

BEFORE THE CORPORATION COMMISSION  
OF THE STATE OF OKLAHOMA

**FILED**  
JUL 18 2013

**APPLICANT:**

**WAYNE A. LEAMON  
REVOCABLE TRUST AND  
JANE GOSS REVOCABLE  
INTER VIVOS TRUST**

COURT CLERK'S OFFICE - OKS  
) CORPORATION COMMISSION  
) OF OKLAHOMA

**RELIEF SOUGHT:**

**DRILLING AND SPACING  
UNITS**

) **CAUSE CD NO.**  
) **201202353**  
)

**LEGAL DESCRIPTION:**

**SECTION 2, TOWNSHIP 25  
NORTH, RANGE 11 WEST,  
ALFALFA COUNTY,  
OKLAHOMA**

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**REPORT OF THE OIL AND GAS APPELLATE REFEREE**

This Cause came on for hearing before **Paul Porter**, Administrative Law Judge for the Corporation Commission of the State of Oklahoma, on the 14<sup>th</sup>, 19<sup>th</sup> and 20<sup>th</sup> day of September, 2012, at 8:30 a.m. in the Commission's Courtroom, Jim Thorpe Building, Oklahoma City, Oklahoma, pursuant to notice given as required by law and the rules of the Commission for the purpose of taking testimony and reporting to the Commission.

**APPEARANCES:** **Gregory L. Mahaffey**, attorney, appeared on behalf of applicant, Wayne A. Leamon Revocable Trust and Jane Goss Revocable Inter Vivos Trust (collectively "Leamon"); **David E. Pepper**, attorney, appeared on behalf of Aexco Petroleum, Inc. ("AEXCO") and Northwest Energy Enterprises ("NEE")(collectively "AEXCO"); **Verland Behrens**, attorney, appeared on behalf of Gamble Trust and Martha Gamble ("Gamble Trust"); **Michael D. Stack**, attorney, appeared on behalf of Eagle Rock Mid-Continent Asset, LLC ("Eagle"); and **Jim Hamilton**, Assistant General Counsel for the Conservation Division, filed notice of appearance.

The Administrative Law Judge ("ALJ") filed his Report of the Administrative Law Judge on the 28<sup>th</sup> day of February, 2013, to which Exceptions were timely filed and proper notice given of the setting of the Exceptions.

The Appellate argument concerning the Oral Exceptions was referred to **Patricia D. MacGuigan**, Oil and Gas Appellate Referee ("Referee"), on the 19<sup>th</sup> day of April, 2013. After considering the arguments of counsel and the record contained within this Cause, the Referee finds as follows:

### **STATEMENT OF THE CASE**

**LEAMON TAKES EXCEPTION** to the ALJ's recommendation that the area should remain on 640 acre spacing because it is most conducive to Mississippi horizontal development.

The area at issue has been spaced on 640 acres for many years. Leamon wishes it respaced on 160 acres for the Oswego, Mississippi Chat and Mississippi Lime. There has been considerable Mississippi horizontal drilling in the area that has proved quite successful. There has been virtually no recent Mississippi vertical drilling in the area, and the few that were drilled, five or six miles away, proved marginal. The Eagle Rock Rose Newby #1 well in the SE/4 of Section 2 was a vertical Mississippi/Oswego well.

### **LEAMON TAKES THE POSITION:**

- 1) The Report of the ALJ is contrary to the law, fails to protect correlative rights, and fails to prevent waste of hydrocarbons.
- 2) The ALJ erred in denying the requested 160 acre spacing since the only engineering evidence indicates that the average drainage of an Oswego well is less than 160 acres. The existing Rose Newby #1 well will drain no more than 101 acres out of the Oswego and there are substantial unrecovered Oswego hydrocarbons for which the current owners have no plans to develop. The ALJ failed to acknowledge that there had been a change of knowledge of condition since the Commission established 640 acres spacing in the Oswego and Mississippi Lime Formation in May of 1974 before any wells had been drilled in the area. It appears that spacing Order No. 105169 prospectively spaced the Oswego formation and the Mississippi Lime before there was production history for either formation in the subject section or in the offsetting sections. This order extended in spacing Order No. 102799 dated January 24, 1974 wherein this Commission found "that one well will efficiently and adequately drain the hydrocarbons from each of the Common sources of supply covered by the applications underlying 640 acres..."

