

**NM1 - 006**

**FINANCIAL  
ASSURANCE**

**2011**



# New Mexico Energy, Minerals and Natural Resources Department

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**Susana Martinez**  
Governor

**John H. Bemis**  
Cabinet Secretary-Designate

**Brett F. Woods, Ph.D.**  
Deputy Cabinet Secretary

**Jami Bailey**  
Division Director  
Oil Conservation Division



December 7, 2011

Mr. Frank W. Schageman  
Executive Vice President  
R360 Environmental Solutions, Inc.  
Greenspoint Plaza 4  
16945 Northchase Drive, Suite 2200  
Houston, TX 77060

**Re: Proposed conversion of Controlled Recovery, Inc. to a limited liability company**

Dear Mr. Schageman:

By letter dated November 11, 2011, you indicated that Controlled Recovery, Inc., holder of a commercial waste management facility permit from the Oil Conservation Division, plans to convert to a limited liability company and change its name. You inquired concerning the procedure that would be involved with the Division, and whether it would be a "minor modification" of Controlled Recovery's permit.

This letter will confirm the advice conveyed to your consultant, Bob Gallagher, by our Assistant General Counsel, David Brooks, in a recent telephone conversation. Under applicable statutes, a New Mexico corporation may be converted to a New Mexico limited liability company, and its name changed, without becoming a different legal entity. Hence, if you choose that procedure, there will be no need to transfer the permit since the new entity will be, in legal contemplation, the same as the old entity. Accordingly, the provision requiring the Division's consent to transfer of the permit would not be triggered.

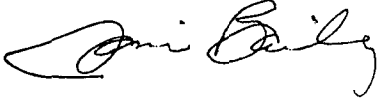
It will be necessary to change all applicable documentation, including Controlled Recovery's financial assurance on file with the Division, and any other permits, licenses or approvals that affect Controlled Recovery's operations, to reflect the new name. This would involve a minor modification of the permit. Please understand that this conclusion relates only to the name change and entity conversion as described in your letter. Any proposed changes in Controlled Recovery's facility must be handled separately.

Oil Conservation Division  
1220 South St. Francis Drive • Santa Fe, New Mexico 87505  
Phone (505) 476-3440 • Fax (505) 476-3462 • [www.emnrd.state.nm.us/OCD](http://www.emnrd.state.nm.us/OCD)



Please contact Mr. Brad Jones of the Division's Environmental Bureau at 505-476-3487 regarding to arrange all details.

Sincerely

A handwritten signature in dark ink, appearing to read "Jami Bailey". The signature is fluid and cursive, with the first name "Jami" and last name "Bailey" clearly distinguishable.

Jami Bailey  
Director

cc:

Mr. Bob Gallagher  
P.O. Box 45375  
Rio Rancho, NM 87174

Mr. Brad Jones  
OCD Santa Fe

Jami

As you requested, after reviewing New Mexico corporate statutes, I spoke with Mr. Gallagher concerning this matter.

He requested a signed letter from you; so I have drafted one (attached) for your approval.

David

A handwritten signature in black ink, consisting of a stylized 'D' followed by a flourish.



Greenspoint Plaza 4  
16945 Northchase Drive, Suite 2200  
Houston, Texas 77060  
**281.872.R360 (7360) Office**  
[www.r360environmentalsolutions.com](http://www.r360environmentalsolutions.com)

November 11, 2011

Jami Bailey, Director  
New Mexico Energy, Minerals, & Natural Resources Department –  
New Mexico Oil Conservation Division  
1220 South St. Francis Drive  
Santa Fe, NM 87505

Re: Controlled Recovery, Inc.

Dear Director Bailey:

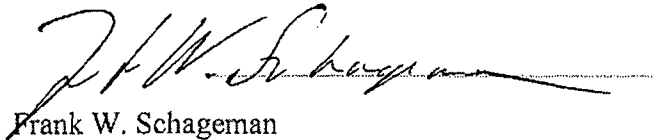
Controlled Recovery, Inc., a New Mexico corporation ("CRI"), owns and operates a surface waste disposal facility and an oil treating plant at a site in the S/2N/2 and the N/2S/2 of Section 27, Township 20 South, Range 32 East, NMPM, Lea County, New Mexico (the "Facility"). CRI operates the Facility pursuant to New Mexico Oil Conservation Division ("OCD") Order No. R-9166 and a January 23, 2004 Settlement Agreement by and between CRI and the New Mexico Oil Conservation Division of the Energy Minerals and Natural Resources Department both of which are attached (collectively the "Permits"). In keeping with Order No. R-9166 and OCD regulations, CRI has posted with the OCD an Irrevocable Letter of Credit issued by Wells Fargo Bank, N.A. dated March 22, 2007 in an aggregate amount not to exceed Fifty Six Thousand and No/100ths Dollars (\$56,000.00).

