UNIT OPERATING AGREEMENT
DEER CANYON UNIT
EDDY COUNTY, NEW MEXICO

I N D E X

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THIS AGREEMENT entered into as of the 1st day of September, 1973, by and between the parties who have signed the original of this instrument, a counterpart thereof, or other instrument agreeing to be bound by the provisions hereof.

WITNESSETH:

WHEREAS, the parties hereto as working interest owners have entered into, as of the date hereof, a Unit Agreement for the Development and Operation of the Deer Canyon Unit Area, Eddy County, New Mexico, hereinafter referred to as the "unit agreement', which among other things provides for a "unit operating agreement", to be entered into by and between the working interest owners for the purpose of providing for the allocation of costs of operation and development of the unit area and the production of unitized substances therefrom among the working interest owners, and to otherwise provide for the development and operation of the unit area as set forth in said unit agreement.

NOW THEREFORE, it is mutually agreed by and between the parties hereto as follows:

ARTICLE I

CONFIRMATION OF UNIT AGREEMENT

1.1 The aforesaid unit agreement and all exhibits attached thereto are hereby confirmed and made a part of this agreement.

ARTICLE II

TITLE EXAMINATION AND LOSS OF LEASES

2.1 Title Examination: The parties hereto shall, as soon as practicable, submit to unit operator copies of their

respective leases embracing lands committed to the unit area, together with all rental receipts and copies of any and all title opinions covering said lands, and shall loan to unit operator for examination all abstracts which they may have covering said lands. Unit operator shall procure all supplemental abstracts and other title papers which may be necessary or required to examine title to the leasehold interests pertinent to any drillsite and all expenses incurred in examining title shall be charged as an expense to the parties participating in the drilling of any test well in proportion to their respective interests.

2.2 Failure of Title: Should any oil and gas lease, or interest therein, be lost through failure of title, this agreement shall nevertheless continue in force as to all remaining leases and interests, and

(1) Each party whose lease or interest therein is affected by the failure of title shall bear alone the entire loss resulting from failure of title to such party's lease or interest therein, and it shall not be entitled to recover from operator or other parties any development or operating costs which it may have theretofore paid, but there shall be no monetary liability on its part to the other parties hereto by reason of such title failure; and

(2) There shall be no retroactive adjustment of expenses incurred or revenues received from the operation of the interest which has been lost, but the interests of the parties shall be revised on an acreage basis, as of the time it is finally determined that title failure has occurred, so that the interest of the party or parties whose lease or interest is affected by the title failure will thereafter be reduced in the unit area by the amount of the interest lost; and

(3) If the proportionate interests of the other parties hereto in any producing well theretofore drilled on the unit area is increased by reason of the title failure, the party whose title has failed shall receive the proceeds attributable to the increase in such interests (less operating costs attributable thereto) until it has been reimbursed for unrecovered costs paid by it in connection with such well; and

(4) Should any person not a party to this agreement, who is determined to be the owner of any interest in the title which has failed, pay in any manner any part of the cost of operation, development or equipment previously paid under this agreement, such amount shall be proportionately paid to the party or parties hereto who in the first instance paid the costs which are so refunded; and

(5) Any liability to account to a third party for prior production of oil and gas which arises by reason of title failure shall be borne by the parties in the same proportion in which they shared in such prior production.

2.3 Loss of Leases for Causes Other Than Title Failure: If any lease or interest subject to this agreement be lost through failure to develop or because express or implied covenants have not been performed, or if any lease be permitted to expire at the end of its primary term and not be renewed or extended, or if any lease or interest therein is lost due to the fact that the production therefrom is shut in by reason of lack of market, the loss shall not be considered a failure of title and all such losses shall be joint losses and shall be borne by all parties in proportion to their interests and there shall be no readjustment of the participating interests of the parties hereto on account thereof.

ARTICLE III

MANAGEMENT OF UNIT

3.1 Unit Operator and Employees. Roberts, Koch & Cartwright, a partnership composed of Ross D. Roberts, Charles E. Koch and Jack C. Cartwright, the party hereto named as unit operator of the unit area under the provisions of the unit agreement, or its duly appointed successor unit operator, shall have the exclusive right to develop and operate the unit area subject to the provisions of this agreement and the unit agreement. All individuals employed by unit operator in the conduct of operations hereunder shall be the employees of unit operator alone and their working hours, rates of compensation and all other matters relating to their employment shall be determined solely by unit operator.