Obviously the Commission's finding in 1974, as perpetuated by the subject spacing Order No. 105169, was incorrect. Mr. Jon Stromberg, the only petroleum engineer to testify in this cause, testified that the actual drainage of the Rose Newby #1 well, if you allocate 50% of the production to both the

Oswego and Mississippi Lime was 37 acres. However, he noted that if all production was allocated 100% to the Oswego, that it would drain 101 acres. Mr. Stromberg further testified that if he used the AEXCO isopach map with his allocation of production, the drainage of the well would only be 146 acres, thus leaving over 400 acres of undeveloped hydrocarbons in Section 2. Mr. Stromberg believed there was substantial amount of Oswego gas left unrecovered in place in Section 2 which can be economically recovered.

The owner of the majority interest in this unit, Eagle Rock, did not actively protest this case, initially, did not exchange any exhibits, and only showed up on the day of trial to assist AEXCO in cross examining witnesses. AEXCO is a newcomer to this section, it is not a record owner and it has purportedly signed a contract that allows it to acquire between 10.9 and 12.5 % of the working interest outside of the wellbore of the Rose Newby #1 well. AEXCO's geologist, Kim Eccles, testified that he would not recommend Oswego vertical drilling and the Oswego was not in his opinion viable on its own (ALJ Report, paragraph 17). Further while AEXCO says it had intentions to try to come in and drill a horizontal Mississippi well, Mr. Eccles stated on more than one occasion that he cannot guarantee that a horizontal well would ever be drilled and that decision will be made by other people within the AEXCO organization.

Section 2 is currently spaced for conventional, vertical drilling. On a vertical basis, had the Commission known that the Oswego and Mississippi Lime would not drain more than 160 acres in 1974, it never would have approved the initial 640 acres spacing but would have granted 160 acre spacing. Where an operator, as here, has no plans to pursue additional drilling for the Oswego and waste will occur by virtue of unproduced hydrocarbons left in the ground, it is appropriate for this Commission to decrease the size of the spacing units. (See *Union Texas Petroleum v. Corporation Commission*, 651 P.2d 652 (Okl. 1981), and *Union Oil Company of California v. Brown*, 641 P.2d 1106 (Okl. 1981).

3) The ALJ failed to deal appropriately with the existing vertical spacing and speculated that there would be future horizontal development and/or horizontal spacing. 52 O.S. Section 87.1 prohibits spacing units larger than 80 acres for oil at a depth of 4,000 feet down to 9,990 feet. Mr. Eccles, geologist for AEXCO testified he expected the Mississippi to be predominately oil. Based upon such reservoir characteristics, the Mississippi Lime should have been spaced no larger than 80 acres back in 1974, not 640 acres. While AEXCO and others may have prospective plans for horizontal drilling, no one has filed an application for horizontal Mississippi spacing units in Section 2.

The only application before this Commission regarding spacing is this application which concerns existing vertical spacing Order No. 105169 and the appropriate size units, should future vertical wells be drilled. Based upon the

overwhelming engineering and geologic testimony, there are substantial amount of unrecovered Oswego and Mississippi Lime hydrocarbons underlying Section 2, a vertical well will either be a gas well that drains less than 160 acres for the Oswego formation, a gas well that drains less than 160 acres for the Mississippi Lime (per Mr. Jon Stromberg) or an oil well (per Mr. Kim Eccles) that will drain substantially less than 80 acres. As noted by the Supreme Court in the *Union Texas Petroleum v. Corporation Commission* case, supra, "protestants and applicants differ more in their proposed solutions to future equitable production than in substantive differences as to past and present known conditions of the Mississippi."

Such is the situation in this case. Leamon and Protestants both agree that the existing wells will have limited drainage and additional drilling is needed. There is only a dispute on whether it should be developed by despadding to 160 acre units or speculative increase density drilling. The Supreme Court went on to say in the *Union Texas Petroleum v. Corporation Commission* case, supra, that:

Protestant's desire to have further development on an increased density basis upon application by an owner of a unit when he determines that such action should be taken. The Commission concluded leaving that decision to the individual unit owners, under these circumstances, amounts to an indirect delegation of its duty to oversee prevention of waste and protection of correlative rights....the Commission concluded that 160 acre units were reasonably required to drain the reservoir effectively and efficiently, notwithstanding the recognized existence of alternate forms of relief that may be available based upon the substantial evidence submitted.