The sole shareholder of CRI, R360 Environmental Solutions, Inc., is contemplating a series of transactions that would convert CRI's form of entity from a New Mexico corporation to either a New Mexico or a Delaware limited liability company that would be named "R360 Permian Basin, LLC." The conversion would be processed in accordance with New Mexico's Limited Liability Company Act or Delaware's Limited Liability Company Act. In either case, CRI's sole shareholder, R360 Environmental Solutions, Inc., would become the general partner of the sole and managing member of R360 Permian Basin, LLC, and the current directors and officers of R360 Environmental Solutions, Inc. would manage R360 Permian Basin, LLC, in R360 Environmental Solutions, Inc.'s capacity as the general partner of the sole and managing member of R360 Permian Basin, LLC. As part of this process, CRI/R360 Permian Basin LLC would amend the Irrevocable Letter of Credit from Wells Fargo Bank to reflect the new entity name. The change in entity form and change of name would not in any manner involve an increase in the area the Facility occupies, a change in the design capacity or nature of the waste stream handled or treated at the Facility, or the addition of any new treatment process.

Paragraph 6 of Order No. R-9166 provides that “[a]uthority for operation of the treating plant and disposal facility shall be transferrable only upon written application and approval by the Division Director.” Because R360 Permian Basin would have the same owner and the same officers and directors as CRI, and because CRI would take all steps necessary to ensure that the Irrevocable Letter of Credit would remain in place, CRI believes that the proposed change in form of entity and accompanying name change would be a minor modification that would be processed administratively without need for a hearing. Before proceeding further with this proposal, we wanted to confirm with you that that understanding is correct and that, following the amendment, the Permits would remain in full force and effect and R360 Permian Basin, LLC could continue to operate the Facility under those Permits.

We would be happy to meet with you to discuss this further or to provide any additional information you may require. I look forward to hearing from you.

Sincerely,



Frank W. Schageman  
Executive Vice President &  
Chief Financial Officer  
R360 Environmental Solutions, Inc.

Office: (281) 873-3210  
[fschageman@r360es.com](mailto:fschageman@r360es.com)

**Attachments:**

1. Order No. R-9166
2. Settlement Agreement

**STATE OF NEW MEXICO  
ENERGY, MINERALS, AND NATURAL RESOURCES DEPARTMENT  
OIL CONSERVATION DIVISION**

**IN THE MATTER OF THE HEARING  
CALLED BY THE OIL CONSERVATION  
DIVISION FOR THE PURPOSE OF  
CONSIDERING:**

**CASE NO. 9882  
Order No. R-9166**

**APPLICATION OF CONTROLLED RECOVERY INC.  
FOR AN OIL TREATING PLANT PERMIT, SURFACE  
WASTE DISPOSAL AND AN EXCEPTION TO ORDER  
NO. R-3221, LEA COUNTY, NEW MEXICO.**

**ORDER OF THE DIVISION**

**BY THE DIVISION:**

This cause came on for hearing at 8:15 a.m. on April 4, 1990, at Santa Fe, New Mexico, before Examiner David R. Catanach.

NOW, on this 27th day of April, 1990, the Division Director, having considered the testimony, the record, and the recommendations of the Examiner, and being fully advised in the premises,

**FINDS THAT:**

(1) Due public notice having been given as required by law, the Division has jurisdiction of this cause and the subject matter thereof.

(2) Decretory Paragraph No. (3) of Division Order No. R-3221, as amended, prohibits in that area encompassed by Lea, Eddy, Chaves, and Roosevelt Counties, New Mexico, the disposal, subject to minor exceptions, of water produced in conjunction with the production of oil or gas, or both, on the surface of the ground, or in any pit, pond, lake, depression, draw, streambed, or arroyo, or in any water course, or in any other place or in any manner which would constitute a hazard to any fresh water supplies.