3.2 Unit Operator - Duties: Unit Operator shall in the conduct of operations hereunder:

(a) Conduct the operations in a good and workmanlike manner, and in the exercise of its judgment and discretion, acting in good faith;

(b) Consult freely with working interest owners concerning unit operations, and keep working interest owners informed of all matters arising during the operation of the unit area which unit operator, in the exercise of its best judgment, considers important;

(c) Keep full and accurate records of all costs incurred, rentals and royalties paid, and controllable materials and equipment, which records, receipts and vouchers in support thereof shall be available for inspection by authorized representatives of the working interest owners at reasonable intervals during usual business hours, at the office of the unit operator;

(d) Permit the working interest owners, each through their duly authorized representatives, but at their sole risk and expense, to have access to the unit area at all times, and to the derrick floor of each well drilled or being drilled hereunder, for the purpose of observing operations conducted hereunder and inspecting jointly owned materials, equipment and other property, and to have access at reasonable times to information and data in the possession of unit operator concerning the unit area;

(e) Furnish to each of the other parties who make timely written request therefor copies of all drilling reports, well logs and samples of cores or cuttings taken from wells drilled hereunder, containers therefor to be furnished by the party requesting such samples;

(f) Comply with the terms and conditions of the unit agreement and all valid applicable federal and state laws and regulations;

(g) Keep the land in the unit area free from liens and encumbrances occasioned by its operations, except such liens as the working interest owners elect to contest, and save only the lien granted the unit operator under this agreement.

3.3 Unit Operator - Restrictions: The unit operator shall not do any of the following things without the consent of the working interest owners obtained as herein provided:

(a) Locate, drill, deepen or plug back any well or let any contract therefor except the initial well, substitute well or second well as provided in Sections 5.1 and 5.2. The approval of the drilling, deepening or plugging back of any other well shall not be construed to mean and include the approval of any necessary expenditures incurred in completing and equipping such well, but shall include the plugging and abandonment of same if a dry hole,

except as otherwise provided in Article V hereof;

(b) Make any expenditures in excess of Ten Thousand Dollars ($10,000.00) for any one single project. Operator shall furnish copies of its "Authority for Expenditures" for any such items.

(c) Make any expenditure for expert technical advice, including any extra services rendered by unit operator's technical staff, not contemplated by the provisions of Exhibit "B" attached hereto, and not covered by the overhead, district and camp expenses therein authorized, which overhead in Exhibit "B" is intended to cover only normal development and operations;

(d) Make any partial relinquishment of the rights of the unit operator;

(e) Abandon any well which has been completed as a producing well or dispose of any major items of surplus material or equipment, other than junk, having an original cost of Three Thousand Dollars ($3,000.00) or more (any such item or items of less cost may be disposed of without such approval), except as may otherwise be provided herein;

(f) Designate the lands to be included in any participating area or enlargement thereof, or submit for approval any plan for the development and operation of the unit area or any participating area or supplement or amendment thereto in accordance with the provisions of the unit agreement;

(g) Determine whether to drill a demanded offset well or pay compensatory royalty;

(h) Drill or abandon any injection wells or convert any well into an injection well;

(i) Determine not to pay the annual rental, advance rental or delay rental under any lease.

In case of blowout, explosion, fire, flood or other sudden emergency, unit operator may take such steps and incur such expense as, in its opinion, are required to deal with the emergency and to safeguard life and property; provided that unit operator shall, as promptly as possible, report the emergency to the other parties and shall endeavor to secure any sanction that might otherwise have been required.

Subject to the provisions of this agreement, unit operator shall have full control of the premises subjected hereto and shall conduct and manage the development and operation of unitized lands for the production of unitized substances therefrom for the account of the parties hereto.

3.4 Designation of Representatives: Each working interest owner shall in writing inform unit operator of the names and addresses of its representative and alternate who are authorized to represent such working interest owner with respect to unit operations. The representative or alternate may be changed from time to time by written notice to unit operator.

3.5 Meetings: All meetings of working interest owners shall be called by unit operator upon its own motion or at the request of two (2) or more working interest owners. No meeting shall be called on less than fourteen (14) days advance written notice, with agenda for the meeting attached. Working interest owners who attend the meeting shall not be prevented from amending items included in the agenda or from deciding the amended item or other items presented at the meeting. The representative of unit operator shall be chairman of each meeting.

3.6 Voting Procedure: Working interest owners shall decide all matters coming before them as follows:

3.6.1 Voting Interest: Each working interest

owner shall have a voting interest equal to its percentage of participation as set out in Column 7 of Exhibit "A" hereof.