An identical situation exists herein and this Commission should take the same course of action that it took in the *Union Texas* case and grant 160 acre spacing, placing back in the hands of the mineral owners and the Commission the proper development of the Oswego Formation and Mississippi Lime in this section, which 160 acre spacing would have occurred initially had the Commission properly spaced the Oswego/Mississippi back in 1974.

4) The ALJ failed to note that all mineral owners are in support of the spacing, including the drill site mineral owners, the Gamble Trust, and that the spacing will not affect the working interest ownership in the wellbore of the Rose Newby #1 well. As noted by the testimony of both Mr. McLinn, contract land man on behalf of Leamon, owners of 320 mineral acres in the W/2, and by Mr. Holliman, land man for AEXCO, there are no mineral owners opposing this application. In fact, all mineral owners appear to be in support of this

application including the Gamble Trust, owners of the minerals in the drill site, SE/4, and represented by separate counsel. Further, it was undisputed that the interest of the leasehold owners appears to be undivided in this section and, thus, whether the unit is spaced on 640 acres or on 160 acres, such leasehold owners will continue to own the same interest within the Rose Newby #1 well. The only potential loss by the leasehold owners could be some leasehold rights outside the drill site quarter section. The fact that AEXCO or Eagle Rock may lose leases outside the drill site should not affect the Commission's decision here to despace the subject unit, such that waste of hydrocarbons can be prevented. As noted by the Supreme Court in *Union Oil Company of California v. Brown*, supra:

Appellant contends the Corporation Commission's order unnecessarily destroyed a vested right embodied in an oil and gas lease. Such a contention is not persuasive of the error alleged. The Commission did not act to change appellant's vested rights in its lease. The Commission granted relief from the continued existence of a 640 acre space unit shown to be productive of oil. The oil and gas conservation statutes specifically disapprove of units of that size productive of oil....Appellant's claim of unnecessary destruction of his vested rights must then rest in his lease contract. However, the Corporation Commission's deletion of the one section unit and subsequent formation of four separate units thereon does not interfere, or even touch upon, the appellant's lease or the parties' contract rights. In effect, the unit previously created has suspended the lessor's ability to enforce certain of the provisions of the contract against appellant....When the leases were tied into a unit of a section, the lessors' ability to demand a release for failure of production of paying quantities from the leased premises after the primary term was suspended by operation of law. The reformation of the larger unit into four units does nothing except remove the lessor's inability to enforce the contract. Consequently, it is determined here that the complained of respacing is statutorily authorized and is not a prohibited interference with the lessee's rights.

Here, Leamon met their burden of proof to show that there is a substantial amount of unrecovered hydrocarbons in both the Oswego and Mississippi Lime underlying Section 2; that the existing well will drain less than 160 acres; that there is no guarantee that AEXCO or any other existing working interest owner is going to drill an additional well in the future to

develop such hydrocarbons (no additional well has been drilled in over 30 years); and that this Commission should despace these formations to the size and shape of units that should have been created in 1974. By despacing to 160 acres, the mineral owners can obtain additional development and prevent the waste of these valuable hydrocarbons. Whether or not AEXCO and Eagle Rock lose some of their existing leases is immaterial to this Commission's decision.

5) Leamon requests that the Report of the ALJ be reversed and that 160 acre spacing be established for the Oswego and Mississippi Lime effective September 1, 2012.

**THE ALJ FOUND:**

1) This area has long been spaced on 640 acres and has one producing well. There is uncertainty about its production. There is no vertical drilling looking for Mississippi or Oswego production in the general area. Several surrounding sections have been spaced on 640 acres to enhance Mississippi horizontal development. AEXCO acquired 1,500 acres in the area for the specific stated purpose of developing Mississippi horizontal projects. They have taken several steps, including a geologic study and filing for increased density drilling authority in pursuit of their project.

2) Area information from 19 horizontal wells found they produce about 21,000 BO and 1.7 BCFG, more impressive production than any vertical Mississippi production in the area. Chesapeake did drill a couple of Mississippi vertical wells five or six miles away in 2006 which have both proved to be marginal wells. There is much evidence presented in this and virtually every other application to the Commission for the last few years that a longer lateral has the enhanced opportunity to produce more hydrocarbons than a vertical well. The horizontal portion of the bore hole encounters more of the productive formation and more natural frac's where fracture stimulation will increase production. Frac'ing techniques have greatly improved production.

