

**RULE 37 CASE NO. 0229580
DISTRICT 02**

**APPLICATION OF BECKHAM RESOURCES, INC., FOR AN EXCEPTION PERMIT
UNDER STATEWIDE RULE 37 TO PLUG BACK WELL NO. 4, MITCHELL, JOHN N.
UNIT, MISSION RIVER FIELD, REFUGIO COUNTY, TEXAS**

APPEARANCES:

REPRESENTING:

FOR APPLICANT:

Jamie Nielson, Attorney
George C. Neale, Attorney
Mark Mathews, Attorney
Don Rhodes, Consultant
Greg Cloud, Consulting Engineer
Don Beckham, President

Beckham Resources, Inc.

FOR PROTESTANT:

Stephen Scanio, Agent
Jerry F. Johnson, Agent

Miguelita Scanio

PROPOSAL FOR DECISION

PROCEDURAL HISTORY

APPLICATION FILED:	September 24, 2001
PREHEARING CONFERENCE:	December 7, 2001
NOTICE OF HEARING:	January 18, 2002
DATE CASE HEARD:	February 22, 2002
HEARD BY:	James M. Doherty, Legal Examiner Donna Chandler, Technical Examiner
PFD CIRCULATION DATE:	April 11, 2002
CURRENT STATUS:	Protested

STATEMENT OF THE CASE

Beckham Resources, Inc. (“Beckham”), seeks an exception to Statewide Rule 37 for the plug back of its Well No. 4, John N. Mitchell Unit (“subject well”) to the Mission River Field, Refugio County, Texas. The Mission River Field is subject to Statewide Rules requiring spacing of 467 feet from lease lines and 1200 feet between wells. The subject well is 336 feet from the north lease line. The location of the subject well is 1200 feet from the nearest applied for, permitted, or completed well on the John N. Mitchell Unit in the Mission River Field. The John N. Mitchell Unit contains sufficient acreage to comply with applicable density requirements.

The application is protested by Miguelita Scanio, an unleased mineral owner of an offsetting tract to the northwest of the John N. Mitchell Unit and royalty owner in the John N. Mitchell Unit. The standing of Ms. Scanio to protest the application was challenged by Beckham at a prehearing conference in this docket on December 7, 2001, on the ground that Ms. Scanio’s offsetting tract is not within 600 feet of the subject well. Evidence presented at the prehearing conference did not show that Ms. Scanio’s interest would not be affected, and the examiner issued a prehearing ruling denying Beckham’s motion to disqualify Ms. Scanio’s protest. No further challenge to Ms. Scanio’s standing was made at the hearing.

At the hearing, Jamie Nielson, George C. Neale, and Mark Mathews, attorneys, Don Rhodes, consultant, Greg Cloud, consulting engineer, and Don Beckham, President, appeared on behalf of Beckham. Ms. Scanio was represented by Stephen Scanio and Jerry F. Johnson. No party requested the preparation of a transcript, and the hearing was tape recorded.

DISCUSSION OF THE EVIDENCE

Beckham’s Evidence and Position

Beckham is the assignee of a 1996 Oil and Gas Lease covering 791.34 acres of land out of the John Mitchell Estate, northeast of the Mission River in the Town of Refugio Survey, Abstract A-345 in Refugio County, Texas. Although the assignment and an area map of the John N. Mitchell Unit presented by Beckham referred to the Refugio Town Tract Survey, Abstract 56, the examiners have officially noticed from the General Land Office’s *Abstract of All Original Texas Land Titles Comprising Grants and Locations to August 31, 1941*, that Abstract 56 has been canceled and replaced by Abstract A-345. Mark Mathews, an attorney representing Beckham in oil and gas matters, has reviewed the lease and has the opinion that it continues in effect. The subject well is located on the 299.72 acre John N. Mitchell Unit. This unit was formed by Beckham in July, 2000, out of the original 791.34 acres covered by the aforementioned Oil and Gas Lease, pursuant to lease provisions requiring a designation of acreage around producing wells during the secondary term of the lease.

The subject well originally was drilled by another operator in late 1964 and completed in the

Mission River (8400) Field in January, 1965, with a producing section from 8,460 feet to 8,468 feet. The well originally was permitted at a regular location. The well produced 158.52 mmcf of gas from 1965 through 1967.

Beckham took its assignment of the aforementioned Oil and Gas Lease in April, 1999. When the 299.72 acre John N. Mitchell Unit was formed in July, 2000, Beckham, apparently through inadvertence, drew the unit boundary in such a way that the well's location was only 336 feet from the north line of the unit, thus creating the need for a Rule 37 exception.

The form W-2 for the recompletion of the subject well indicates that the well is currently perforated from 5,482 feet to 5,492 feet and from 5,783 feet to 5,793 feet. A cast iron bridge plug is set at 5,830 feet, with 20 feet of cement on top, shutting off the lower perforations through which the well previously produced. A 24 hour potential test on September 11, 2001, showed that the well pumped 9 BO, 1 mcf of gas and no water.

The Mission River Field was discovered in 1932 and has cumulative production of about 3.8 million BO. Beckham is the only operator in the field.

