

Attached to and made a part of Unit Accounting
Agreement (Southern Union Production Company,
Operator) dated November 28, 1947.

ACCOUNTING PROCEDURE (UNIT AND JOINT LEASE SCHEDULE)

The term "joint property" as herein used shall be construed to mean the subject area covered by the agreement to which this "Accounting Procedure" is attached, **and physical facilities appurtenant to such area.**

The term "Operator" as herein used shall be construed to mean the party designated to conduct the development and operation of the leased premises for the joint account.

The term "Non-operator" as herein used shall be construed to mean any one or more of the non-operating parties.

Operator shall bill Non-operator on or before the last day of each month for its proportionate share of costs and expenditures during the preceding calendar month. Itemized statements shall accompany such bills. Each party shall pay its proportion of all such bills within fifteen (15) days after the receipt thereof. If payment is not made within such time, the unpaid balance shall bear interest at the rate of ~~five percent~~ **7%** per annum until paid. Payment of any such bill shall not prejudice the right of any party to protest or question the correctness thereof.

I. DEVELOPMENT AND OPERATING CHARGES

Subject to limitations hereinafter prescribed, Operator shall charge the joint account with the following items:

- (1) Delay or other rentals, when such rentals are paid by Operator for the joint account; royalties, when not paid direct to royalty owners by the purchaser of the oil, gas, casinghead gas or other products.
- (2) Labor, teaming and other services necessary for the development, maintenance and operation of the joint property.
- (3) Materials, equipment and supplies purchased and/or furnished by Operator from its warehouse stocks or from its other leases for use on the joint property. In so far as is practical and consistent with efficient and economical operation, only such materials shall be purchased for or transferred to the joint property as are required for immediate use, and the accumulation of warehouse and/or lease stock on the joint property shall be avoided.
- (4) Moving materials to the joint property from vendor's or from Operator's warehouse in the district or from other properties of Operator, but in either of the last events no charge shall be made to the joint account for a distance greater than the distance from the nearest reliable supply store or railway receiving point.
- (5) Moving surplus materials from the joint property to outside vendees, if sold f. o. b. destination, or minor returns to Operator's warehouse or other storage point. No charge shall be made to the joint account for moving major surplus materials to Operator's warehouse or other storage point for a distance greater than the distance to the nearest reliable supply store or railway receiving point, except by special agreement with Non-operator; and no charge shall be made to the joint account for moving materials to other properties belonging to Operator, except by special agreement with Non-operator.
- (6) Use of and service by Operator's exclusively owned equipment and utilities as provided in Paragraph (6) of Section II: "Basis of Charges to Joint Account."
- (7) Damages or losses incurred by fire, flood, storm or from any other cause not controllable by Operator through the exercise of reasonable diligence. Operator shall furnish Non-operator written notice of damages or losses incurred by fire, storm, flood or other natural or accidental causes as soon as practicable after report of the same has been received by Operator.
- (8) Expenses of litigation, liens, judgments and liquidated claims involving the joint property or incident to its development and operation. Actual expenses incurred by Operator or Non-operator in securing evidence pertaining to the joint property shall be a proper charge against the joint account.
 - (a) When any case, by prior agreement, is handled by Operator's and/or Non-operator's legal staff, thereby eliminating the retaining of outside counsel, a charge commensurate with the cost of services rendered may be made to the joint account. Charges of this nature shall not be rendered until the respective legal departments have agreed upon the proper amount.
 - (b) Fees and expenses of outside attorneys shall not be charged to the joint account except where the employment of such outside attorneys is authorized by a vote of the majority interests.
- (9) All taxes paid for the benefit of the parties hereto including ad valorem, property, gross production, occupation and any other taxes assessed against the ~~properties~~ properties, the production therefrom or the operations thereon.
- (10) Insurance:
 - (a) Premiums paid for insurance carried for the benefit of the joint account together with all expenditures incurred and paid in settlement of any and all losses, claims, damages, judgments and other expenses, including legal services, not recovered from insurance carrier.
 - (b) If no insurance is required to be carried, all actual expenditures incurred and paid by Operator in settlement of any and all losses, claims, damages, judgments and any other expenses, including legal services, shall be charged to the joint account.
- (11) District and Camp Expense:
 - (a) District Expense: A proportionate share of the salaries and expenses of Operator's district superintendent and other general district employes serving the joint property whose time is not allocated directly to the joint property, and a proportionate share of the expense of maintaining and operating a district office in conducting the management of operations on the joint property and other properties in the same locality owned and operated by Operator, such charges to be apportioned to such properties served on the following basis: **on a well basis, each drilling well equivalent to 4 producing wells.**
 - (b) Camp Expense: The expense of providing and maintaining on or in the vicinity of the joint property all necessary camps, housing facilities for employes and boarding employes, if necessary. When properties other than the joint property are served by these facilities, then an equitable distribution of expense, including depreciation, or a fair monthly rental in lieu of the investment, maintenance and operating cost of buildings and other camp facilities, shall be prorated against all properties so served on the following basis: **on a well basis, each drilling well equivalent to 4 producing wells.**
- (12) Overhead charges, which shall be in lieu of any charges for any part of the compensation or salaries paid to managing officers and employes of Operator, including the division superintendent, the entire staff and expenses of the division office located at Santa Fe, New Mexico, any portion of the office expense of the principal business office located at Dallas, Texas but not in lieu of field office expenses incurred in operating any such properties, and such overhead charges do not include any other expenses of Operator incurred in the development and operation of said properties, and Operator shall have the right to assess against the joint property covered hereby the following overhead charges:

- (a) \$ **150.00** per month for each drilling well, beginning on the date the well is spudded and terminating when it is on production or is plugged, as the case may be, except that no charge shall be made during suspension of drilling operations for fifteen (15) or more consecutive days.
- (b) \$ **25.00** per well per month for the first five (5) producing wells
- (c) \$ **15.00** per well per month for the second five (5) producing wells.
- (d) \$ **10.00** per well per month for all producing wells over ten (10).

In connection with overhead charges, the status of wells shall be as follows:

- (1) In-pit or key wells shall be included in overhead schedule the same as producing oil wells.
- (2) Producing gas wells shall be included in overhead schedule the same as producing oil wells.
- (3) Wells permanently shut down but on which plugging operations are deferred, shall be dropped from overhead schedule at the time the shutdown is effected. When such wells are plugged, overhead shall be charged at the producing well rate during the time required for the plugging operation.
- (4) Wells being plugged back or drilled deeper shall be included in overhead schedule the same as drilling wells.
- (5) Wells which are shut down temporarily and later replaced on production. If and when a well is shut down (other than for production) and not produced or worked upon for a period of a full calendar month, it shall not be included on the overhead schedule for such month.
- (6) Salt water disposal wells shall not be included in overhead schedule.

The above specific overhead rates may be amended from time to time by agreement between Operator and Non-operator if, in practice, they are found to be insufficient or excessive.

(13) Warehouse Handling Charges: ~~None~~

- (14) Any other expenditure incurred by Operator for the necessary and proper development, maintenance and operation of the joint property, except that Operator shall not charge the joint account with any expenditure or contribution made by Operator towards employees' stock purchase plan, group life insurance, pension, retirement, or bonus, other than such expenditures or contributions ~~for Operator's employees serving the joint property full time.~~

II. BASIS OF CHARGES TO JOINT ACCOUNT

- (1) Outside Purchases: All materials and equipment purchased and all service procured from outside sources shall be charged at their actual cost to Operator, after deducting any and all trade and/or cash discounts actually allowed off invoices, or received by Operator

- (2) New materials furnished by Operator (Condition "A"):

New materials transferred to the joint property from Operator's warehouse or other properties shall be priced f. o. b. the nearest supply store or railway receiving point at replacement cost of the same kind of materials. This will include large equipment such as tanks, rigs, pumps, boilers and engines. All tubular goods (2" and over) shall be charged on the basis of mill shipment or carload price. Other materials, where the replacement cost cannot be readily ascertained, may, for the purposes of consistency and convenience, be charged on the basis of a reputable supply company's preferential list price f. o. b. nearest supply store or railway receiving point to the joint property prevailing on the date of transfer of the materials to the joint property.

In determining the value of any transferred materials, all special and preferential discounts shall be allowed but the regular cash discount shall not be considered.

- (3) Secondhand materials furnished by Operator (Conditions "B" and "C"):

(a) Tubular goods (2" and over), fittings, machinery and other equipment which is in sound and serviceable condition at date of transfer, will be classed as condition "B" and charged at 75% of the price of new materials in accordance with the provisions of Paragraph (2) above.

(b) Tanks, derricks, and buildings or other equipment involving erection costs shall be charged on a basis not to exceed 75% of knocked-down new price for similar materials.

(c) Other secondhand materials, such as units of machinery or other equipment that is serviceable, but substantially not good enough to be considered first-class secondhand material when transferred to the joint property, shall be classed as condition "C" and charged at 50% of the new price.

(d) There may also be cases where some items of equipment, due to their unusual condition, should be fairly and equitably priced by Operator.

- (4) Warranty of Materials Furnished by Operator: Operator does not warrant the materials furnished from its warehouse or other properties beyond or back of the dealer's or manufacturer's guaranty, and in case of defective materials, credit shall not be passed until adjustment has been received by Operator from the manufacturers or their agents.

- (5) If materials required are not available in Operator's surplus stocks, Operator shall, whenever in its judgment it is practical to do so, give Non-operator opportunity of furnishing the materials required in proportion to his or its interest, provided that the same can be furnished at the time such materials are required, and further provided that any such materials so furnished shall be in condition acceptable to Operator and shall be charged to the joint account on the same terms and conditions as are provided herein to cover the furnishing of materials by Operator.