3) Since the predominant reasoning for reducing the spacing from 640 acres to 160 acre is to allow vertical projects, there seems little support for the despacing application. It was mentioned several times during the hearing that one possible result of despacing would be to allow new leasing opportunities. Insufficient evidence was submitted, either way, on this subject. It is treated as speculation, although money does often motivate people to action. To change existing spacing would not prevent waste. Because Leamon has not presented sufficient evidence to meet its burden to despace the 640 acre unit and respace it as 160 acre units, the ALJ recommended the application be denied and the 640 acre spacing remain.

## POSITIONS OF THE PARTIES

### LEAMON

- 1) **Gregory L. Mahaffey**, attorney, appearing on behalf of Leamon, notes that the Leamons are mineral owners in a 320 acre tract in the W/2 of Section 2.
- 2) Leamon contends that a change of condition has occurred and thus the spacing order should be critically re-evaluated.
- 3) Leamon notes that all the mineral owners within the section at issue are either in support of the application or are not in opposition. Also, the only protest to the application came from AEXCO, who was not an owner of record when the application was filed. AEXCO's interest had been farmed-out prior to Leamon's filing.
- 4) Leamon notes that all the data relating to the Mississippi and Oswego reservoirs in the section at issue was acquired after May 10, 1974, the date on which the current drilling and spacing unit was created by Order No. 105169. Leamon argues that this constitutes a substantial change in condition since all of the reservoir information has been accumulated since the spacing order was issued. One well will not drain the hydrocarbons from 640 acres.
- 5) Leamon directs the court's attention to the testimony of petroleum engineer Jon Stromberg who stated that there had indeed been a change of condition since May of 1974 regarding one well's ability to effectively drain hydrocarbons from the 640 acre section.
- 6) Leamon argues that, based on Mr. Stromberg's testimony, the proper spacing for Section 2 would be on a 160 acre basis, rather than its current 640 acre spacing. Mr. Stromberg testified that the existing vertical Newby Rose #1 well would only drain 101 acres from the Oswego reservoir, leaving a significant amount of hydrocarbons unrecovered. Also, according to the testimony of Mr. Eccles, a vertical well in the Mississippi reservoir would only drain several acres. Leamon argues that the ALJ erred by not considering these facts as evidence for a change in condition.
- 7) Leamon also notes that, according to Mr. Eccles, the Mississippi reservoir would produce oil rather than natural gas. Because the Mississippi is between 4,000 and 10,000 feet in depth, statutes require that the section should not be spaced larger than 80 acres.
- 8) Leamon argues that AEXCO has no plans or desire to develop the Oswego. Further, the current operators have had several decades to drill additional wells since the spacing order was issued and have neglected to do

so. This should then result in the mineral owners regaining control of their minerals and thus spurring new development in the section.

9) Leamon examines the proper role of the Commission by relying on *Union Oil Co. v. Brown*, 641 P.2d 1106 (Ok. 1981); which held that the Commission's charge is to prevent the waste of hydrocarbons and protecting correlative rights, with the latter yielding to the former. Leamon also relies on *Union Texas Petroleum v. Corp. Comm'n*, supra, which contains facts similar to the present case. There the Court determined that a substantial change in condition or knowledge of conditions had taken place and that de-spacing to a 160 acre basis would be the best approach to prevent waste and would allow the mineral owners to find an operator that would develop the section.

10) Leamon again notes that all of the mineral owners in the section are in support of the 160 acre spacing and argues that the ALJ erred by neglecting to take this into account.

11) Leamon argues that the Oswego underlies the entire section but that AEXCO has no plans to actively develop this formation. Speculation that AEXCO or another operator could possibly drill a horizontal well in the area should form no basis for the Commission to deny spacing in this situation. Rather, the Commission should consider the current vertical spacing and the proper size for development.

12) Leamon concludes by arguing that the decision of the ALJ be reversed and that the Commission should follow *Union Texas* by ignoring the possible loss of the operator's leases and respace the section on a 160 acre basis.

### **AEXCO**

1) **David E. Pepper**, attorney, appearing on behalf of AEXCO, disputes Leamon's assertion that there has been no development activity by the existing owners for the past 30 years. AEXCO notes that they recently filed an increased density application in the section soon after they acquired their interest.