There are two wells, including the subject well, completed in the Mission River Field on the John N. Mitchell Unit. The only production data for the unit available to Beckham's consulting petroleum engineer was for September-October, 2001. Unit production for September 2001 was 121 BO, or about 4 BOPD, and 5 mcf of gas. Unit production for October 2001 was 101 BO, or about 3 BOPD, and 5 mcf of gas. Due to the limited production data available for the John N. Mitchell Unit, a decline curve was prepared for the nearby John Mitchell Lease to arrive at a decline rate of 5.6 % for use in projecting estimated ultimate recovery for the subject well. Extrapolation of production data available for the John N. Mitchell Unit using the 5.6 % decline rate developed an estimated ultimate recovery for the unit of 16,240 BO, and Beckham's consulting petroleum engineer estimated that each of the two wells on the unit would recover about 8,000 BO.

Beckham's consulting petroleum engineer also calculated the drainage area of the two wells on the John N. Mitchell Unit, using average porosity of 28.0 %, average water saturation of 30.0 %, and an oil formation volume factor of 1.15 reservoir barrels per stock tank barrel, all said to be typical of the Frio formation, and a recovery factor of 20 % based on the high permeability of this solution gas drive reservoir. Based on the previously calculated EUR for the John N. Mitchell Unit, the estimated per well recovery, and net pay of five feet, Beckham's consulting petroleum engineer expressed the opinion that the per well drainage area is six acres and the drainage radius of each well is 292 feet.

Beckham's consulting petroleum engineer concluded that a new well drilled on the John N. Mitchell Unit would cost about \$300,000.00, and no reasonably prudent operator would drill such a well to recover 8,000 BO. He also concluded that Well No. 1 on the John N. Mitchell Unit will not recover the reserves projected to be recovered by the subject well due to the limited drainage area of wells on the unit, and such reserves will not be recovered by any other existing well. Since

Ms. Scanio's offsetting unleased tract to the northwest is about 650 feet from the subject well, and the drainage radius of the subject well is calculated at only 292 feet, Beckham's consulting petroleum engineer has the opinion that Ms. Scanio will not be affected.

Beckham takes the position that its requested Rule 37 exception is necessary to recover hydrocarbons which will go unrecovered if no exception is granted (waste prevention).

Ms. Scanio's Evidence and Position

Ms. Scanio presented no evidence other than to call Don Beckham, Beckham's President, and to question him about the production history of the subject well and the timing of Beckham's request for a Rule 37 exception. Ms. Scanio protested the application because she was unsuccessful in getting desired information from Beckham. Having seen the evidence presented at the hearing, she "somewhat agrees" with what Beckham is saying, in particular that it is not economically feasible to drill another well on the John N. Mitchell Unit. However, Ms. Scanio continues to have reservations about the production history of the subject well and whether the lease assigned to Beckham remains effective.

EXAMINERS' OPINION

Beckham bases its application on the proposition that an exception to Rule 37 is necessary in order to prevent waste of hydrocarbons. An applicant seeking an exception to Rule 37 based on waste must demonstrate that: (1) unusual conditions, different from conditions in adjacent parts of the field, exist on the tract for which the exception is sought; and (2) as a result of these conditions, a substantial volume of hydrocarbons will be recovered by the well for which a permit is sought that would not be recovered by any existing well or by additional wells drilled at regular locations. *Hawkins v. Texas Co.*, 209 S.W.2d 338, 343-44 (Tex. 1948).

In *Exxon v. Railroad Commission of Texas*, 571 S.W.2d 497 (Tex. 1978), the Texas Supreme Court held that economic factors are relevant to a determination of whether a Rule 37 exception is necessary to prevent the waste of oil. The court held that "unusual conditions" are not limited to subsurface conditions and may include an existing wellbore when a new well would not be drilled at a regular location for economic reasons. *Exxon* at 501. Accordingly, the Commission may grant a Rule 37 exception if an existing wellbore for which the exception is sought will recover reserves that cannot be recovered by any other existing well and it is not economically feasible to drill a new well at a regular location. *Exxon* at 501-02; *Schlachter v. Railroad Commission of Texas*, 825 S.W.2d 732, 741 (Tex. Civ. App.-Austin 1992, writ denied). However, under the *Exxon* economic waste doctrine, an exception will not be granted merely upon a showing that the drilling of a new well will be uneconomic. The applicant must demonstrate that the existing well was drilled and completed in the original formation legitimately and in good faith and not as a subterfuge to bolster a later exception under Rule 37. *Exxon* at 501.

Here, the uncontroverted evidence shows that no existing well is capable of recovering, or

will recover, the reserves that are the target of the subject well as recompleted. This includes Well No. 1 on the John N. Mitchell Unit which is 1200 feet away from the subject well and has a drainage radius of only 292 feet. The uncontroverted evidence shows also that the reserves that will be recovered by the subject well, as recompleted, will not be recovered by any future well. The estimated ultimate recovery of the subject well is about 8,000 BO. The cost of drilling a new well to recover these reserves is about \$300,000.00. No reasonably prudent operator would make this expenditure to recover 8,000 BO. Drilling of a new well at a regular location to recover the reserves that will be recovered by the subject well, as recompleted, is not economically feasible.

