

RULE 37 CASE NO. 0254223
District 7C

APPLICATION OF MICHAEL D. LILLIS FOR AN EXCEPTION TO STATEWIDE RULE 37 TO DRILL THE BENGE LEASE, WELL NO. 5, MILLERSVIEW, W. (CAMAR SD.) FIELD, CONCHO COUNTY, TEXAS

APPEARANCES:

FOR APPLICANT:

Michael D. Lillis
Jay Fulfur

APPLICANT:

Michael D. Lillis

FOR PROTESTANT:

Royce D. Walker

PROTESTANT:

LeClair Operating Co., Inc.

PROPOSAL FOR DECISION

PROCEDURAL HISTORY

DATE APPLICATION FILED:

September 17, 2007

DATE OF NOTICE OF HEARING:

November 16, 2007

DATE OF HEARING:

January 9, 2008

HEARD BY:

James M. Doherty, Hearings
Examiner

Andres J. Trevino, Technical Examiner

DATE TRANSCRIPT RECEIVED:

January 25, 2008

DATE PFD CIRCULATED:

March 3, 2008

STATEMENT OF THE CASE

This is the application of Michael D. Lillis ("Lillis") for an exception to Statewide Rule 37 to drill the Benge Lease, Well No. 5, Millersview, W. (Camar SD.) Field, Concho County, Texas. The Millersview, W. (Camar SD.) Field is subject to statewide rules providing for 467' lease line and 1,200' between well spacing and 40 acre drilling units.

Proposed Well No. 5 will be the third well on the 240.47 acre Benge Lease in the Millersview, W. (Camar SD.) Field. The examiners have officially noticed the Commission's P-4 Inquiry Database which shows that the two existing wells in this field on the Benge Lease are the Benge Well No. 2 and the Benge Well No. 3. Lillis proposes to drill Well No. 5 at a location 500' from the west line and 1,175' from the north line of the Benge Lease. A between well spacing exception is required for Well No. 5 because the proposed location of the well is only 973' from

Benge Well No. 2 and 1,003' from Benge Well No. 3. A copy of the plat submitted with the Form W-1 filed by Lillis is attached to this proposal for decision as Appendix 1.

The application is protested by LeClair Operating Co., Inc. ("LeClair"), which is the operator of offset tracts to the west and south of the Benge Lease. Lillis is his own offset to the north and east of the Benge Lease.

DISCUSSION OF THE EVIDENCE

Lillis

Regular locations exist on the Benge Lease where a well might be drilled 467' or more from lease lines and 1,200' or more from the existing wells on the Benge Lease which are producing from the Millersview, W. (Camar SD.) Field. Lillis prefers not to drill at these regular locations based on his understanding of the geology of the area.

According to Lillis' geologist, in the Millersview, W. (Camar SD.) Field, the sands are progradating shore line sands complicated by a calcite cement caused by bioturbation. These are not clean sands and have pockets of porosity. Sand bars with thicker sands have the best chance of containing porosity.

Lillis' geologist believes that the LeClair well to the west, apparently the LeClair Barker No. 1, is on the same sand bar beneath Lillis' Benge Lease¹ and Lillis needs proposed Well No. 5 to offset the LeClair Barker No. 1 and to make adequate recovery of the Benge Lease reserves. The area being drained by the Barker No. 1 is not known with precision, but depending on porosity, this well theoretically could be draining the Benge Lease.² The existing Benge Lease Well No. 2 is thought to be too far away to offset the Barker well.

No accurate determination has been made of the current recoverable reserves under the Benge Lease, and only "very rough" calculations have been made of the estimated ultimate recovery of the two existing wells on the Benge Lease from the Millersview, W. (Camar SD.) Field. Lillis' geologist believes a "good estimate" of reserves in these wells would be 0.5 BCF per well, but the basis for this estimate is not clear.

¹ Lillis geologist testified that his opinion that the LeClair Barker No. 1 is on the same sand bar which underlies the Benge Lease is based on his "regional study" of several hundred wells.

² Based on the rudimentary plat submitted by LeClair, it appears that the Barker No. 1 is 467' off Lillis' lease line and approximately 1,000' southwest of the proposed location of the Benge No. 5. The Barker No. 1 presently is carried in the Millersview, W. (Cross Cut SD) Field, but LeClair believes that this is the same sand from which the Benge Lease wells produce.

Lillis' geologist, when questioned about isopach maps, stated that he had made "lots of different kinds of maps" from well data, but none that he wished to present as evidence because "it's a competitive area."