2) AEXCO argues that this case falls under the ruling in *Winter v. Corp. Comm'n*, 660 P.2d 145 (Ok.Civ.App. 1983); which holds that, "Having been given a choice of remedies, it is incumbent upon the Commission to use the remedy which will prevent waste and protect correlative rights."

3) AEXCO notes that even if all the relevant mineral owners support the applicant's despadding request, that fact is irrelevant to the Commission's

decision. AEXCO contrasts the mineral owner's agreement by noting that 100 % of the working interest owners support development through increased density rather than respacing.

4) AEXCO points to the testimony of the Leamon's geologist, Mr. Stromberg, who admitted that three new vertical wells would be necessary in order to fully develop the section under a 160 acre basis. He also stated that there was significant activity in horizontal exploration of the Mississippian in the general area. AEXCO disputes the idea that the Mississippi formation will be developed using vertical wells and contends instead that any future development will certainly come from horizontal drilling.

5) AEXCO alleges that the strategy used by Mr. Mahaffey's in the present litigation is very similar to methods he used in prior cases. In these past cases, a mineral owner files an application to despace while at the same time the mineral owner files an application in District Court to cancel the lease for failure to produce in commercial quantities. AEXCO argues that this practice is used by mineral owners in order to release their leases so they can try to lease them to somebody else and get a cash bonus.

6) AEXCO notes that the working interest owners have already proposed a horizontal Mississippian well and have sought the Commission's approval for an increased density order so that the prospective well can be drilled.

7) AEXCO argues that the current 640 acre spacing would currently permit horizontal drilling and that if this section were respaced on a 160 acre basis it would have to be subsequently respaced in order for any future horizontal drilling to occur.

8) AEXCO points to the testimony of Mr. Eccles in which he argues that he would not drill three vertical wells targeting the Oswego formation based on his research and knowledge of the section's geology. He also testified that the vertical portion of the proposed horizontal well would be drilled in a location that would penetrate the Oswego for the purposes of production. AEXCO offers this testimony as evidence that they are indeed interested in the Oswego formation.

9) AEXCO notes several of the facts determined by the ALJ. AEXCO has a colorable interest in the property at issue. There have been no vertical Mississippi wells drilled in the general area since 1988. There are no vertical Oswego drilling projects in the nine section area. In the four township area there are 52 horizontal Mississippi projects on-going with at least 23 producing wells. Nineteen of those horizontal wells are producing on average 21,000 BO and 1.7 BCFG. AEXCO acquired 1500 acres for the purpose of pursuing a horizontal drilling program. AEXCO has requested increased density drilling authority. AEXCO has done a geological study of the area.

10) AEXCO argues that the Commission should determine the best method of development and asserts that the record clearly supports developing the section through a horizontal Mississippian well.

11) AEXCO concludes by requesting that the decision of the ALJ be affirmed by the Referee.

### **EAGLE**

1) **Michael D. Stack**, attorney, appearing on behalf of Eagle, agrees with Leamon that it is incumbent on the Commission to determine if there has been a substantial change in conditions which would justify the spacing application.

2) Eagle argues that the change of condition requirement has not been satisfied by the fact that there have been no vertical wells drilled targeting the Mississippi in the general area since 1988. There are no vertical Mississippi drilling projects in the nine-section area. However, there are 52 current horizontal Mississippi projects with 23 producing wells.

3) Eagle contests the idea that the section is spaced on a "vertical 640" acre basis. Eagle argues that no such designation exists and an operator can drill a horizontal well under this conventional spacing arrangement.

4) Eagle cites the decision in *Denver Production and Refinery Co. v. State*, 184 P.2d 961 (Okl. 1947) in which the Supreme Court held that "In most instances it is impossible to use a formula which will apply equally to all persons producing from a common source of supply. In striking a balance between conservation of natural resources and protection of correlative rights, the latter is secondary and must yield to the reasonable exercise of the former." Leamon argues the 640 acre spacing should be changed to 160 acre spacing, but then later AEXCO can come back and put it on a horizontal 640 spacing. Eagle argues that the action is, at its core, an attempt to cause the operators leases to expire.

5) Eagle concludes by examining the Commission procedural outline. This makes it clear that it is the ALJ's role to evaluate the expert witness testimony and to give it proper weight in making their decision. Eagle argues that there is no legal basis for finding fault with the ALJ's decision and it consequently should be upheld.

