

FINAL

RULE B-40 - AUTHORIZATION FOR DIRECTOR OF PRODUCTION AND CONSERVATION TO ADMINISTRATIVELY APPROVE APPLICATIONS FOR EXCEPTIONAL WELL LOCATIONS

- a) The Director of Production and Conservation or his designee is authorized to issue a Drilling Permit for a well proposed to be drilled, is being drilled, or has been drilled, but prior to commencement of production, at a location within an established drilling unit, which fails to conform to the drilling unit setback distance requirements as measured from the approximate center of the wellbore to unit boundary lines under applicable field rules or Commission general rules. This rule is only applicable:
- (1) To dry gas wells drilled vertically or directionally and does not apply to any type of dry gas well drilled as a wildcat well, as defined in General Rule B-3, or for dry gas wells drilled in Exploratory Units established by Commission order; or
 - (2) To oil or gas condensate wells drilled in standard drilling units from which the well setbacks are defined by distance from a drilling unit boundary defined by a legal land description and does not apply to drilling units where well setbacks are established by other methods, or for wildcat wells or for wells in Exploratory Units established by the Commission; or
 - (3) To oil wells located in uncontrolled fields where the standard well setback as specified in General Rule B-3, apply to lease lines rather than drilling unit lines.
- b) In each such instance in which a permit is issued, except in uncontrolled fields which are not subject to an allowable, a reduction (penalty) in the allowable to which such well would otherwise be entitled, under the provisions of the applicable field rules or other general well spacing rules, shall be assessed by multiplying a fraction, the numerator of which shall be the distance expressed in feet between the location of such proposed well and the boundary of the drilling unit in which the well is to be drilled and the denominator of which shall be the distance expressed in feet at which wells within such field and/or drilling unit are otherwise required to be located. If the proposed location encroaches upon more than one boundary of said unit, then the penalty to be imposed upon the production allowable shall be cumulative of the penalties from both boundaries as described in sub section 1) below.
- 1) If the proposed location encroaches upon more than one boundary as specified in section (b) above, the reduction in the allowable shall be calculated as follows:

First boundary encroachment expressed as:

$$\frac{\text{setback footage specified by rule (minus)(-) actual footage of proposed well from unit boundary (divided by)(\div)}{\text{setback footage specified by rule, plus (+)}}$$

Second boundary encroachment expressed as:

$$\frac{\text{setback footage specified by rule (minus)(-)} \text{ actual footage of proposed well from unit boundary (divided by)(\div)}{\text{setback footage specified by rule}} = \text{penalty factor}$$

Then:

$$\text{penalty factor (x) full calculated allowable (MCF or bbl)} = \text{amount allowable reduced (MCF or bbl)}$$

Then:

$$\text{full calculated allowable (MCF or bbl) (minus)(-)} \text{ amount allowable reduced (MCF or bbl)} = \text{production allowable (MCF or bbl)}$$

- 2) Each such application for an exceptional location shall be submitted on a form prescribed by the Director of Production and Conservation, accompanied by an application fee of \$500.00 and include the name and address of each owner, as defined in A.C.A. § 15-72-102(9), within the drilling unit in which the proposed well is to be drilled and within the drilling units offsetting the boundary line or lines, or in the case of wells in uncontrolled fields within the boundaries of mineral lease lines and the offsetting lease(s), which shall be encroached upon by the proposed exceptional well location.
- 3) Concurrently with the filing of an application in accordance with this rule, the applicant shall send to each owner specified in sub-section 2) above a notice of the application filing and verify such mailing by affidavit, setting out the names and addresses of all owners and the date(s) of mailing.
- 4) Any owner noticed in accordance with sub-section 2) shall have the right to object to the granting of such application within fifteen (15) days after the receipt of the application by the Commission. Each objection must be made in writing and filed with the Director. If a timely written objection is filed as herein provided, then the applicant shall be promptly furnished a copy of such application and the objection shall be denied. If the application is denied under this subsection, the applicant may request to have the application placed, in accordance with General Rule A-2, A-3, and other applicable hearing procedures, on the docket of a regularly scheduled Commission hearing for a Commission determination, except that no additional application fee is required.
- 5) An application may be referred to the Commission for determination when the Director: (1) deems the penalty to be imposed upon the allowable for such well, calculated as herein provided, to be inadequate to offset any advantage which the applicant may have over any other producer, as defined in A.C.A. § 15-72-102(8), by reason of the drilling of the well at such exceptional location, or (2) deems it necessary that the Commission make such determination for the purpose of protecting correlative rights of all parties. Promptly upon such determination, and not later than fifteen (15) days after receipt of the application, the Director shall give the applicant written notice, citing the reason(s) for denial of the application under this rule and the referral to the full Commission for determination.

