
* KEY ISSUES: CONFISCATION *
* good faith claim to title *
* faulting *
* *
* *
* FINAL ORDER: R37 GRANTED *

RULE 37 CASE NO. 0213270

APPLICATION OF COASTAL OIL & GAS CORPORATION FOR AN EXCEPTION TO STATEWIDE RULE 37 FOR THE ADAME GU LEASE, WELL NO. 2, WILDCAT (00008001) FIELD, JEFFRESS, N.E. (VICKSBURG, LO.) (46091450) FIELD, JEFFRESS, N.E. (T, LO.-FB,A) (46091400) FIELD, JEFFRESS, N.E. (VICKSBURG T) (46091500) FIELD, JEFFRESS, N.E. (VICKSBURG T LO) (46091550) FIELD, JEFFRESS, N.E. (VICKSBURG L) (46091430) FIELD, HIDALGO COUNTY, TEXAS

APPEARANCES:

FOR APPLICANT:

Doug Dashiell (attorney)
Steve Salge
R. E. Hilty
Terry Payne

APPLICANT:

Coastal Oil & Gas Corporation

FOR PROTESTANT:

George C. Neale (attorney)
Sherrie Green

PROTESTANT:

Coates Energy Trust

PROCEDURAL HISTORY

Date of Hearing:	October 23, 1996
Transcript Received:	December 1, 1996
Heard By:	Meredith Kawaguchi, Legal Examiner Margaret Allen, Technical Examiner
PFD Circulation Date:	February 7, 1997
Current Status:	Protested

STATEMENT OF THE CASE

Coastal Oil & Gas Corporation ("Coastal") has applied to drill a second well, Well No. 2, on its 170.52 acre Adame Gas Unit in Hidalgo County, Texas. Coastal requests a Rule 37 permit for the following fields: the Jeffress, N.E. (Vicksburg Lo) Field, which is the primary objective; the Jeffress, N.E. (T, Lo-FB,A) Field; the Jeffress, N.E. (Vicksburg T) Field; the Jeffress, N.E. (Vicks. T-Lower) Field; the Jeffress, N.E. (Vicksburg L.) Field; and Wildcat (above 16,500').

Coastal proposes to locate the well 349' from its nearest lease line, whereas field rules for all applied-for fields require a distance of 467'. Therefore, a Rule 37 exception is necessary.

Coastal's application is protested by Coates Energy Trust ("Coates"). Coates owns a royalty interest and appears to own an unleased mineral interest below 13,710' under an immediately offsetting tract. Initially, Coastal challenged Coates' standing to protest but withdrew its objection after conceding that Coates probably has mineral ownership below 13,710' on the tract to the east of the Adame Gas Unit. Coates also claims ownership of a strip of land within the Adame Gas Unit on its eastern edge. This claim has resulted in a title dispute between Coastal and Coates that is now before the courts. The proposed well is not located on this disputed strip.

Before presenting its technical case on the merits, Coastal established its good faith claim to title to the disputed strip through deeds, oil and gas leases, and an affidavit of adverse possession. Coates did not contend that Coastal failed to prove a good faith claim to title. The parties recognize that the title question must be resolved by the courts.

DISCUSSION OF THE EVIDENCE

Coastal presented the only evidence concerning the merits of its Rule 37 application. Its case is based on confiscation; the issue of waste was not addressed.

The primary target, the Jeffress, N.E. (Vicksburg Lo) Field, was referred to throughout the hearing as the "W" sand. The lower Vicksburg in Hidalgo County is composed of a sequence of sands amid a series of down-to-the-basin and antithetic faults. Coastal designated four sand objectives in this area, the "W" sand being the deepest at approximately 13,400'.

The original recoverable reserves under the Adame Gas Unit in the "W" sand were 7.3 billion cubic feet ("BCF") of gas. Decline curve analysis indicates that the existing well, the Adame Well No. 1, will ultimately recover only 2 BCF. Because of faulting in the upper lobe of the "W" sand, approximately 240' of section is missing from the Adame Well No. 1. Therefore, the net pay that is characteristic of that upper lobe in surrounding wells is not available to the Adame Well No. 1. An offset well, the Coastal E-1, is draining the area of the proposed well on the Adame Gas Unit. Ultimately, if this drainage continues unchecked, the Coastal E-1 will recover

approximately 2.9 BCF from under the Adame Gas Unit. (Total recovery for the Coastal E-1 is estimated to be 10.5 BCF.) There remain current recoverable reserves under the Adame Gas Unit that will be unrecovered by Coastal if Coastal does not drill a second well on the unit. Royalty owners within the Adame Gas Unit do not participate in production in the "W" sand from any offset well.

There are no regular locations that will afford the mineral owners an opportunity to recover their share of the hydrocarbons in the "W" sand. Due to extensive faulting in the area, a regular location to the east of the proposed location would encounter the downthrown side of Fault "E". All regular locations in the southern portion of the Adame Gas Unit fall in the middle of Fault "D".