**RESPONSE OF LEAMON**

- 1) Leamon notes that if the spacing unit were decreased as Leamon's request, it would not prohibit an operator from drilling a horizontal well.
- 2) Leamon directs the courts attention to fact that a prior operator, Crow Creek, never indicated any desire to drill additional wells in Section 2, in spite of the wishes of the mineral owners.
- 3) Leamon argues that AEXCO's suggestion that they may possibly drill horizontal wells in the section is mere speculation. Leamon notes that, Mr. Eccles, in prior testimony, had admitted that the Oswego was likely productive but that AXECO had no concrete plans for development.
- 4) Leamon contends that the Commission should focus on the proper method of development for the section and not on whether the operators will lose their lease or be obligated to pay additional royalties. Leamon reiterates that the working interest owners would not be barred from developing the section.
- 5) Leamon argues that the section would likely be spaced on a different basis if the Commission had access to the same data that is available today at the time of the original spacing order.
- 6) Leamon argues that the spacing regime at the time only contemplated vertical wells and when the original spacing order for Section 2 was issued there was no exploration by the use of horizontal drilling, as the method had not yet been adopted by the industry.
- 7) Leamon notes that the Commission is not bound by the requests of the parties in its decision to enter new spacing. Rather, the Commission may take all the relevant evidence into account and enter whatever spacing it feels is appropriate.
- 8) Leamon points to the testimony of Mr. Stromberg who admitted that there is a significant amount of gas remaining in the reservoir and yet the mineral owners are not allowed to seek additional development because the section is held by production.
- 9) Leamon concludes by stating that a 160 acre spacing unit is the appropriate one and asks that the decision of the ALJ denying this spacing be reversed.

## CONCLUSIONS

**The Referee finds that the Report of the Administrative Law Judge should be affirmed.**

1) The Referee finds the ALJ's determination to recommend denial of the Leamon application to be supported by the weight of the evidence and free of reversible error. In order to modify the prior 640 acre spacing of Section 2, it was incumbent upon Leamon to establish a substantial change of conditions or change in knowledge of conditions since the issuance of prior Order No. 105169 on May 9, 1974. *Corporation Commission v. Phillips Petroleum*, 536 P.2d 1284 (Okl. 1975); and *Marlin Oil Corporation v. Corporation Commission*, 569 P.2d 961 (Okl. 1977).

2) As the Court stated in *Wood Oil Company v. Corporation Commission*, 239 P.2d 1021 (Okl. 1950):

...The exercise of the authority to modify the previous order necessarily involves a changed factual situation from that which obtained at the time of making the order sought to be modified.

3) In *Phillips Petroleum Company v. Corporation Commission*, 482 P.2d 607 (Okl. 1971); the Court stated:

The phrase "change in knowledge of conditions" (as would warrant a change by order) does not encompass a mere change of interpretation on the part of the Commission. Rather, it encompasses an acquisition of additional or new data or the discovery of new scientific or technical knowledge since the date of the original order was entered which requires a reevaluation of the geological opinion concerning the reservoir...

4) One hundred percent of the working interest owners support development through increased density rather than respacing. Leamon's geologist noted that three new vertical wells would be necessary in order to fully develop the section under a 160 acre basis. There has been significant activity in horizontal exploration of the Mississippian in the general area. Leamon's expert admitted there hadn't been any vertical wells drilled in the Mississippian in a number of years. In 2006 Chesapeake drilled some vertical Mississippi wells but they were very marginal wells. There has been significant activity in horizontal exploration of the Mississippian in the general area.

AEXCO has already sought Commission's approval for an increased density order so that the prospective horizontal Mississippian well can be drilled in Section 2. AEXCO has already received increased density in T25N-R11W to drill a horizontal well. AEXCO's engineer also stated that he would not drill three vertical wells targeting the Oswego formation but the vertical portion of the proposed horizontal well would be drilled in a location that would penetrate the Oswego for the purposes of evaluating prospective production.

5) There have been no vertical Mississippian wells drilled in the general area since 1988. There are no vertical Oswego drilling projects in the nine section area. In the four township area there are 52 horizontal Mississippian projects ongoing with 23 producing wells. Nineteen of those horizontal wells are producing on average 20,974 BO per well and have made 1.7 BCFG. AEXCO has purchased 1500 acres for the purpose of pursuing a horizontal drilling program.