The evidence shows also that the subject well was not drilled originally as a subterfuge to bolster a later exception under Rule 37. To the contrary, the evidence establishes that the well was drilled and completed in the original formation legitimately and in good faith. These conclusions are supported by the fact that the well originally was drilled by a previous operator in 1964 and produced 158.52 mmcf of gas from the Mission River (8400) Field. It appears that a Rule 37 exception was necessitated only when Beckham chose to draw the north boundary of the John N. Mitchell Unit in July, 2000.

In view of the limited drainage area of the subject well, Ms. Scanio's unleased mineral interest in the offsetting tract to the northwest will not likely be affected by the granting of the requested Rule 37 exception. While Ms. Scanio asserts continued reservations about the continued effectiveness of the assigned mineral lease held by Beckham, the evidence establishes that Beckham has at least a good faith claim of right to operate the John N. Mitchell Unit.

Accordingly, the examiners conclude that Beckham is entitled to an exception to Rule 37 to prevent waste, and recommend adoption of the following Findings of Fact and Conclusions of Law:

FINDINGS OF FACT

1. At least ten (10) days notice of hearing was sent to all affected persons, who, for tracts closer to the well than the greater of one-half (1/2) of the prescribed minimum between-well spacing distance or the minimum lease-line spacing distance, included the designated operator, all lessees of record for tracts that have no designated operator, and all owners of record of unleased mineral interests. Notice was sent to protestant Miguelita Scanio, and, in addition, notice was served by publication.
2. Beckham Resources, Inc. ("Beckham") seeks an exception to Statewide Rule 37 for the plug back of its Well No. 4, John N. Mitchell Unit, Refugio County, Texas ("subject well") to the Mission River Field.
3. The Mission River Field is subject to Statewide Rules requiring spacing of 467 feet from lease lines and 1200 feet between wells.
4. The existing wellbore for which an exception is sought is located on the 299.72 acre John

- N. Mitchell Unit and is 336 feet from the north line of the unit.
5. On April 1, 1999, Beckham received an assignment of a September 1, 1996, Oil and Gas Lease of a 791.34 acre tract which included the acreage now embraced by the John N. Mitchell Unit.
 6. The John N. Mitchell Unit was formed by Beckham in July 2000.
 7. The subject well originally was permitted at a regular location, drilled by a previous operator in late 1964, and completed in January 1965 in the Mission River (8400) Field.
 8. The subject well originally produced 158.52 mmcf of gas from the Mission River (8400) Field from 1965 through 1967.
 9. The subject well was plugged back by Beckham to the Mission River Field in 1999-2000.
 10. The Mission River Field was discovered in 1932, and cumulative production for the field is 3.8 million BO. Beckham is the only operator in the field.
 11. There are two wells completed in the Mission River Field on the John N. Mitchell Unit, the subject well and Well No.1. Well No. 1 is located 1200 feet from the subject well.
 12. Estimated ultimate recovery from the subject field for the two wells on the John N. Mitchell Unit, including the subject well as recompleted, is 16,240 BO. Each well will recover about 8,000 BO.
 13. The calculated drainage area in the subject field for the two wells on the John N. Mitchell Unit is six acres per well, and the drainage radius for each well is about 292 feet.
 14. Protestant Miguelita Scanio is a royalty owner under the John N. Mitchell Unit and the owner of an unleased mineral interest in a tract about 650 feet to the northwest of the subject well. This latter tract will not be drained by the subject well.
 15. No existing well will recover the reserves that will be recovered by the subject well as recompleted.
 16. The drilling of a new well at a regular location to recover the reserves that will be recovered by the subject well would cost about \$300,000.00.
 17. No reasonably prudent operator would drill a new well to recover 8,000 BO, the reserves that will be recovered by the subject well as recompleted.

18. If Beckham is not granted the requested Rule 37 exception permit, the reserves that would be recovered by the subject well will be wasted.

CONCLUSIONS OF LAW

1. Proper notice of hearing was timely issued by the Railroad Commission to appropriate persons legally entitled to notice.
2. All things necessary to the Commission attaining jurisdiction over the subject matter and the parties in this hearing have been performed.
3. Beckham Resources, Inc., has a good faith claim of right to operate the John N. Mitchell Unit.
4. The subject wellbore was drilled and completed in the original formation legitimately and in good faith and not as a subterfuge to bolster a later Rule 37 application in the recompletion zone.
5. The pre-existing wellbore for the subject well constitutes an unusual condition on the John N. Mitchell Unit within the meaning of *Exxon v. Railroad Commission of Texas*, 571 S.W.2d 497 (Tex. 1978).
6. Approval of Beckham's application for an exception to Rule 37 is necessary in order to prevent waste.

RECOMMENDATION

The examiners recommend approval of the application of Beckham Resources, Inc., for an exception to Statewide Rule 37 for the plug back of its Well No. 4, John N. Mitchell Unit, Refugio County, Texas, to the Mission River Field.

Respectfully submitted,

James M. Doherty
Legal Examiner

Donna Chandler
Technical Examiner