LeClair

On its offset tract to the west, LeClair operates the Barker No. 1 well, and to the southwest of the Benge Lease, LeClair operates the Mims No. 1 and has just logged the Barker 'A' well. To the south, and not directly offsetting the Benge Lease, is LeClair's Stansberry Lease, where LeClair operates the Stansberry Well Nos. 1, 2, and 3, and five other Stansberry wells further south. The Stansberry wells are carried in the Millersview, W. (Cross-Cut Sand) Field, but LeClair's reservoir engineer believes that well logs demonstrate correlation with the Millersview, W. (Camar SD.) sand.

About one year ago, LeClair constructed P/Z versus cum plots to estimate reserves for the Stansberry Well Nos. 1, 2, 3, 5, 6, 7, and 8, and estimated reserves of about 0.25 BCF to 0.33 BCF per well. Using log parameters for the Stansberry Well Nos. 1, 2, and 3, LeClair calculated a drainage area of 60 to 90 acres per well.³ Because of the correlation of sands in these wells with the Millersview (Camar SD.) sand, LeClair's reservoir engineer believes that Lillis' existing Benge Well Nos. 2 and 3 will drain the west side of the Benge Lease, and the Barker No. 1 will drain LeClair's offset acreage to the west. It is LeClair's position that if Lillis wants to drill another well on the west side of the Benge Lease, he should not be allowed to produce the well concurrently with the Benge No. 2 and the well should be located at least 1,200' from the Benge No. 3.

EXAMINERS' OPINION

An owner of oil and gas is entitled to an opportunity to recover the reserves underlying his tract, and any denial of that opportunity amounts to confiscation. *Atlantic Refining Co. v. Railroad Commission*, 346 S.W.2d 801 (Tex. 1961); *Imperial American Resources Fund, Inc. v. Railroad Commission*, 557 S.W.2d 280 (Tex. 1977). When the subject tract is capable of supporting a regular location, the applicant for a Rule 37 exception based on confiscation must prove that the proposed irregular location is necessary because of surface or subsurface conditions and that the proposed location is reasonable. To do this, the applicant must show that it is not feasible to recover its fair share of hydrocarbons from regular locations.

In addition, if a substantial amount of hydrocarbons will be produced by the proposed Rule 37 well that otherwise would ultimately be lost, a permit to drill the well may be justified to prevent waste. *Hawkins v. Texas Co.*, 209 S.W.2d 338, 343 (Tex. 1948). An applicant seeking an exception to Rule 37 based on waste must show that: (1) unusual conditions, different from conditions in

³ Lillis made the point that wells in this area of the field are not all alike. His Benge Lease wells and wells to the north of the Benge Lease are said to be better wells than wells to the south. Porosities in these wells average about 12.5%. These are tight sands, and wells must be frac'd to produce. So, Lillis disagrees with LeClair's calculation of average drainage areas for wells in the field.

adjacent parts of the field, exist under the tract for which the exception is sought; and (2) as a result of these unusual conditions, hydrocarbons will be recovered by the well for which the exception is sought that would not be recovered by any existing well or by an additional well drilled at a regular location; and (3) the amount of otherwise unrecoverable hydrocarbons is substantial.

The examiners are unable to conclude that the requested Rule 37 exception is necessary to prevent confiscation. Lillis apparently believes that the proposed well is needed to offset the LeClair Barker No. 1. However, the opinions expressed by Lillis' geologist about geology of the area and need for the proposed well are unsupported by any structure maps, structural cross sections, isopach maps, well logs, or reservoir engineering studies.⁴ The LeClair Barker No. 1 appears from a plat submitted by LeClair to be 467' from Lillis lease line. No drainage area calculations were presented for the Barker No. 1, and Lillis' geologist could not express an opinion as to what area this well might be draining, except to say that it was theoretically possible that the well might be draining gas from Lillis' Bengé Lease.

The proposed well would be the third well on the Bengé Lease in the Millersview, W. (Camar SD.) Field. No evidence was presented by Lillis to quantify the current recoverable reserves in this field under the Bengé Lease, and no engineering studies were presented as to the estimated ultimate recoveries from the field of the two existing wells on the lease, the Bengé Well Nos. 2 and 3. In addition, there are regular locations on the Bengé Lease where an additional well might be drilled to the Millersview, W. (Camar SD.) Field, and no persuasive evidence was presented by Lillis to condemn these regular locations.