3.6.2 Vote Required: Working interest owners shall act upon and determine all matters coming before them by an affirmative vote of 75% of the voting power of the working interest owners having leasehold interests committed to the unit agreement; provided, however, should any one working interest owner have 75% or more voting interest its vote must be supported by the vote of one other working interest owner.

3.6.3 Vote at Meeting by Nonattending Working Interest Owner: Any working interest owner who is not represented at a meeting may vote either by written proxy or by letter or telegram addressed to the representative of the unit operator, provided such letter or telegram is received prior to the submission of such item to vote. If the vote is by letter or telegram such vote shall not be counted with respect to any item on the agenda which has been materially changed at the meeting.

3.6.4 Poll Votes: Working interest owners may vote on and decide, by letter or telegram, any matter submitted in writing to working interest owners, if no meeting is requested as provided in Section 3.5 within seven (7) days after the proposal is sent to working interest owners. Unit operator shall give prompt notice of the results of the voting to all working interest owners.

3.7 Unit Operator - Liabilities: Unit Operator shall not be liable to any of the working interest owners for anything done or omitted to be done by it in the conduct of operations hereunder while acting in compliance with Section 3.2(a) hereof, except in connection with any losses or liabilities sustained as a result of gross negligence. The provisions of this section shall not relieve operator of its duty to obtain the consent of the working interest owners in accordance with the provisions of Section 3.6.

ARTICLE IV

COST OF OPERATIONS AND
ALLOCATION OF PRODUCTION

4.1 Cost of Operations and Accounting Procedures: The actual cost to the unit operator of performing its obligations as unit operator hereunder shall be apportioned, except with respect to the initial test well, substitute test well and second test well as provided in Section 5.1 and 5.2 hereof, among the working interest owners having leasehold interests committed to the unit agreement in accordance with the percentages set forth in Column 7, Page 3, of Exhibit "A" attached hereto and made a part hereof, and said owners in accordance with the Accounting Procedure attached hereto, made a part hereof, and for purposes of identification marked Exhibit "B".

4.2 Allocation of Production: All unitized substances produced and saved from each participating area established pursuant to the unit agreement shall be deemed to have been produced equally on an acreage basis from the several tracts of unitized lands of the participating area established for such production and for the purpose of computing and paying all royalties, overriding royalties and obligations payable out of production of the respective working interest owners, each such tract of unitized land shall have allocated to it such percentage of said production as the number of acres of each tract included in said participating area bears to the total number of acres of unitized land in said participating area in conformity with Section 12 of the unit agreement.

All production remaining after allocating the production for the purpose of paying royalties, overriding royalties and obligations payable out of production as above provided (and being the working interest) shall be allocated to the respective working interest owners (except as to the initial test well, substitute well and second test well as provided in Sections 5.1 and 5.2) in

accordance with the percentages reflecting their net respective beneficial interests as shown in Column 8 on Page 3 of Exhibit "A" attached hereto.

Exhibit "A" shows the interest of each working interest owner as of the time of the commitment of the respective tracts to the unit agreement, as well as the beneficial interests of each working interest owner, after taking into consideration the contribution of certain interests in connection with the drilling of the initial test well as reflected in said exhibit.

The beneficial interests of the respective working interest owners as shown on Exhibit "A" have been determined as to each party on an adjusted surface acreage basis. The adjustment insurface area has been made by determining the fraction of the total unitized substances produced from or allocated to any tract which may be required to meet all royalty, overriding royalty, production payments or other obligations payable out of production from or allocated to such tract and multiplying that fraction by the number of acres contained in such tract and deducting the product from the total number of acres in said tract, the remainder being the adjusted surface acreage in each such tract. The beneficial interest of each party shown on Exhibit "A" attached hereto represents the sum of the net acre interests in all tracts committed by each party to the unit agreement divided by the total number of net acres committed to the unit area.

Except as hereinafter provided, the percentages of participation of the parties hereto in costs of operation and allocation of production as shown on Exhibit "A" shall remain the same regardless of any contraction of the unit area or automatic elimination of lands therefrom in accordance with Section 2 of the unit agreement. There shall be a readjustment of the adjusted surface acres among the parties hereto on the basis set forth hereinabove and

the interests of the parties recomputed on the basis of the revised acreage upon the occurrence of any of the following events:

(i) the working interest in any tract shown on Exhibit "A" is not committed to the unit agreement;

(ii) upon the commitment of any working interest to the unit agreement after operations have been commenced in accordance with Section 8.3 hereof;

(iii) any tract is eliminated through failure of title or lost through failure to pay rentals in conformity with Section 6.1 hereof;

(iv) if there should be any errors in mathematical computations or there is any additional overriding royalty interest or lease burden unknown to the parties hereto outstanding as of the time of the commitment of the respective tracts to the unit agreement;

(v) to carry out the adjustments in acreage ownership and participating interests required by the acreage contribution agreements referred to in Section 5.1 hereof;

If any tract committed to the unit agreement becomes burdened with any additional overriding royalties, production payments or lease burdens other than those shown on Exhibit "B" attached to the unit agreement, the same shall be borne exclusively by the owner or owners of such tract.