6) The ALJ is the trier of fact. It is the ALJ's duty as the trier of fact to observe the demeanor of the witnesses, assess their credibility and assign the appropriate weight to their opinions. *Grison Oil Corporation v. Corporation Commission*, 99 P.2d 134 (Okl. 1940). The ALJ also weighed the expert opinion espoused before him and found the AEXCO opinion to be worth greater weight. *Haymaker v. Oklahoma Corporation Commission*, 731 P.2d 1008 (Ok1.Civ.App. 1986); and *Downs v. Longfellow Corporation*, 351 P.2d 999 (Okl. 1960).

7) The Referee also finds that the ALJ's recommendation to deny Leamon's application for 160 acre spacing prevents waste. The Supreme Court in *Denver Producing & Refining Company v. State*, 184 P.2d 961 (Okl. 1947) found:

...In striking a balance between conservation of natural resources and protection of correlative rights, the latter is secondary and must yield to a reasonable exercise of the former.

It is the Referee's opinion that the facts in the instant cause require the spacing be left on a 640 acre basis as it conforms to the principles of preventing waste.

8) Title 52 O.S. Section 87.1 provides in relevant part:

a) To prevent or to assist in preventing the various types of waste of oil or gas prohibited by statute, or any of said wastes, or to protect or assist in protecting the correlative rights of interested parties, the Corporation Commission, upon a proper application

and notice given as hereinafter provided, and after a hearing as provided in said notice, shall have the power to establish well spacing and drilling units of specified and approximately uniformed size and shape covering any common source of supply, or prospective common source of supply, of oil or gas within the State of Oklahoma....

9) As stated in *Winter v. Corporation Commission of State of Oklahoma*, 660 P.2d 145 (Okl.Civ.App. 1983):

Having been given a choice of remedies, it is incumbent upon the Commission to use the remedy which will best prevent waste and protect correlative rights....

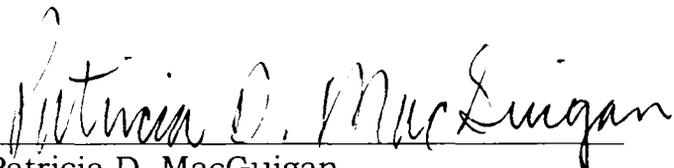
The Referee believes that the best method of development is horizontal drilling and asserts that the record fully supports such development. It has been pointed out in the evidence presented before the ALJ that despacing would allow new leasing opportunities which would allow Leamon to release their property to someone else and get additional compensation, which does not prevent waste or insure orderly development.

10) As stated by the Court in *Winter v. Corporation Comm'n of State of Oklahoma*, supra, at 147:

Prior spacing order No. 192841, entered on April 19, 1977, established Section 13 as a 640-acre drilling and spacing unit for the Mississippian (Mississippi solid) common source of supply underlying Section 13 and authorized the drilling of only one well in the unit. Both Withrow, et al. and Winter, et al. sought to modify the spacing order and were required to prove initially that there had been a substantial change of condition or substantial change in knowledge of conditions in the area since the prior order had been issued. If they were successful in establishing a substantial change of conditions or knowledge then they were required to prove, that their particular method of modifying the spacing order would either prevent waste or protect correlative rights (footnotes omitted).

11) Leamon failed to meet both burdens of proof, as it did not establish a change in knowledge of conditions in the area nor did it establish that its particular modification would prevent waste and allow for orderly development. The larger 640 acre unit is necessary to provide the necessary flexibility to properly locate the horizontal well and develop the common sources of supply. In the present circumstances, the weight of the evidence determined that a 640 acre unit will more properly obtain orderly development and best comport with the intent of the legislature in enacting the spacing law. The Referee therefore believes the ALJ's Report should be affirmed.

**RESPECTFULLY SUBMITTED THIS 18<sup>th</sup> day of July, 2013.**

  
Patricia D. MacGuigan  
OIL & GAS APPELLATE REFEREE

PM:ac

xc: Commissioner Douglas  
Commissioner Anthony  
Commissioner Murphy  
Jim Hamilton  
ALJ Paul Porter  
Gregory L. Mahaffey  
David E. Pepper  
Verland Behrens  
Michael D. Stack  
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