- 6) Applications for exceptional locations resulting from directional drilling shall be considered for administrative approval in accordance with this rule, provided, that no allowable shall be authorized until the Commission has been furnished a bottom hole directional survey for each common source of supply for which an allowable is requested. In all such cases where directional surveys are made available, the distance, of the mid-point perforations, for each common source of supply in a directional well, from the drilling unit boundary shall be used in calculating the allowable.
 - 7) If the Director has not notified the applicant of the determination to refer the application to the Commission within the fifteen (15) day period in accordance with the foregoing provisions, and if no objection is received at the office of the Commission within the fifteen (15) days as provided for in sub-section 4), the application shall be approved and a Drilling Permit issued.
- c) For dry gas wells, as specified in sub-section a) 1) above, an alternative to a reduction in the allowable (penalty) method, as outlines in Section b) above, may be requested if each affected drilling unit has been previously integrated, by Commission Order or is 100% leased, and is currently held by production, and if all the working interest owners in each affected drilling unit agree, in writing, to share the proceeds from a well which encroaches upon the drilling unit boundary. The below methodology for determining percentages for the sharing of costs, production and royalty among the affected drilling units, may be administratively authorized by the Director or his designee. The method for determining the percentages for sharing the costs of and the proceeds of production from one or more separately metered wells shall be as follows:
- 1) For vertical or directionally drilled wells, the acreage within an agreed upon area extending out from the perforated interval, as defined in General Rule B-3, shall be calculated for each such separately metered well (the "calculated area"). The calculated area shall be based upon the estimated drainage area of the perforated interval.
 - 2) Each calculated area shall be allocated and assigned to each drilling unit according to that portion of the calculated area occurring within each drilling unit.
 - 3) Each such application for utilizing the above methodology shall be submitted on a form prescribed by the Director of Production and Conservation, accompanied by an application fee of \$500.00 and include the name and address of each owner, as defined in A.C.A. § 15-72-102(9), within each of the drilling units in which the proposed well is to be drilled and/or completed and which contains a portion of the calculated area as defined in sub-section c) 1) above.
 - 4) Concurrently with the filing of an application utilizing the above methodology, the applicant shall send in written authorization from each owner specified in sub-section c) 3) above.
 - 5) An application may be referred to the Commission for determination when the Director deems it necessary that the Commission make such determination for the purpose of protecting correlative rights of all parties. Promptly upon such determination, and not later than fifteen (15) days after receipt of the application,

the Director shall give the applicant written notice, citing the reason(s) for denial of the application under this rule and the referral to the full Commission for determination.

- 6) If the Director has not notified the applicant of the determination to refer the application to the Commission within the fifteen (15) day period in accordance with the foregoing provisions, and if no objection is received at the office of the Commission within the fifteen (15) days as provided for in subsection (c)(5), the application shall be approved and a drilling permit issued.
- 7) Upon receipt of the drilling permit, the applicant shall give the other working interest parties written notice that the drilling permit has been issued. The working interest parties, who have not previously made an election, shall have fifteen (15) days after receipt of said notice within which to make an election to participate in the well or be deemed as electing non-consent and subject to the non-consent penalty set out in the existing Joint Operating Agreement(s) covering their respective drilling unit.
- 8) Following completion of the well and prior to the issuance by the Commission of the Certificate of Compliance to commence production, the final location of the perforated interval shall be submitted to the Commission to verify the proposed portion of the calculated area occurring within each drilling unit as specified in subsection (c)(1) above.