4.3 Conflict of Instruments: In the event of any conflict between the provisions contained either in the body of this instrument or in the unit agreement and those contained in the Accounting Procedure, the provisions of the unit agreement shall govern to the extent of such conflict. If any provision of Exhibit "B" shall be inconsistent with any provision contained in the body of this agreement, the provisions in the body of this agreement shall prevail. The term "Operator" as used in Exhibit "B" shall be deemed to refer to the unit operator, and the term "Non-Operators" as used in Exhibit "B" shall be deemed to refer to the working interest owners herein other than the operator.

4.4 Advances: Operator, at its election, shall have the right from time to time to demand and receive from the other

parties which are participating in the unit operation then being carried on payment in advance of their respective shares of the estimated amount of the costs to be incurred in operations hereunder during the next succeeding month, which right may be exercised only by submission to each such party of an itemized statement of such estimated costs, together with an invoice for its share thereof. Each such statement and invoice for the payment in advance of estimated costs shall be submitted on or before the 20th day of the next preceding month. Each party shall pay to Operator its proportionate share of such estimate within fifteen (15) days after such estimate and invoice is received. If any party fails to pay its share of said estimate within said time, the amount due shall bear interest at the rate of ten percent (10%) per annum until paid. Proper adjustment shall be made monthly between advances and actual cost, to the end that such party shall bear and pay its proportionate part of actual costs incurred, and no more.

4.5 Taxes: All of the jointly owned personal property within the unit area shall be rendered by the unit operator for ad valorem taxes if necessary. The unit operator shall pay all ad.valorem taxes rendered or assessed against said properties, and all such amounts so paid by the unit operator shall be charged to the joint account of the parties hereto. All other taxes which may be levied upon or against the respective leasehold interests or measured by the production of unitized substances allocated to the respective tracts under the terms of the unit agreement and this agreement shall be paid by the respective working interest owners having interests in such tracts.

4.6 Insurance: As to all operations hereunder, unit operator shall carry for the benefit and protection of the parties

insurance as specified in Exhibit "C". Operator shall require all contractors engaged in work on or for the unit area to comply with workmen's compensation laws of the state where the operations are being conducted and to maintain such other insurance as Operator may require.

4.7 Operator's Lien: Each non-operator hereby grants to Operator a first and preferred lien on the interest of such non-operator and all property covered by this agreement whether now owned or hereafter acquired on the unit area and such party's interest in oil and gas produced and the proceeds thereof, and upon such party's interest in material and equipment,to secure the payment of all sums due from such party to operator.

In the event any party fails to pay any amount owing by it to operator as its share of such costs and expenses or such advance estimate within the time limited for payment thereof, operator, without prejudice to other existing remedies, is authorized at its election (unless there is a bona fide dispute) to collect from the purchaser or purchasers of oil or gas, the proceeds accruing to the working interest or interests in the unit area of the delinquent party up to the amount owing by such party, and each purchaser of oil or gas is authorized to rely upon operator's statement as to the amount owing by such party.

In the event of the neglect or failure of any non-operating party to promptly pay its proportionate part of the cost and expense of development and operation when due, the other non-operating parties (which are participating in the unit operation for which such costs and expenses were incurred) and operator, within thirty (30) days after the rendition of statements therefor by operator, shall proportionately contribute to the payment of such delinquent indebtedness and the non-operating parties so contributing shall

be entitled to the same lien rights as are granted to operator in this section. Upon the payment by such delinquent or defaulting party to operator of any amount or amounts on such delinquent indebtedness, or upon any recovery on behalf of the non-operating parties under the lien conferred above, the amount or amounts so paid or recovered shall be distributed and paid by operator to the other non-operating parties and operator proportionately in accordance with the contributions theretofore made by them.

Likewise, non-operators are hereby granted a prior lien on the rights and interest of the unit operator as a working interest owner in the unit area and unitized substances and, upon the interest of the unit operator in all materials and equipment, to secure the payment of any amounts which may become due and owing from unit operator to any of the non-operators, which lien shall be subject to all of the terms and conditions provided for in the preceding paragraph.