(3) The aforesaid Order No. R-3221 was issued in order to afford reasonable protection against contamination of fresh water supplies designated by the State Engineer through disposal of water produced in conjunction with the production of oil or gas, or both, in unlined surface pits.

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Order No. R-9166  
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(4) The State Engineer has designated all underground water in the State of New Mexico containing 10,000 parts per million or less of dissolved solids as fresh water supplies to be afforded reasonable protection against contamination; except that said designation does not include any water for which there is no present or reasonably foreseeable beneficial use that would be impaired by contamination.

(5) The applicant, Controlled Recovery Inc., seeks authority to construct and operate a surface waste disposal facility and an oil treating plant for the purpose of treating and reclaiming sediment oil and for the collection, disposal, evaporation, or storage of produced water, drilling fluids, drill cuttings, completion fluids and other non-hazardous oilfield related waste in unlined surface pits at a site in the S/2 N/2 and the N/2 S/2 of Section 27, Township 20 South, Range 32 East, NMPM, Lea County, New Mexico.

(6) The applicant proposes to install and operate an effective system, consisting of separating tanks, a water disposal pit, a solids disposal pit, and associated skimming, heat, and/or chemical separating equipment for the removal and reclamation of oil and basic sediments from the produced water to be disposed of, and a settling area to separate other solid waste.

(7) The proposed plant and method of processing will efficiently process, treat, and reclaim the aforementioned waste oil, thereby salvaging oil which would otherwise be unrecoverable.

(8) No interested party appeared at the hearing in opposition to the application.

(9) A naturally occurring salt lake (Laguna Toston) is located in the S/2 of Section 21 and the N/2 of Section 28, Township 20 South, Range 32 East, NMPM, Lea County, New Mexico, and is approximately three-quarters of a mile from the proposed disposal area.

(10) The hydrogeologic evidence presented in this case establishes that:

- a) Triassic redbeds, comprised of the Chinle Shale, Santa Rosa sandstone, and the Dewey Lake formation, underlies both Laguna Toston and the proposed water disposal site;



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- b) Shales within the Triassic redbeds underlying the proposed waste disposal site and Laguna Toston are virtually impermeable and therefore prevent vertical seepage of the waters from the site and Laguna Toston into sand stringers within the redbeds which may contain fresh water;**
- c) The surface of the Triassic redbeds is depressed in the vicinity of the waste disposal site and Laguna Toston thus creating a "collapse feature";**
- d) The major flow of surface and subsurface water within the boundaries of the "collapse feature" is toward Laguna Toston;**
- e) Seepage from the impoundments at the proposed waste disposal site will infiltrate into the subsurface and migrate toward Laguna Toston;**
- f) After the seepage reaches Laguna Toston, practically all of the seepage will evaporate;**
- g) There is no present or reasonably foreseeable beneficial use of the waters of Laguna Toston;**
- h) There are no known sources of potable groundwater in sediments underlying the Triassic redbeds at Laguna Toston;**
- i) The utilization of the proposed disposal site adjacent to Laguna Toston for the disposal of water produced in conjunction with the production of oil or gas, or both, and other non-hazardous oilfield waste products, including drill cuttings and drilling muds should not constitute a hazard to any fresh water supplies.**

**(11) The applicant should be authorized to utilize the unlined pits described in Finding Paragraph Nos. (5) and (6) above, for the disposal of water produced in conjunction with the production of oil or gas, or both, and other non-hazardous oilfield waste products, including drill cuttings and drilling muds.**

**(12) The maximum fill level in both of the above-described pits should be limited to a plane below the crest of the dikes surrounding the pits in order to preclude over-tapping of the dikes.**

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**(13) The proposed oil treating plant and disposal facility should be constructed in accordance with the engineering plat and topographic map presented as evidence in this case and in accordance with such additional conditions and requirements as may be directed by the Division Director, and should be operated and maintained in such a manner as to preclude spills and fires, and protect persons and livestock.**

**(14) Prior to initiating operations, the facility should be inspected by a representative of the Hobbs district office of the Division in order to determine the adequacy of fences, gates and cattleguards necessary to preclude livestock and unauthorized persons from entering and/or utilizing said facility, and also to determine the adequacy of dikes and berms needed to assure safe plant operation.**

**(15) The Director of the Division should be authorized to administratively grant approval for the expansion or modification of the proposed treating plant.**

