

May 24, 2000

Ms. Lori Wrotenbery
New Mexico Oil Conservation Division
2040 South Pacheco
Santa Fe, New Mexico 87505

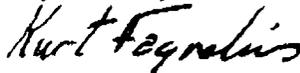
Dear Ms. Lori Wrotenbery:

I enjoyed meeting and talking with you here in Farmington at the Oil and Gas conference a few weeks ago.

We discussed the NMOCD's denial of Dugan's application for unorthodox location for the Carpenter Com #90. As a result of our conversation, I am putting together an application for two unorthodox proration units.

Attached you will find a rough draft of my application. In the application our conversation is referenced to the best of my recollection. Could you please review my letter for accuracy and content? If your impression of our meeting was different from mine, please let me know and I will make the appropriate changes to my application letter.

Very Sincerely,



Kurt H. Fagrelis

ROUGH DRAFT

Re: Application for Administrative Approval of Unorthodox Proration Units
SE/4 Sec. 26 and SW/4 (Lots 4, 5, N/2SW/4) Sec. 25, T30N, R14W (± 320.36 acres)
NE/4 Sec. 26 and NW/4 Sec. 25, T30N, R14W (± 320 acres)
San Juan County, New Mexico
Basin Fruitland Coal Pool

Dear Ms. Wrotenbery:

Recently, Dugan Production Corp. submitted an application to the New Mexico Oil Conservation Division for administrative approval of an unorthodox location for the Carpenter Com # 90 well. The unorthodox location is necessitated by extreme topographic conditions and would insure the conservation of surface and subsurface resources in the area (Exhibit 1 and Exhibit 2). The application was rejected based on the Oil Conservation Division's concern that offsetting, correlative rights would not be protected if it were approved.

2/3

During a discussion with you and Frank Chavez at the Four Corners Oil and Gas Conference on May 9, 2000, a solution to Dugan's location problem with the Carpenter Com #90 was proposed. You recommended and encouraged Dugan to make application for two unorthodox proration units. These proration units would protect correlative rights and insure full, orderly development of the Fruitland Coal in the subject area. Dugan would be able to locate and operate a Fruitland Coal well at an orthodox location in an area of very rough topographic terrain, and the impact on surface resources and risk to producing gas wells would be minimized.

As allowed by Rule 6 (paragraphs d and e) of the Special Rules and Regulations for the Basin Fruitland Coal Gas Pool (Order R-8768-A), Dugan Production Corp. hereby requests administrative approval for the following two unorthodox proration units:

1. SE/4 of Sec. 26 and SW/4 Sec. 25, T30N, R14W (\pm 320.36 acres)
2. NE/4 of Sec. 26 and NW/4 Sec. 25, T30N, R14W (\pm 320 acres)

Attached for your reference are the following exhibits:

1. Letter to Ms. Lori Wrotenbery asking the NMOCD to review their ruling on Dugan's unorthodox location application for the Carpenter Com #90 well.
2. Topographic map.
3. Offsetting operator map.
4. Letter to Mr. Jim Lovato asking the BLM to support this application and describing Dugan's development plans for the subject area if the unorthodox proration units are approved.
5. BLM letter supporting application.

Copies of this application and the request for administrative approval have been sent by certified mail to all offsetting Fruitland Coal operators and the BLM.

From our previous discussion and the rules cited above, it is our understanding that the Division Director may approve our application administratively if no affected, offsetting party objects to the formation of these unorthodox proration units within 30 days after the Division Director receives this application.

Please contact me if you have any questions or need additional information.

Very Sincerely,

Kurt H. Fagrelus
Geologist

*will be
taken
under
advisement
?*

*- all mineral
interest owners
in the
excluded
area?*

3/3