ARTICLE V

WELLS

5.1 Initial Test Well: Within 30 days after the effective date of the unit agreement, unit operator shall commence operations on the initial test well which is required to be drilled pursuant to the provisions of Section 9 of the unit agreement (unless such well should be commenced prior to the effective date of said unit agreement). Said well shall be located 660 feet from West Line and 1980 feet from North Line, Section 14, Township 20 South, Range 21 East, N.M.P.M. and shall be drilled in compliance with Section 9 of the unit agreement and shall also be drilled in accordance with the applicable regulations of the Secretary of the Interior and the New Mexico Oil Conservation Commission; provided, however, unit operator shall not in any event be required to drill said

well to a depth in excess of 8,700 feet and the drilling of said well may be discontinued at a lesser depth if granite or other practically impenetrable substance should be encountered or if the parties participating in the cost of drilling the well agree to complete the well at a lesser depth, and provided, further, in the event difficulty should be encountered in drilling which results in the loss of the hole, making it necessary to abandon the same, a substitute well may be commenced within 60 days and such substitute well shall be considered the same as the initial test well and all provisions hereof applicable to the initial test well shall be applicable to the substitute well. Operator shall make reasonable tests of all formations encountered during drilling which give indication of containing oil or gas in sufficient quantities to test.

All costs incurred in drilling, completing and placing said well on production, if completed as a producer, and of plugging and abandoning the same, if completed as a dry hole, shall be borne only by the parties hereto as shown in Column 5, Page 3, of Exhibit "A" attached hereto and made a part hereof.

In the event of the discovery of unitized substances in paying quantities, the initial test well shall be completed and placed on production as such wells are usually and customarily completed in accordance with good oil field practices and all casing, tubing, wellhead connections, flow lines, tanks and other equipment which may be installed in or used in connection with said well shall be owned by the parties participating in the cost of drilling said well in the proportions shown in Column 6 on Page 3 of said Exhibit "A" until said well shall have paid out as herein provided.

Cities Service Oil Company, Petroleum, Inc., Aztec Oil & Gas Company and Union Oil Company of California (hereinafter referred to as "contributing parties") have agreed to make acreage contributions to Roberts, Koch & Cartwright toward the drilling of the initial test well upon the following terms and conditions: Upon the initial test well being drilled to the depth provided herein and being completed as a well capable of producing unitized substances in paying quantities, Roberts, Koch & Cartwright shall earn and be entitled to an undivided 1/2 interest in and to all lease rights of the contributing parties in and to the leasehold interest committed by said parties to the unit agreement as shown on Exhibit "B" attached thereto down to 100 feet below total depth drilled in said well and in addition, Roberts, Koch & Cartwright shall be entitled to receive and the contributing parties do hereby relinquish to Roberts, Koch & Cartwright all of their rights to participate in and to any of the production of unitized substances from the initial test well until such time as said well has paid out as hereinafter defined; provided, however, the contributing party shall be entitled to receive and Roberts, Koch & Cartwright shall pay out of its working interest the following overriding royalty interest based upon all unitized substances produced, saved and marketed from the initial test well until said well is paid out:

Cities Service Oil Company ---------- 28.47535% of 6.25% of 8/8

Petroleum, Inc. ---------- 15.66464% of 5% of 8/8

Aztec Oil & Gas Company ---------- 7.71087% of 5% of 8/8

Union Oil Company of California ------- 6.76763% of 5% of 8/8

Upon the completion of the initial test well or any substitute therefor as a well capable of producing unitized substances in paying quantities, the contributing parties shall as

soon as practicable and in any event within 30 days from the time of completion of said well execute and deliver to Roberts, Koch & Cartwright good and sufficient instruments without warranty of title conveying an undivided 1/2 interest in and to the leasehold interest committed by said parties to the unit agreement down to 100 feet below total depth drilled in said well. The acreage contributions referred to herein are more particularly shown on Page 3 of Exhibit "A" attached hereto.

For the purposes of this agreement, the initial test well shall be considered as paid out beginning as of 7 a.m. on the first day following the date on which Roberts, Koch & Cartwright has recovered out of the beneficial interest production which would otherwise have been attributable to the contributing parties after deducting all severance, ad valorem and production taxes apportionable thereto that portion of the actual cost of drilling, completing, testing and equipping said well (including necessary wellhead connections, flow lines, tanks, pumping and other equipment in connection with said well), together with all costs of operating the same during the payout period which would otherwise have been allocated to the contributing parties in connection with the initial test well. Operator shall furnish to all of the parties hereto as soon as possible and in any event within 60 days from date of completion of said well an itemized statement of the costs of drilling, testing, completing and placing the well on production and the Operator shall also furnish to the parties hereto monthly reports showing the unitized substances produced, saved and marketed from said well and the operating costs incurred in connection therewith. All costs incurred in connection with said well shall be in accordance with the Accounting Procedure attached hereto as Exhibit "B".

