

Robert E. Landreth
OIL AND GAS EXPLORATION

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August 28, 1998

Santa Fe Energy Resources, Inc.
550 W. Texas, Suite 1330
Midland, Texas 79701

ATTN: Mr. Steve Smith

RE: Proposed 13,700' Morrow Test
Rio Blanco "4" Fed COM #1 Well
1980' FNL & 1980' FWL
Section 4, T-23-S, R-34-E
Lea County, New Mexico
RIO BLANCO PROSPCT-NM0964

Dear Mr. Smith:

Reference your letter this date, captioned subject, received by us by fax this morning.

As I am sure you are aware, my past negotiations with Santa Fe in this area have, on several occasions, been less than favorable or amicable. I know that you are new to this situation, but I understand from talking to other industry people here in Midland that you are honest and straightforward. With that in mind, perhaps we could get a few things behind us and then see if we can work out a mutually agreeable trade.

You indicated that you have read correspondence in files dealing with our mutual negotiations in this area. You are probably aware that after considerable negotiation, I joined for a working interest in the Gaucho Unit Well #2-Y and was force pooled, against my wishes, for the remainder of my working interest, having preferred to work out a farmout deal with Santa Fe on that portion. Consequently, I have to tell you that it is like putting salt in old wounds when Santa Fe calls to say that, on the proposed Rio Blanco well, Santa Fe is not in a position to offer me the opportunity to participate for a portion of my interest and farmout the balance. That is obviously an option that anyone in the oil business has, or should have, the force pooling statutes of New Mexico notwithstanding. I can perfect that right simply by assigning the fraction for which I choose not to participate to someone else, who can either join or be force pooled as to that fraction. I take exception to Santa Fe again attempting to use this as a negotiating tool.

BEFORE THE
OIL CONSERVATION DIVISION
Case No. 12043 Exhibit No. 7
Submitted By:
Santa Fe Energy Resources
Hearing Date: September 17, 1998

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Secondly, I resent the continuing implication by Santa Fe that it has done me a favor by drilling the Gaucho #2-Y in time to protect my Federal lease which otherwise was about to expire. Certainly I appreciate Santa Fe's efforts, as I would any other Operator (including myself) who works to put trades together that wind up benefiting others as well as himself, and I believe that I can honestly state as an Operator that I have done the same on several occasions. But the other side of the coin here is that, without exceptional perseverance on our part to protect the remaining leasehold position which we have in this area, Santa Fe would have simply waited us out and wound up with all of it. Our efforts to interest Santa Fe in such things as jointly drilling a shallow well to obtain a two-year extension of my now-expired Federal lease covering W/2 Section 33, T-22-S, R-34-E, or to partner with us in acquiring new leases on tracts which we held, have always been rebuffed. Consequently, we have gone to the Federal auction and bid against Santa Fe, on tracts such as the NE/4 of Section 29 in the Gaucho Unit, at prices up to \$1,300 per acre in an effort to preserve our position.

Your August 28 letter with regard to the Rio Blanco #1 states that the farmout terms which I have proposed are, in Santa Fe's opinion, excessive, given the risk involved. Maybe so. However, I do not consider them to be any more excessive than the terms which Santa Fe saddled us with in 1994 when we were attempting to put together a unit for the drilling of a Morrow well covering these same lands. Santa Fe refused to join or farmout to the proposed unit, and opted instead to grant a farmout of a Federal lease obtained from Amoco and subject to an 81.8% NRI, delivering 75% NRI with the option to convert the retained override to a 33-1/3% working interest at payout. So far as I can see, the risk of drilling this well today is not any different than it was four years ago. Also, the overriding royalty contractually owed to Scott Tanberg is his alone and cannot be converted to working interest. Even with his 1% of 8/8 override, my average NRI across the proposed N/2 spacing unit is still 81.75% of working interest.

Putting all this behind us, here is my bottom line position with respect to Section 4:

1. I will join for 1/8 working interest in the proposed well.
2. I will farmout my remaining 3/8 working interest in the N/2, delivering 75% NRI with the option to convert 6.75% ORRI to a proportionate 25% working interest at payout.
3. We are not willing to commit to farmout terms in the S/2 of Section 4 at this time. If in the future we should elect to farmout all or a portion of our interest

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therein, we will initially offer it pro rata to the parties who participate in the Rio Blanco #1.

4. We would like to review any geophysical data which Santa Fe has which influences the drilling of this well.

Since Santa Fe has filed for a force pooling hearing for this well, we would like to hear from Santa Fe in this regard by Wednesday, September 2, 1998.

Sincerely,



Robert E. Landreth

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FACSIMILE COVER SHEET

TO: Steve Smith
Santa Fe Energy

DATE: 8/31/98

FAX NO: 686-677

FROM: Bob Landreth

RE: Re: Borehole "4" Fed Cont



Number of pages including this cover page: 4

If all pages are not received please call at : 915/684-4781

COMMENTS: _____

