

**KEY ISSUES: Confiscation
Failure to Negate Regular Location**

R37 DENIED

April 5, 2000

**Rule 37 Case No. 0222867
District 2**

APPLICATION OF UNION GAS OPERATING COMPANY FOR AN EXCEPTION TO STATEWIDE RULE 37 TO DRILL ITS NO. 1 WELL, JUNG GAS UNIT, ENKE (700), ENKE (800), KAREN BEAUCHAMP (PETTUS), KAREN BEAUCHAMP (VICKSBURG), KAREN BEAUCHAMP (YEGUA), KAREN BEAUCHAMP (YEGUA 4747), KAREN BEAUCHAMP (1650), KAREN BEAUCHAMP (1950), KAREN BEAUCHAMP (2100), KAREN BEAUCHAMP (2300), KAREN BEAUCHAMP (2400), KAREN BEAUCHAMP (2500), KAREN BEAUCHAMP (2600), KAREN BEAUCHAMP (2626), KAREN BEAUCHAMP (2700), KAREN BEAUCHAMP (2800), KAREN BEAUCHAMP (2900), KAREN BEAUCHAMP (3000), KAREN BEAUCHAMP (3200), AND WILDCAT FIELDS, GOLIAD COUNTY, TEXAS

APPEARANCES:

FOR APPLICANT:

John P. Moffitt - Geologist
Tio Newton - Landman

APPLICANT:

Union Gas Operating Company
" "

FOR PROTESTANT:

Steven C. Paulsgrove - Attorney
James Karnei

PROTESTANT:

James Karnei
" "

PROPOSAL FOR DECISION

PROCEDURAL HISTORY

APPLICATION FILED:

October 5, 1999

NOTICE OF HEARING:

October 29, 1999

HEARD BY:

Marshall Enquist - Hearings Examiner
Thomas Richter - Technical Examiner

HEARING DATE :

December 6, 1999

TRANSCRIPT DATE:

January 10, 2000

PFD PREPARED BY:

Mark Helmueller - Hearings Examiner

Thomas Richter - Technical Examiner

PFD CIRCULATION DATE:

April 5, 2000

Statement of the Case

Union Gas Operating Company ("Union Gas" or "Applicant"), seeks an exception to Statewide Rule 37 to drill its No.1 well, Jung Gas Unit, in the Enke (700), Enke (800), Karen Beauchamp (Pettus), Karen Beauchamp (Vicksburg), Karen Beauchamp (Yegua), Karen Beauchamp (Yegua 4747), Karen Beauchamp (1650), Karen Beauchamp (1950), Karen Beauchamp (2100), Karen Beauchamp (2300), Karen Beauchamp (2400), Karen Beauchamp (2500), Karen Beauchamp (2600), Karen Beauchamp (2626), Karen Beauchamp (2700), Karen Beauchamp (2800), Karen Beauchamp (2900), Karen Beauchamp (3000), Karen Beauchamp (3200), and Wildcat Fields, Goliad County, Texas. All the applied-for fields are subject to the Statewide Rule 37 spacing requirements of 467 feet minimum spacing to the nearest lease line and 1200 feet minimum spacing between wells. The subject lease is rectangular and locations regular to lease-lines are available. The proposed location is 177 feet away from the nearest lease line, as seen in the attached plat.

The Jung Gas Unit (the "Jung Lease" or "subject lease") comprises 84 acres as outlined on the plat attached to the Form W-1 (Application for Permit to Drill, Deepen, Plug Back, or Re-Enter) submitted by Union Gas on October 5, 1999. The proposed well on the subject lease is the first well in the applied-for fields.

Union Gas' application is protested by James Karnei ("Protestant"). Mr. Karnei is the mineral interest owner for the offset tract located to the southwest of the subject lease.

Applicant's Position and Evidence

Union Gas' application seeks a Rule 37 exception for 19 Commission recognized fields, as well as any Wildcat reservoirs encountered. However, Union Gas only submitted evidence for one of the Commission recognized fields, the Karen Beauchamp (Yegua) Field ("Yegua Field"). Union Gas argued that it required the exception location both to avoid a fault and to remain high on the Yegua structure. The subject Yegua Field could be either a pressure depletion drive or water drive.

Union Gas also produced a structural map of the Yegua Field underlying its Jung lease. The Yegua Field is bounded to the northwest by a fault with a 40' throw. Union Gas claims that any regular location northwest of the proposed location would be at a much higher risk of missing the Yegua Field due to the proximity of the fault. However, Union Gas' geologist could not state that the fault was a sealing fault in the Yegua Field. Finally, Union Gas presented no estimate of the recoverable reserves in the Yegua Field beneath the Jung Lease.