Within 30 days after receiving notice from Operator of payout of the initial test well, each of the contributing parties shall have the right to continue to receive said overriding royalty by giving notice thereof to Operator within such time. Upon failure of any contributing party to exercise said option to continue to receive said overriding royalty within said time, the overriding royalty of each such party shall terminate and the respective contributing party shall be entitled to receive from the time of payout their proportionate part of production as shown in Column 8 on Page 3 of Exhibit "A" and shall also own their proportionate parts of all equipment installed in and used in connection with the initial test well as shown in Column 7 on Page 3 of Exhibit "A".

5.2 Second Test Well: If the initial test well provided for in Section 5.1 hereof is drilled to the objective depth provided in said section and is completed as a dry hole or well not capable of producing unitized substances in paying quantities, operator shall have the right and option to commence or possibly commence operation within 80 days from the time of completion of said well an additional test well at a location of its choice upon the unit area and if operator elects to drill the second test well the same shall be drilled upon the same terms and conditions as provided in Section 5.1 hereof for the drilling of the initial test well, and if such second well is completed as a well capable of producing unitized substances in paying quantities operator shall earn the same interest as far as the contributing parties referred to in Section 5.1 are concerned as it would have earned had the initial test well been completed as a well capable of producing unitized substances in paying quantities, and all of the provisions of Exhibit "A" relating to the rights and interests of contributing parties in the cost applicable to the test well shall be applicable

to said well. However, the payout provisions hereof shall be limited to the cost of drilling, completing, testing and equipping said second test well and shall not include the cost of the initial test well or the plugging and abandoning of the same.

If operator does not elect to exercise its option to drill a second test well within the time herein provided and the parties cannot mutually agree upon the drilling of an additional exploratory well, such well may be drilled by any of the parties hereto in accordance with the provisions of Section 5.6 hereof, provided said well is commenced within the time provided under the unit agreement for the drilling of an additional well or extension of the time which may be granted for the drilling of such well.

5.3 Modification of Drilling Requirements of Unit Agreement: The unit operator may apply for and obtain a modification of the drilling requirements of said unit agreement or an extension or extensions of time within which to comply therewith as provided by the terms of said unit agreement, and any such application or applications may be made without the consent of any of the working interest owners subscribing hereto as parties of the second part.

5.4 Drilling Contracts: All wells drilled on the unit area shall be drilled on a competitive contract basis at the usual rates prevailing in the area. Operator, if it so desires, may employ its own tools and equipment in the drilling of wells, but its charges therefor shall not exceed the prevailing rates in the field, and the rate of such charges shall be agreed upon by the participating parties in writing before drilling operations are commenced, and such work shall be performed by operator under the same terms and conditions as shall be customary and usual in the field in contracts of independent contractors who are doing work of a similar nature.

5.5 Development and Operation Subsequent to Discovery of Unitized Substances in Paying Quantities: After the discovery of unitized substances in paying quantities on the unit area, unit operator shall only drill such wells as may be provided for in any plan of development and operation for the unit area or amendment or supplement thereto filed and approved as provided by Section 10 of the unit agreement after approval by the parties hereto as provided by Section 3.3 hereof, and all such wells shall be drilled for the joint account of the parties hereto and the production of unitized substances therefrom shall be allocated to said parties as provided in Column 8, Page 3, of Exhibit "A"; provided, however, the drilling, deepening, plugging back or re-working of any such well shall be subject to the non-consent provisions of Section 5.6 hereof.

5.6 Operations by Less Than All Parties: If all of the parties cannot mutually agree upon the drilling of any well on the unit area (other than the initial or substitute test well provided for in Section 5.1 or a second exploratory well in the event operator should elect to drill the same in accordance with the provisions of Section 5.2 hereof) or upon the reworking, deepening, or plugging back of a dry hole at the joint expense of all parties or a well jointly owned by all the parties and not then producing in paying quantities on the unit area, any party or parties wishing to drill, rework, deepen or plug back such a well may give the other parties written notice of the proposed operation, specifying the work to be performed, the location, proposed depth, objective formation and the estimated cost of the operation. The parties receiving such a notice shall have 30 days

(except where a drilling rig is on location the period shall be limited to forty-eight (48) hours exclusive of Saturday, Sunday or holidays) after receipt of the notice within which to notify the parties wishing to do the work whether they elect to participate in the cost of the proposed operation. Failure of a party receiving such a notice to reply to it within the period above fixed shall constitute an election by that party not to participate in the cost of the proposed operation.