To support its drainage theory, Lillis was required to show that the Bengé Lease suffers net uncompensated drainage, and that Lillis cannot recover his fair share of reserves without the proposed well. Current recoverable reserves are the measure of Lillis' fair share, and neither the amount of current recoverable reserves or net uncompensated drainage were proved. Without quantification of Lillis' fair share of reserves, and without proof that the existing wells on the Bengé Lease and additional wells that might be drilled at regular locations will not recover Lillis' fair share, the application may not be approved on a confiscation theory.

Lillis also failed to prove that an exception is needed for the proposed well to prevent waste. First, no unusual conditions beneath the Bengé Lease, different from conditions in adjacent parts of the field, were proved. In addition, Lillis did not prove, and really made no effort to prove, that the two existing wells on the Bengé Lease completed in the Millersview, W. (Camar SD.) Field or additional wells that might be drilled at regular locations on the lease, will be incapable of recovering the gas beneath the lease. There simply is no evidence that inability to drill Well No. 5 at the proposed location will result in the ultimate loss of any hydrocarbons.

Accordingly, based on the record in this case, the examiners recommend that the

⁴ Lillis presented no exhibits at the hearing.

Commission adopt the following Findings of Fact and Conclusions of Law.

FINDINGS OF FACT

1. At least ten (10) days notice of hearing was provided to all persons affected by this application.
2. Michael D. Lillis ("Lillis") requests an exception to Statewide Rule 37 to drill its Benge Lease, Well No. 5, in the Millersview, W. (Camar SD.) Field, Concho County, Texas.
3. The Lillis application is opposed by LeClair Operating Co., Inc., which is the operator of offset tracts to the west and south of the Benge Lease.
4. The Millersview, W. (Camar SD.) Field is subject to statewide rules providing for 467' lease line and 1,200' between well spacing and 40 acre drilling units.
5. Proposed Well No. 5 would be the third well on the 240.47 acre Benge Lease in the Millersview, W. (Camar SD.) Field. Existing wells in this field on the Benge Lease are the Benge Nos. 2 and 3.
6. Lillis proposes to drill proposed Well No. 5 at a location 500' from the west line and 1,175' from the north line of the Benge Lease. A between well spacing exception is required for the proposed location of Well No. 5 because the location is only 973' from the Benge No. 2 and 1,003' from the Benge No. 3.
7. Regular locations exist on the Benge Lease where a well might be drilled to the Millersview, W. (Camar SD.) Field that are 467' or more from lease lines and 1,200' or more from the existing wells in this field on the lease.
8. Lillis presented no structure map, structural cross section, isopach map, well log, or reservoir engineering study in support of its application.
9. Lillis did not establish the amount of current recoverable reserves in the Millersview, W. (Camar SD.) Field beneath the Benge Lease.
10. Lillis did not establish that the current recoverable reserves in the Millersview, W. (Camar SD.) Field beneath the Benge Lease cannot be recovered by the Benge No. 2 and 3 wells and/or additional wells that might be drilled at regular locations on the lease.
11. Lillis did not establish that proposed Well No. 5 is necessary to prevent net uncompensated drainage of reserves in the Millersview, W. (Camar SD.) Field from the Benge Lease.
12. Lillis did not establish that unusual subsurface conditions, different from adjacent parts of

the subject field, exist beneath the Benge Lease.

13. Lillis did not establish that drilling of Well No. 5 at the proposed location on the Benge Lease is necessary to prevent the ultimate loss of hydrocarbons.

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. Michael D. Lillis failed to prove that the granting of an exception to Statewide Rule 37 [Tex. R.R. Comm'n, 16 TEX. ADMIN. CODE §3.37] to drill the Benge Lease, Well No. 5, Millersview, W. (Camar SD.) Field, Concho County, Texas, is necessary to prevent confiscation or protect correlative rights.
4. Michael D. Lillis failed to prove that the granting of an exception to Statewide Rule 37 [Tex. R.R. Comm'n, 16 TEX. ADMIN. CODE §3.37] to drill the Benge Lease, Well No. 5, Millersview, W. (Camar SD.) Field, Concho County, Texas, is necessary to prevent waste.

RECOMMENDATION

The examiners recommend that the application of Michael D. Lillis for an exception to Statewide Rule 37 to drill its Benge Lease, Well No. 5, Millersview, W. (Camar SD.) Field, Concho County, Texas, be denied.

Respectfully submitted,

James M. Doherty
Hearings Examiner

Andres J. Trevino
Technical Examiner