If Coastal drilled at these regular locations, it would again lose a large section of the "W" sand, with significant decrease in the well's recoverable reserves. This loss of a large section of the reservoir combined with reduced net pay (less than 50') as one moves west in the reservoir on the southern portion of the tract make it impossible for applicant to recover its fair share from this portion of the tract. The net pay is approximately 50' at the proposed location.

EXAMINERS' OPINION

The examiners are of the opinion that an additional well on the Adame Gas Unit is necessary to protect the correlative rights of the Adame royalty owners, who do not share in production from the "W" sand from any offset well. Because of loss of a section of reservoir due to the fault, the existing well will recover only 2 BCF of the recoverable gas of 7.3 BCF under the Adame Gas Unit.

A Rule 37 location is necessary. Wells at regular locations would encounter the numerous faults and consequent loss of a portion of the reservoir. At such locations Coastal and its royalty owners would not have an opportunity to recover the hydrocarbons under the Adame Gas Unit. The proposed Rule 37 location is reasonable. It is a location that offsets the Coastal E-1 well and counters the ongoing drainage of the Adame Gas Unit on the "W" sand. The proposed location is approximately 900' from the Adame Gas Unit's east lease line, which separates the applicant's and protestant's leases.

Coastal did not present any evidence of the amount of recoverable reserves under the Adame Gas Unit in the Jeffress, N.E. (T, LO.-FB,A), Jeffress, N.E. (Vicksburg T), Jeffress, N.E. (Vicksburg T Lo), and Jeffress, N.E. (Vicksburg L) Fields. Similarly, Coastal did not present any evidence that a well at a regular location could not produce Coastal's fair share of these reserves.

FINDINGS OF FACT

1. At least ten (10) days notice of hearing was sent to all designated operators,

lessees of record for tracts having no designated operator, and owners of record of unleased mineral interests, for each adjacent tract and each tract nearer than 467' to the applicant's proposed well.

2. Coastal Oil and Gas Corporation, the applicant herein, has requested on Form W-1 a Rule 37 exception to drill Well No. 2 on the Adame Gas Unit in Hidalgo County, Texas. The proposed well will be 349' from the nearest lease line, whereas field rules for the applied-for fields require a distance of 467'.
3. Coastal's application is for the following primary objective: Jeffress, N.E. (Vicksburg Lo) Field ("the "W" sand"). Secondary objectives are Jeffress, N.E. (T, Lo-FB,A), Jeffress, N.E. (Vicksburg T), Jeffress, N.E. (Vicks. T-Lower), Jeffress, N.E. (Vicksburg L.), and Wildcat (above 16,500') Fields.
4. The existing well, the Adame No. 1, is incapable of producing all of the recoverable gas under the Adame Unit in the "W" sand.
 - a. The Adame Well No. 1 is expected to produce ultimately approximately 2 BCF of gas. Ultimate recoveries by adjacent wells producing from the "W" sand range from 19 BCF to 10.4 BCF.
 - b. The poor performance of the Adame No. 1 relative to the other wells in the field is attributable to a fault cut in the "W" sand.
5. A well at any regular location on the Adame Gas Unit could also be expected to be cut by a fault, lose a portion of the reservoir, and not recover the tract's reserves.
6. There are recoverable gas reserves of approximately 7.3 BCF under the Adame Gas Unit. The existing well will not recover 5.3 BCF under the Adame Gas Unit.
7. A well at the proposed location is necessary to allow penetration of the entire "W" sand interval and is necessary to give the mineral interest owners of the Adame tract a reasonable opportunity to recover the reserves under the tract.
8. Royalty owners of the Adame Gas Unit do not participate in production in the "W" sand from any adjacent well.
9. Regular locations exist on the Adame Gas Unit, and there is insufficient evidence that a Rule 37 location is necessary to recover the reserves, which were not quantified, in the Jeffress, N.E. (T, Lo-FB,A), Jeffress, N.E. (Vicksburg T), Jeffress, N.E. (Vicks. T-Lower), and Jeffress, N.E. (Vicksburg L.) Fields.
10. Applicant would not drill a well on the subject tract solely for the Wildcat (above 16,500').

CONCLUSIONS OF LAW

1. Proper notice was issued timely to all persons legally entitled to notice.
2. All things have been done or have occurred to give the Railroad Commission jurisdiction to decide this matter.
3. The applicant proved that Well No. 2 at the proposed Rule 37 exception location is necessary to give the mineral owners of the Adame Gas Unit an opportunity to recover their fair share of the hydrocarbons from the Jeffress N.E. (Vicksburg Lo) and Wildcat (above 16,500') Fields.
4. The applicant failed to establish that the applied-for location is necessary to recover the tract's reserves in the Jeffress, N.E. (T, Lo.-FB,A), Jeffress, N.E. (Vicksburg T), Jeffress, N.E. (Vicksburg T Lo), and Jeffress, N.E. (Vicksburg L) Fields.

RECOMMENDATION

The examiners recommend approval of Coastal's application to drill Well No. 2 at the proposed Rule 37 location on the Adame Gas Unit to encounter the "W" sand and the Wildcat Field. We recommend denial of the application in all other applied-for fields.

Respectfully submitted,

Meredith Kawaguchi
Legal Examiner

Margaret Allen
Technical Examiner

MFK/ds