



May 22, 1998

VIA TELECOPY (505) 748-4572

Mr. Robert Bullock
Yates Petroleum Corporation
105 South Fourth Street
Artesia, New Mexico 88210

RE: Competing Compulsory Pooling Applications
Lots 9-16 and the South One-half of Section 2, T16S, R35E, NMPM
Lea County, New Mexico

Dear Robert:

In reference to the captioned Applications, Ocean Energy, Inc. ("OEI") hereby offers to Yates Petroleum Corporation ("Yates") the following settlement proposal. This proposal is based upon the verbal proposal submitted by Yates to OEI on January 16, 1998 subject to certain revisions.

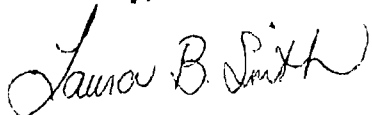
- 1) OEI shall withdraw its Townsend State Com. #2 Well proposal and shall support Yates' Field APK State Com. #3 Well proposal subject to a laydown 320 acre unit consisting of Lots 9-16 of Section 2 for all pools or formations spaced on 320 acres and an 80 acre unit consisting of Lots 13 and 14 for all pools or formations spaced on 80 acres.
- 2) Yates shall withdraw its Application for Compulsory Pooling covering Lots 11-14 and the SW/4 of Section 2.
- 3) Yates shall be named the Applicant and Operator under OEI's Application for Compulsory Pooling and an Unorthodox Well Location covering Lots 9-16 of Section 2. The Unorthodox Well Location shall be amended to include Yates' Field APK State Com. #3 Well (the "Field #3") to be drilled at a location 760' FWL and 3300' FSL of Section 2, T16S, R35E, NMPM, Lea County, New Mexico.
- 4) Yates shall also be named Applicant and Operator under OEI's Application for Compulsory Pooling covering the South one-half of Section 2 for the Townsend State Com. #6 Well (the "Townsend #6").
- 5) In the event the Hearing for the Field #3 Unorthodox Well Location results in a production penalty no greater than twenty-five percent (25%), or in the alternative, a minimum allowable of 2 MMCFGPD or greater, Yates shall commence drilling operations on the Field #3 and the Townsend #6 as set forth below.

- 6) In the event the production penalty is greater or the minimum allowable is less than stated above, Yates shall amend the Field #3 Unorthodox Well Location to include a location 1400' FWL and 3250' FSL of Section 2. Yates shall commence drilling operations on the Field #3 and the Townsend #6 as set forth below.
- 7) As an additional concession, in order that Yates may own a consistent interest in all potential zones in the Townsend #6, OEI agrees to assign to Yates an undivided 12.5% Working Interest and 10.9375% Net Revenue Interest in the Strawn Carbonate formation in the E/2SW/4 of Section 2. An 80 acre unit consisting of the E/2SW/4 of Section 2 shall be established for all pools or formations spaced on 80 acres. Yates agrees to assign to OEI an undivided 25% Working Interest and 21.875% Net Revenue Interest in the Strawn Carbonate formation in Lot 13 of Section 2. The stratigraphic equivalent of the Strawn Carbonate formation is found at 11,506' in the Yates Shell Lusk ANB Com. #1 Well located 1980' FNL and 1980' FWL of Section 11, T16S, R35E, NMPM, Lea County, New Mexico.
- 8) Even though OEI owns 75% Working Interest in the Atoka formation and 87.5% Working Interest (or 100% should Yates not desire to acquire the 12.5% offered by OEI) in the Strawn Carbonate formation, in order to alleviate Yates concerns over OEI's operations, Yates shall be named Operator of the Townsend #6 subject to the following conditions:
 - a) Yates shall be named Operator through the drilling of the Townsend #6 to its total depth.
 - b) Yates' drilling prognosis and vendor lists shall be subject to OEI's approval.
 - c) OEI shall have the right to determine all testing, coring and logging to be conducted in the Townsend #6.
 - d) At casing point, OEI shall assume operatorship of the Townsend #6 and the Contract Area.
- 9) Within 30 days from receipt of all regulatory approval necessary to commence operations of the Townsend #6, Yates shall commence actual drilling operations of the Townsend #6. Yates shall diligently proceed in obtaining all such regulatory approvals. The Townsend #6 shall be drilled at a location of 930' FSL and 1650' FWL of Section 2 and under OEI's well proposal dated March 26, 1998 pursuant to the terms of a mutually acceptable Operating Agreement.
- 10) Notwithstanding the foregoing, if for any reason, Yates fails to commence actual drilling operations on the Townsend #6 by August 15, 1998, OEI shall become Operator of the Townsend #6 and the Contract Area and Yates shall immediately execute all documents necessary to effectuate OEI's assumption of operations.
- 11) Notwithstanding anything contained in the Operating Agreement or Compulsory Pooling Order, OEI shall be given a 30 day deferred election from the release of the drilling rig of the Townsend #6 to make an election to participate in the Field #3. OEI's election shall be made under the terms of an Operating Agreement identical in form to the Operating Agreement for

the Townsend #6. In the event OEI elects to participate in the Field #3, Yates shall commence actual drilling operations of the Field #3 within 45 days following the release of the drilling rig of the Townsend #6. The Field #3 shall be drilled under Yates's well proposal dated December 1, 1997. In the event Yates timely commences drilling operations, Yates shall operate the Field #3 in its entirety. If Yates fails to timely commence drilling operations, OEI shall become Operator of the Field #3 and the Contract Area and Yates shall immediately execute all documents necessary to effectuate OEI's assumption of operations.

OEI believes this settlement offer is beneficial to both parties. This proposal should alleviate Yates' concerns about OEI's operations. This proposal also gives Yates the right to participate in a Strawn Carbonate completion in the Townsend #6 or OEI's permitted Townsend State #3 Well. OEI respectfully requests that Yates give this proposal its full consideration. Should the foregoing meet with your approval, please so indicate by executing in the space provided below and returning one copy to my attention at fax no. (303) 573-0813 no later than the close of business on May 26, 1998 at which time this offer shall automatically terminate.

Sincerely,



Laura B. Smith
Senior Landman

AGREED TO AND ACCEPTED THIS _____ DAY OF MAY, 1998.

YATES PETROLEUM CORPORATION

By: _____
Title: _____

cc: Mr. Michael Stogner
Mr. Jim Bruce