Protestant's Position and Evidence

Protestant is the mineral interest owner of the tract located to the immediate southeast of the

Jung Lease. Protestant contends that Union Gas chose the exception location as a reprisal for his refusal to extend his lease with Union Gas. Protestant also contends that Union Gas's exception location would drain substantial reserves from his adjacent tract. Finally, protestant argued that Union Gas failed to establish it was entitled to an exception location based on waste or confiscation.

Examiners' Opinion

The Commission may grant an exception to Rule 37 to prevent confiscation or to prevent waste. Applicant was unable to articulate whether it sought an exception to prevent waste or confiscation. However, it appears to the examiners that Union Gas' argument is best characterized as a claim that it is entitled to an exception to prevent confiscation in the Karen Beauchamp (Yegua) Field. In any event, Union Gas failed to submit evidence that an exception is necessary to prevent waste as it failed to show an unusual condition that would preclude recovery of hydrocarbons. Further, Union Gas submitted no evidence to support its application for an exception in the Enke (700), Enke (800), Karen Beauchamp (Pettus), Karen Beauchamp (Vicksburg), Karen Beauchamp (Yegua 4747), Karen Beauchamp (1650), Karen Beauchamp (1950), Karen Beauchamp (2100), Karen Beauchamp (2300), Karen Beauchamp (2400), Karen Beauchamp (2500), Karen Beauchamp (2600), Karen Beauchamp (2626), Karen Beauchamp (2700), Karen Beauchamp (2800), Karen Beauchamp (2900), Karen Beauchamp (3000), Karen Beauchamp (3200), and Wildcat Fields.

To establish entitlement to an exception to Rule 37 to prevent confiscation, an applicant must show that absent the applied-for well, it will be denied a reasonable opportunity to recover its fair share of hydrocarbons currently in place under the lease, or its equivalent in kind. The applicant must satisfy a two pronged test: 1) the applicant must show that it will not be afforded a reasonable opportunity to recover its fair share of hydrocarbons currently in place by drilling a well at a regular location; and 2) the applicant must show that the proposed irregular location is reasonable.

Because Union Gas only submitted evidence in support of its application for an exception in the Karen Beauchamp (Yegua) Field, it failed to establish entitlement to a Rule 37 exception for any of the other applied-for fields. Accordingly, the examiners recommend denial of the application for an exception in the Enke (700), Enke (800), Karen Beauchamp (Pettus), Karen Beauchamp (Vicksburg), Karen Beauchamp (Yegua 4747), Karen Beauchamp (1650), Karen Beauchamp (1950), Karen Beauchamp (2100), Karen Beauchamp (2300), Karen Beauchamp (2400), Karen Beauchamp (2500), Karen Beauchamp (2600), Karen Beauchamp (2626), Karen Beauchamp (2700), Karen Beauchamp (2800), Karen Beauchamp (2900), Karen Beauchamp (3000), Karen Beauchamp (3200), and Wildcat Fields.

Failure to Negate a Regular Location

It is the basic right of every landowner or lessee to a fair and reasonable chance to recover the oil and gas under his property as recognized by the Texas Supreme Court in *Gulf Land Co. v. Atlantic Refining Co.*, 131 S.W.2d 73, 80 (Tex. 1939). Denial of that fair chance is confiscation within the meaning of Rule 37. *Id.* Because an application cannot seek redress for past drainage, an applicant must provide evidence that it will not be afforded an opportunity to recover the reserves **currently** in place under its lease - this is its "fair share".

Union Gas' own evidence illustrated that viable regular locations exist on the Jung Lease. Though regular locations exist on the subject lease, Union Gas claimed that it could not drill anywhere but the proposed location due to an increased risk that the well would be faulted out. Union Gas' geologist could not state that the fault was a sealing fault in the Yegua Field.

Exceptions to Rule 37 are not granted to eliminate all risk for an operator, but to provide a reasonable opportunity to recover the oil and gas on an operator's lease. Union Gas' structure map of the Yegua Field depicts a regular location to the northwest of the proposed location which is within the confines of the reservoir and not faulted out. Union Gas was required to produce evidence to rule out any regular locations in order to justify its application for a Rule 37 exception. Union Gas failed to produce any such evidence and therefore failed to establish that an exception was necessary to afford it a reasonable opportunity to recover the reserves on its Jung Lease.