**(16) Authority for operation of the treating plant and disposal facility should be suspended or rescinded whenever such suspension or rescission should appear necessary to protect human health or property, to protect fresh water supplies from contamination, to prevent waste, or for non-compliance with the terms and conditions of this order or Division Rules and Regulations.**

**(17) Prior to constructing said facility, the applicant should be required to submit to the Santa Fe office of the Division a surety or cash bond in the amount of \$25,000 in a form approved by the Division.**

**(18) Authority for operation of the treating plant and disposal facility should be transferrable only upon written application and approval by the Division Director.**

**(19) The granting of this application should not endanger designated fresh water supplies, and will prevent waste by allowing the recovery of otherwise unrecoverable oil.**

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**IT IS THEREFORE ORDERED THAT:**

(1) The applicant, Controlled Recovery Inc., is hereby authorized to construct and operate a surface waste disposal facility complete with unlined surface pits and an oil treating plant at a site in the S/2 N/2 and the N/2 S/2 of Section 27, Township 20 South, Range 32 East, NMPM, Lea County, New Mexico, for the purpose of treating and reclaiming sediment oil and for the collection, disposal, evaporation, or storage of produced water, drilling fluids, drill cuttings, completion fluids and other non-hazardous oilfield related waste.

**PROVIDED HOWEVER THAT,** the proposed oil treating plant and disposal facility shall be constructed in accordance with the engineering plat and topographic map presented as evidence in this case and in accordance with such additional conditions and requirements as may be directed by the Division Director, and shall be operated and maintained in such a manner as to preclude spills and fires, and protect persons and livestock.

**PROVIDED FURTHER THAT,** prior to initiating operations, the facility shall be inspected by a representative of the Hobbs district office of the Division in order to determine the adequacy of fences, gates and cattleguards necessary to preclude livestock and unauthorized persons from entering and/or utilizing said facility, and also to determine the adequacy of dikes and berms needed to assure safe plant operation.

(2) The maximum fill level in both of the proposed unlined surface pits shall be limited to a plane below the crest of the dikes surrounding the pits in order to preclude over-tapping of the dikes.

(3) The Director of the Division shall be authorized to administratively grant approval for the expansion or modification of the proposed treating plant.

(4) Authority for operation of the treating plant and disposal facility shall be suspended or rescinded whenever such suspension or rescission should appear necessary to protect human health or property, to protect fresh water supplies from contamination, to prevent waste, or for non-compliance with the terms and conditions of this order or Division Rules and Regulations.

(5) Prior to constructing said facility, the applicant shall submit, to the Santa Fe office of the Division, a surety or cash bond in the amount of \$25,000 in a form approved by the Division.

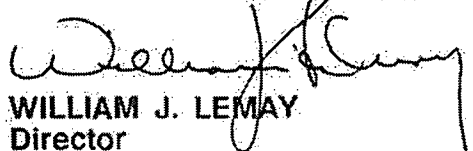
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(6) Authority for operation of the treating plant and disposal facility shall be transferrable only upon written application and approval by the Division Director.

(7) Jurisdiction of this cause is retained for the entry of such further orders as the Division may deem necessary.

DONE at Santa Fe, New Mexico, on the day and year hereinabove designated.

STATE OF NEW MEXICO  
OIL CONSERVATION DIVISION

  
WILLIAM J. LEMAY  
Director

S E A L

RECEIVED

SETTLEMENT AGREEMENT

This Settlement Agreement is entered into as of the 23rd day of February, 2004, by and between Controlled Recovery, Inc. ("CRI") and the New Mexico Oil Conservation Division of the Energy Minerals and Natural Resources Department ("Division").

WHEREAS, CRI operates a commercial surface waste management facility in Lea County, New Mexico, under the authority of Division Order R-9166;

WHEREAS, by letters dated July 3, 2000; September 27, 2000; and July 6, 2001, the Division sought to "re-permit" CRI's facility, impose new operational conditions, and revoke certain netting exemptions CRI has operated under since 1991;

WHEREAS, on August 17, 2001, CRI filed a Complaint for Declaratory and Injunctive Relief in the Fifth Judicial District Court of the State of New Mexico, Lea County, against the Division, its director and its district supervisor seeking declaratory and injunctive relief in a case styled *Controlled Recovery Inc., v. Chris Williams et al.*, Cause No. CV 2001-310G ("CRI's Complaint");

WHEREAS, without admission of liability or fault, the parties desire to resolve the issues raised by the Division's letters and CRI's Complaint without the necessity of further litigation and the costs associated with such litigation.