If any party receiving such a notice elects not to participate in the proposed operation (such party or parties being hereafter referred to as "non-consenting party"), then in order to be entitled to the benefits of this section, the party or parties giving the notice and such other parties as shall elect to participate in the operation (all such parties being hereafter referred to as the "consenting parties") shall, within thirty (30) days after the expiration of the notice period of thirty (30) days (or as promptly as possible after the expiration of the 48-hour period where the drilling rig is on location, as the case may be) actually commence work on the proposed operation and complete it with due diligence.

The entire cost and risk of conducting such operations shall be borne by the consenting parties in the proportions that their respective interests bear to the aggregate interests of the consenting parties. Consenting parties shall keep the leasehold estates involved in such operations free and clear of all liens and encumbrances of every kind created by or arising from the operations of the consenting parties. If such an operation results in a dry hole, the consenting parties shall plug and abandon the well at their sole cost, risk and expense. If any well drilled, reworked, deepened or plugged back under the pro-

visions of this section results in a producer of oil or gas in paying quantities, the consenting parties shall complete and equip the well to produce at their sole cost and risk, and the well shall then be turned over to the operator and shall be operated at the expense and for the account of the consenting parties. Upon commencement of operations for the drilling, re-working, deepening or plugging back of any such well by consenting parties in accordance with the provisions of this section, each non-consenting party shall be deemed to have relinquished to consenting parties, and consenting parties shall own and be entitled to receive, in proportion to their respective interests, all of such non-consenting party's interest in the well, its lease-hold operating rights, and share of production therefrom until the proceeds or market value thereof (after deducting production taxes, royalty, overriding royalty and other interests payable out of or measured by the production from such well accruing with respect to such interest until it reverts) shall equal the total of the following;

(a) 100% of each such non-consenting party's share of the cost of any newly acquired surface equipment beyond the well connections (including, but not limited to, stock tanks, separators, treaters, pumping equipment and piping), plus 100% of each such non-consenting party's share of the cost of operation of the well commencing with first production and continuing until each such non-consenting party's relinquished interest shall revert to it under other provisions of this section, it being agreed that each non-consenting party's share of such costs and equipment will be that interest which would have been chargeable to each non-consenting party had it participated in the well from the beginning of the operation; and

(b) 200% of that portion of the costs and expenses of drilling, reworking, deepening or plugging back, testing and completing, and 200% of that portion of the cost of newly acquired equipment in the well (to and including the wellhead connections), which would have been chargeable to such non-consenting party if it had participated therein.

In the case of any reworking, plugging back or deeper drilling operation, the consenting parties shall be permitted to use, free of cost, all casing, tubing and other equipment in the well, but the ownership of all such equipment shall remain unchanged, and upon abandonment of a well after such reworking, plugging back or deeper drilling, the consenting parties shall account for all such equipment to the owners thereof, with each party receiving its proportionate part in kind or in value.

Within 60 days after the completion of any operation under this section, the party conducting the operations for the consenting parties shall furnish each non-consenting party with an inventory of the equipment in and connected to the well, and an itemized statement of the cost of drilling, deepening, plugging back, testing, completing and equipping the well for production. Each month thereafter, during the time the consenting parties are being reimbursed as above provided, the consenting parties shall furnish the non-consenting parties with an itemized statement of all costs and liabilities incurred in the operation of the well, together with a statement of the quantity of oil and gas produced from it and the amount of proceeds realized from the sale of the well's working interest production during the preceding month. Any amount realized from the sale or other disposition of equipment newly acquired

in connection with any such operation which would have been owned by a non-consenting party had it participated therein shall be credited against the total unreturned costs of the work done and if the equipment purchased in determining when the interest of such non-consenting party shall revert to it as above provided; if there is a credit balance, it shall be paid to such non-consenting party.

If and when the consenting parties recover from a non-consenting party's relinquished interest the amounts provided for above, the relinquished interests of such non-consenting party shall automatically revert to it and from and after such reversion such non-consenting party shall own the same interest in such well, the operating rights and working interest therein, the material and equipment in or pertaining thereto, and the production therefrom as such non-consenting party would have owned had it participated in the drilling, reworking, deepening, or plugging back of said well. Thereafter, said non-consenting party shall be charged with and shall pay its proportionate part of the further costs of the operation of said well in accordance with the terms of this agreement and the Accounting Procedure, Exhibit "B", attached hereto.