Additionally, Union Gas failed to prove that a well at a regular location in the Yegua Field would be adversely affected by the 40' fault depicted by Union Gas on its structure map. Union Gas admitted that it did not know if the fault was a sealing fault. Accordingly, Union Gas may still have a reasonable opportunity to recover its fair share of hydrocarbons in the Yegua Field even if it encounters the fault.

Finally, Union Gas provided no estimate of reserves for the Yegua Field. Without an accurate estimate of current reserves, or "fair share", there is no "benchmark" to measure against to determine whether a regular location will allow an applicant a reasonable opportunity to recover its fair share.

CONCLUSION

The evidence and legal authority presented establish that Union Gas is not entitled to a Rule 37 exception in order to prevent confiscation in any of the applied-for fields. The examiners therefore recommend that the subject application be denied.

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

FINDINGS OF FACT

1. At least 10 days notice of this hearing was given to the designated operator, all lessees of record for tracts that have a designated operator, all lessors of record for tracts that have no designated operator, and all owners of record of unleased mineral interests for each affected tract adjacent to the Jung Gas Unit ("subject lease") and each tract nearer to the proposed well location than the prescribed minimum distance.
2. The application for an exception to Statewide Rule 37 was originally filed with the Commission by Union Gas Operating Company. ("Union Gas") on Form W-1 (Application to Drill, Deepen, Plug Back or Re-Enter) on October 5, 1999.

3. Union Gas seeks an exception to Statewide Rule 37 to drill Well #1 on the subject lease to the Enke (700), Enke (800), Karen Beauchamp (Pettus), Karen Beauchamp (Vicksburg), Karen Beauchamp (Yegua), Karen Beauchamp (Yegua 4747), Karen Beauchamp (1650), Karen Beauchamp (1950), Karen Beauchamp (2100), Karen Beauchamp (2300), Karen Beauchamp (2400), Karen Beauchamp (2500), Karen Beauchamp (2600), Karen Beauchamp (2626), Karen Beauchamp (2700), Karen Beauchamp (2800), Karen Beauchamp (2900), Karen Beauchamp (3000), Karen Beauchamp (3200), and Wildcat Fields. All applied-for fields are subject to the Statewide Rule 37 spacing requirements of 467' minimum spacing to the nearest lease line and 1200' minimum spacing between wells. The subject lease is rectangular. Locations regular to lease-lines are available. The proposed well would be located 177' from the nearest lease line.
4. Union Gas' application is protested by James Karnei. Mr. Karnei is the mineral interest owner of an adjacent tract to the southwest of the subject lease.
5. Union Gas only presented evidence in support of its application for the Karen Beauchamp (Yegua) Field. Union Gas submitted no evidence to support its application for an exception in the Enke (700), Enke (800), Karen Beauchamp (Pettus), Karen Beauchamp (Vicksburg), Karen Beauchamp (Yegua 4747), Karen Beauchamp (1650), Karen Beauchamp (1950), Karen Beauchamp (2100), Karen Beauchamp (2300), Karen Beauchamp (2400), Karen Beauchamp (2500), Karen Beauchamp (2600), Karen Beauchamp (2626), Karen Beauchamp (2700), Karen Beauchamp (2800), Karen Beauchamp (2900), Karen Beauchamp (3000), Karen Beauchamp (3200), and Wildcat Fields.
6. There are regular locations on the subject lease that would encounter the targeted structural high in the Karen Beauchamp (Yegua) Field ("Yegua Field"). These locations are also south of a fault identified by Union Gas.
7. The fault identified by Union Gas has a throw of 40 feet. It is unknown whether the fault is a sealing fault in the Yegua Field.
8. Union Gas did not provide any estimate of the current recoverable reserves underlying the subject lease in the Yegua Field.
9. Regular locations exist on the subject lease which would give Union Gas a reasonable opportunity to recover the reserves currently underlying the subject lease in the Yegua Field.

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. Union Gas failed to rebut the presumption that a well location regular to lease lines will allow

it to recover the reserves currently in place under the subject lease.

4. A well spacing rules exception is not required to give Union Gas a reasonable opportunity to recover its fair share of hydrocarbons from the applied-for fields.
5. An exception to Statewide Rule 37 for a well at the applied-for location is not necessary to prevent confiscation.

RECOMMENDATION

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

Respectfully submitted,

Mark J. Helmueller
Hearings Examiner

Thomas Richter
Technical Examiner