NOW, THEREFORE, in consideration of the mutual covenants and agreements of the parties and other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, and for the purpose of fully and completely resolving the claims asserted in CRI's Complaint and all other claims, known or unknown, arising out of or concerning the operation of CRI's facility in Lea County, the parties agree as follows:

- A. Withdrawal of Prior Letters and Recognition of No Violations. The letters issued by the Division to CRI Dated July 3, 2000; September 27, 2000; and July 6, 2001 are hereby withdrawn and shall have no force or effect. The Division acknowledges that to the best of its knowledge, pending formal inspection, CRI's facility is in full compliance with all applicable rules and orders of the Division.
- B. Netting Exemptions Remain. The netting exemptions issued by the Division for CRI's facility in July of 1991 under Permit No. H-76 and by letter dated April 7, 1997, remain in full force and affect.
- C. Closure Plan, Bonding, and Closure of Pit Nos. 13 and 16. The Division accepts and approves the closure plan submitted by CRI on September 1, 2000. CRI shall immediately increase its closure bond with the Division to the total amount of \$53,000 plus tax. In addition, CRI shall close within six months storage pits Nos. 13 and 16 pursuant to CRI's closure plan. In the event that these storage pits are not closed within 6 months of the execution of this Settlement Agreement,

then CRI shall further increase its closure bond to a total amount of \$73, 000 plus tax.

- D. Operational Conditions.** In addition to the operational conditions imposed on CRI's facility by Order R-9166 and Division Rule 711.C and 711.D as presently codified and enacted, CRI agrees to abide by the following additional operational conditions:

**Overall Facility Operation**

1. The facility must be fenced and have a sign at each entrance. The sign must be legible from at least 50 feet and contain the following information: a) name of the facility; b) location by section, township and range; c) emergency phone number; and d) OCD order number.
2. The facility will be maintained, contoured, and bermed to prevent runoff and runoff of the portion of the facility containing contaminated solids and liquids.
3. All above ground tanks and fuel tanks will be bermed, the current berm height will be maintained, and the tanks will be labeled as to the contents with standard hazard labels.
4. Sumps and below grade tanks without leak detection systems shall have their integrity tested annually. Sumps and below grade tanks that can be removed from their emplacements may be tested by visual inspection. Other sumps and below grade tanks shall be tested by appropriate mechanical means.
5. Sumps and below grade tanks will be inspected weekly and fluid will be removed as necessary to prevent overflow. If any defects are noted, repairs must be made as soon as possible.
6. All saddle tanks and drums containing materials other than fresh water must be labeled as to contents with standard hazard labels.
7. A checklist of all inspections at CRI's facility will be kept and maintained for Division review.
8. The OCD shall be notified prior to the installation of any pipes or wells or other construction within the boundaries of the facility that are not associated with the operation of the facility.
9. Any major design changes to CRI's facility must be submitted to the Division's Santa Fe Office for approval.

#### Pond and Pit Operation

10. All produced water must be unloaded into tanks. The produced water must reside in the tank and skim pit system long enough to allow for oil separation. Oil recovered must be stored in above-ground storage tanks.
11. All pits and ponds that contain liquids must have sufficient freeboard to prevent overtopping and a minimum freeboard of (1) one foot.
12. Free oil within the ponds and pits must be removed as soon as possible.
13. Ponds and pits will be inspected on a weekly basis and, if any defect is noted, repairs must be made as soon as possible.
14. A sign or other such marker with the pit/pond number must be clearly posted at each pit/pond location.

#### H2S Prevention & Contingency Plan

15. CRI personnel will wear H2S personnel monitors under circumstances in which H2S may be present, including the unloading of materials that may contain H2S. The monitors shall issue a visual and audible signal at 10 ppm of H2S in the ambient air that becomes more rapid at 20 ppm. An inspection for the presence of H2S shall be conducted weekly and reported on the inspection checklist.
16. In the event that a reading of 10 ppm is registered at CRI's facility, CRI personnel will evacuate the area and CRI will monitor H2S levels along the downwind boundary of the facility. If H2S levels reach 20 ppm, the facility will be closed and notification will be given to the following:  
  
New Mexico State Police  
Lea County Sheriff  
The Division's Hobbs District office
17. CRI will notify Calaway Safety in Hobbs to provide personnel, equipment, and supplies to mitigate the source of an H2S reading of 10 ppm or greater.
18. CRI will log and report to the Division all incidences where a reading of 10 ppm H2S or greater is registered at CRI's facility.