- (6) Operator's Exclusively-owned Facilities: The following rates shall apply to service rendered to the joint property by facilities owned exclusively by Operator:

(a) Water service, gas, teaming, power, and compressor service: All at rates currently prevailing in the field where the joint property is located.

(b) Automotive Equipment: Rates commensurate with cost of ownership and operation and in line with schedule of rates adopted by the Petroleum Motor Transport Association as recommended uniform standardized charges against the joint account. Automotive charges will be based on use in actual service on or in connection with the joint property. Truck, tractor and pulling unit rates shall include wages and expenses of driver.

(c) A fair rate shall be charged for the use of drilling and cleaning-out tools and any other items of Operator's fully-owned machinery or equipment which shall be ample to cover maintenance, repairs, depreciation and the service furnished the joint property. Provided, however, that such charges shall not exceed those currently prevailing in the field where the joint property is located.

(d) Whenever requested, Operator shall inform Non-operator in advance of the rates it proposes to charge.

(e) Rates shall be revised and adjusted from time to time when found to be either excessive or insufficient.

III. DISPOSAL OF LEASE EQUIPMENT AND MATERIALS

- (1) Materials purchased by Operator shall be credited to the joint account and included in the monthly statement of operations for the month in which the materials are removed from the joint property.

- (2) Materials purchased by Non-operator shall be invoiced by Operator and paid for by Non-operator to Operator immediately following receipt of invoice and delivery of materials. Operator shall thereupon immediately pass credit to the joint account and include the same in the monthly statement of operations for the month in which the materials were paid for by Non-operator.

- (3) Division of materials in kind, if made between Operator and Non-operator, shall be in proportion to their respective interests in the joint property. Each party will thereupon be charged individually with the value of the materials received or receivable and corresponding credits will be made to the joint account by Operator, and both credits shall appear in the same monthly operating statement.

- (4) Sales to outsiders of major materials shall be made only with the consent of Non-operator as to both terms and price and where made the proceeds shall be credited by Operator to the joint account at the full amount collected from vendee. Any claims by vendee for defective materials or otherwise shall be charged back to the joint account, if and when paid by Operator.

IV. BASIS OF PRICING MATERIALS TRANSFERRED FROM JOINT ACCOUNT

Materials and equipment purchased by either Operator or Non-operator, or divided in kind between them, unless otherwise agreed, shall be valued on the following basis of condition and price: (New price as used in the following paragraphs shall have the same meaning and application as that used above in Section II: "Basis of Charges to Joint Account.")

- (1) New Materials: (Condition "A") being new equipment or supplies purchased or procured for the joint property but never used thereon; at 100% of current new prices.

- (2) Good Secondhand Materials: (Condition "B") being good serviceable materials which are further usable without repair, at:

(a) 75% of current new prices, if materials were new when originally charged to the joint property.

(b) 75% of current new prices less depreciation consistent with their usage on and service to the joint property, if materials were originally charged to the joint property as secondhand at 75% of new prices.

- (3) Other Used Materials: (Condition "C") being materials further usable for their original function only after repair and reconditioning; at 50% of current new prices.

- (4) Bad Order Materials: (Condition "D") being materials not further usable for their original function but for possible other service; at 25% of current new prices.

- (5) Junk: (Condition "E") being obsolete and unserviceable materials; at prevailing junk prices in the district. Where practicable, junk should be disposed of at the joint property.

- (6) Temporarily Used Materials: When the use of certain items of equipment on the joint property has been only temporary, and the time of actual use thereon does not justify the deduction of depreciation as listed in (a) and (b) of Paragraph (2) hereof, such materials will be priced on a basis that will leave a net charge against the joint account consistent with the service rendered and adequate for the time the materials were in use.

V. INVENTORIES

- (1) Periodic inventories shall be taken by Operator of the materials and equipment on the joint property, which shall include such materials and equipment as are ordinarily considered controllable by operators of oil and gas properties.

- (2) Notice of intention to take inventory shall be given by Operator to Non-operator a week before any inventory is to begin, so that Non-operator may be represented when any inventory is being taken.

- (3) Special inventories shall be taken whenever there is any sale or change of interest in the joint property, and it shall be the duty of the party selling to notify the other party as quickly as possible after the transfer of interest takes place. In such cases both the seller and the purchaser shall be represented and shall be governed by the joint inventory.

- (4) If the initial test on the joint property is a dry hole and no further tests thereon are immediately contemplated, Non-operator may require that an inventory be taken of all materials as soon as the casing has been recovered from the well and that the materials be classified before any materials are removed from the joint property by Operator or otherwise disposed of.

- (5) Failure of Non-operator to be represented at the physical inventory shall bind it to accept the inventory taken by Operator who shall in that event furnish Non-operator with a copy thereof.

- (6) Reconciliation of inventory with charges to the joint account shall be made by each party at interest, and a list of overages and shortages shall be jointly determined by Operator and Non-operator.

- (7) Inventory adjustments shall be made by Operator on the joint account for overages and shortages, but Operator shall only be held accountable to Non-operator for shortages due to lack of reasonable diligence.