an area of potential surface strip mining by Texas Utilities Mining Company ("Tumco"). Testimony from Mr. Mehringer, the supervisor of construction and permitting for Tumco at this potential mine site, indicated that the remaining regular locations in the Unit fall within an area of possible future mining. Applicants' witness testified that a block of land with a surface area 600' x 600' would be left around a gas well in an area to be mined due to regulatory and operational constraints. Evidence shows the proposed exception location lies in a ribbon of land void of lignite deposits approximately 500' wide. This strip lies between potential future mining areas. No evidence was presented revealing how the area void of lignite was discovered.

The economic impact of a gas well in the mine area at a regular location was shown to be approximately \$1,243,000. This includes \$1,100,000 in lost lignite, \$90,000 in increased access costs (relocation of road and pipeline) and \$53,000 in additional operational cost incurred in moving the dragline.

Protestant did not counter the cost figures but showed that there is presently no permit or application filed for any mining activity over the Unit. Mining activities are permitted in the area of the Lockridge Unit through the year 2006. Planned mining activities in the area run through 2011.

Tumco testified that firm boundaries are known surrounding potential mining areas including the Lockridge Unit. No presently approved or pending application contains the Lockridge Unit in its mine plan area. Tumco noted that it expects to include it in an application to be filed in 1994.

Protestant noted several wells in the planned mine areas which have been drilled since Tumco acquired their leases. Tumco testified that mining around these existing wells was not their only alternative. Several alternatives were presented. Testimony showed that Tumco has plugged and abandoned wells to gain access to the lignite reserves. They have also mined over producing wells and then reset pipe to restore the well to productive status. Also, a directional well drilled from an area with no lignite to a regular bottomhole location would not interfere with mining operations because the kick-off point is well below 200 feet, the depth of Tumco's surface leases. Protestant presented evidence of two directional wells drilled in the last 10 years to the Cotton Valley Formation. Both wells were within 6 miles of the Lockridge Unit. Directional wells were shown to cost approximately \$200,000 more than a vertical well.

Tumco testified that they have lignite reserves to last beyond the economic life of the power generation facilities and that they have some flexibility in determining where to mine next. Plans which have been previously approved can be revised through a permit revision process if necessary. As noted earlier, no application has been made for the mine area covering the Ed Lockridge Unit.

No estimate of ultimate reserves under the Unit was made. An iso-ultimate map presented by both parties shows that a well at a regular location will recover approximately 1.6 BCF of gas. A well drilled at the applied for exception location would recover approximately 1.9 BCF with 327 MMCF coming from Protestant's tract.

EXAMINERS' OPINION

Applicant did not meet its burden of proof in proving either confiscation or waste. No estimate of ultimate reserves under the tract was made; denial of opportunity to recover its fair share was not shown. There was no showing negating regular locations which are available. The Protestant countered any potential problems due to mining operations at the regular surface location sites by presenting several options including directional drilling.

The necessity of the exception location based on waste was not proven. No "unusual condition" exists which differentiates the applied-for exception location from a regular location. In this situation, the possible surface impediments due to surface mining operations do not rise to the level of "unusual circumstances at the applied-for location" justifying an exception, particularly in light of the many alternate solutions presented.

FINDINGS OF FACT

1. Notice of hearing was sent at least ten days prior to the hearing on February 2, 1993, to all designated operators, lessees of record for tracts that have no designated operator, and owners of record of unleased mineral interests for each adjacent tract and each tract nearer to the well than the prescribed minimum lease-line spacing distance.
2. Applicant, Verado Energy Inc., the operator of the 669.9456 acre Ed Lockridge Gas Unit O/A, has applied on Form W-1 for a permit to drill Well No. 3 on the Ed Lockridge Gas Unit O/A. Applicant proposes to drill its well 346 feet from the easterly west line and 933 feet from the north line of the unit, and 933 feet from the northerly north line and 2,550 feet from the northerly east line of the survey. Applicant has applied for completion of its proposed well in the Oak Hill (Cotton Valley) Field. The spacing rules for this field are 933 feet from lease lines and 1867 feet between wells with 640 acre spacing and optional 320 and 160 acre units.
3. The proposed well would be the fourth unit well in the field.
4. Undrilled regular locations exist on the Ed Lockridge Gas Unit O/A for the applied-for field.
5. Applicant failed to show that a regular location would not provide the mineral interest owners a reasonable opportunity to recover their tract's fair share of hydrocarbons.
 - a. Without an estimate of the ultimate recoverable reserves of this unit, and having only the iso-ultimate estimates, no fair share calculation or determination that waste would occur can be made.
6. An exception to the lease line spacing rules for the applied-for fields is not necessary to give the mineral interest owners a reasonable opportunity to recover their fair share of hydrocarbons in the subject fields underlying the unit.
7. No showing of unusual conditions peculiar to the drillsite tract was made.

CONCLUSIONS OF LAW

1. Proper notice of hearing was timely given to all persons legally entitled to notice.
2. The application on Form W-1 was properly filed.
3. All things have occurred and have been done to give the Commission jurisdiction to decide this matter.

4. Denial of the application will not result in confiscation or waste.

RECOMMENDATION

The examiners recommend that the subject application be denied in accordance with the attached final order.

Respectfully submitted,

Donna Chandler, P.E.
Technical Examiner

David Clarkson
Hearings Examiner

DLC