#### Treating Plant Operations

19. The treating plant will be inspected weekly and if any defect is noted repairs will be made as soon as possible. If the defect will jeopardize the integrity of the plant, the plant will be shut down until repairs have been completed.
20. The treating plant may use diesel and gasoline from storage tanks that are to be pulled, repaired, or replaced. This material may only be used in the treating plant as a product to aid in the chemical treatment and blending of crude oil.
21. CRI shall submit to the Division a functional diagram or engineering schematic that depicts the functioning of the treating plant as a whole, and each major element thereof.

#### Solid Waste Disposal

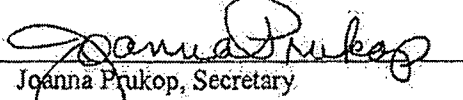
22. CRI shall submit to the Division a general plan of operations for solid waste disposal areas 50 and 51 that will provide a written description of the ongoing excavation and closure operations. CRI will also submit an updated plat showing all current disposal cells and past burial operations.
  23. Mechanical stabilization of liquids may be used prior to disposal.
  24. Free liquids will not be disposed of in the solid waste disposal pits.
  25. The solid waste disposal area will be inspected on a weekly basis and, if any defect is noted, repairs must be made as soon as possible.
  26. The solid waste disposal area will be bermed to prevent runoff and runoff of rain and storm water.
  27. All trash accepted at the facility that has the potential for blowing away or being transported by other vectors must be covered with soil within 24 hours of disposal into the solid waste pit.
  28. The Division will be notified before any new cells or expansion of existing cells in the solid waste disposal area are constructed.
- E. Dismissal of Complaint. Upon the execution of this agreement, CRI's Complaint shall be dismissed, with each party bearing their own attorneys' fees, costs, expenses, and disbursements. The parties will cooperate to promptly file all documents necessary to accomplish such dismissal.



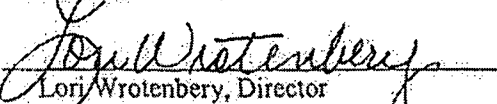
- F. **No admission.** This Agreement represents the settlement of disputed claims, and does not constitute an admission of the correctness of any position asserted by any party, or an admission of liability of any wrongdoing by any party.
- G. **Construction.** This Agreement shall be construed based upon its terms and stated intent, including the recitals, and shall not be construed in the favor of one or another party based upon who may have contributed to its drafting, or on any other basis.
- H. **Counterparts.** This Agreement may be executed in counterparts, each of which is hereby deemed an original, but all of which together shall constitute one and the same instrument.
- I. **Entire Agreement.** This Agreement constitutes the entire agreement between the parties, and any modification of or addition to this agreement must be in writing and signed by all parties hereto.
- J. **Authority.** The signatories to this agreement represent and warrant that they have full power and authority to enter into this Agreement on behalf of the parties indicated.
- K. **Advice of Counsel.** The parties acknowledge that they have been and are fully advised by competent legal counsel of their own choice, that they have read this entire agreement and fully understand its terms and conditions of this Agreement, and that their execution of this Agreement is with the advice of counsel and of their own free will and desire.
- L. **Binding on Successors.** This agreement shall bind and benefit the successors and assigns of CRI's facility, provided this provision should not authorize transfer of CRI's facility or permit without permission of OCD in accordance with Order No. R-9166 and Rule 711.

IN WITNESS WHEREOF, the parties have executed this Agreement by their duly authorized representatives, whose signatures appear below.

NEW MEXICO ENERGY MINERALS AND  
NATURAL RESOURCES DEPARTMENT

By:   
Joanna Prukop, Secretary

NEW MEXICO OIL CONSERVATION DIVISION

By:   
Lori Wrotenbery, Director

NEW MEXICO OIL CONSERVATION DIVISION

By: Chris Williams  
Chris Williams, District 1 Supervisor

APPROVED

By: David K. Brooks  
David K. Brooks,  
Special Assistant Attorney General

CONTROLLED RECOVERY INC.

By: Ken Marsh  
Ken Marsh, President



Bob Gallagher

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