No well drilled by less than all parties pursuant to the provisions of this Section 5.6 shall be completed as a gas well in the same formation as any other gas well then producing, or capable of producing, gas in paying quantities from the unit area unless the same be located on a regular well spacing or proration unit established for the area by the New Mexico Conservation Commission, so that the well density in the same formation will not be greater than that established or prescribed by the Commission for said area. No well drilled or completed by less than

all of the parties pursuant to the provisions of this Section 5.6 shall be completed as an oil well in the same formation as any other oil well then producing from the unit area if, as a result of the completion of said well, there would exist on the unit area a well density in the same formation of more than one producing oil well to a proration unit.

If any party hereto shall hereafter create any overriding royalty, production payment or other burden against its working interest production and if any other party or parties should conduct non-consent operations pursuant to the provisions of Section 5.6 and as a result, become entitled to receive the working interest production otherwise belonging to the non-participating party, the party or parties entitled to receive the working interest production of the non-participating party shall receive such production free and clear of burdens against such production which may have been created subsequent to this agreement and the non-participating party creating such burdens shall save the participating party or parties harmless with respect to the receipt of such working interest production.

The provisions of this section shall have separate application to the cost of completing and equipping any well drilled under the provisions of Section 5.6 and any party who has elected to join in the drilling, reworking, deepening, or plugging back of a well may refrain from joining in the completion thereof. However, the party who has refrained from joining in the drilling, reworking, deepening or plugging back of a well shall have no right to join in the completion thereof. After any well hereunder has been drilled to its authorized or projected depth and has been adequately tested, operator shall give notice to non-operators of its election as to whether such well should

be plugged and abandoned as a dry hole or casing be set in an attempt to complete the well as a producer or that such well be drilled deeper. Non-Operator shall have forty-eight (48) hours after receipt of the aforementioned notice from operator within which to notify operator whether it elects to have said well plugged and abandoned as a dry hole or have casing set in an attempt to complete the well as a producer or that such well be drilled deeper. Failure of non-operator to so notify operator within the above specified time shall be deemed concurrence in the operator's election. If the parties are able to agree, operator shall conduct future operations for the joint account. In the event of disagreement, the party or parties wishing to set casing in an attempt to complete the well or to deepen the well may do so at its sole risk, cost and expense and with right of recoupment pursuant to the provisions of Section 5.6 of this Agreement, provided, however, in the event of a conflict between an election to complete and an election to deepen, the party or parties electing to complete shall have the paramount right.

5.7 Abandonment of Producing Wells: No well, other than any which has been drilled or reworked pursuant to Section 5.6 hereof for which the consenting parties have not been fully reimbursed as therein provided, which has been completed as a producer shall be plugged and abandoned without the consent of all parties; provided, however, if all parties do not agree to the abandonment of any well, those wishing to continue its operation shall tender to each of the other parties its proportionate share of the value of the well's salvageable material and equipment, determined in accordance with the provisions of Exhibit "B", less the estimated cost of salvaging the estimated cost of plugging and abandoning. Each abandoning party shall then assign to the non-abandoning

parties, without warranty, express or implied, as to title or as to quantity, quality or fitness for use of the equipment and material, all of its interest in the well and its equipment, together with its interest in the leasehold estate as to, but only as to, the interval or intervals of the formation or formations then open to production. The assignments, so limited, shall encompass the "drilling unit" upon which the well is located. The payments by, and assignments to, the assignees shall be in a ratio based upon the relationship of their respective percentages of participation in the unit area to the aggregate of the percentages of participation in the unit area of all assignees. There shall be no readjustments of interests in the remaining portion of the unit area.

After the assignment, the assignors shall have no further responsibility, liability or interest in the operation of or production from the well in the interval or intervals then open. Upon request of the assignees, operator shall continue to operate the assigned well for the account of the non-abandoning parties at the rates and charges contemplated by this agreement, plus any additional costs and charges which may arise as the result of the separate ownership of the assigned well.

5.8 Required Well. For purposes of this article, a well shall be deemed a required well if the drilling thereof is required by the final order of an authorized representative of the Department of Interior or the Commissioner of Public Lands. Such an order shall be deemed final upon expiration of the time allowed for appeal therefrom without the commencement of appropriate legal proceedings or if such proceedings are commenced within said time upon the final disposition of the appeal. Whenever Operator receives any such order, it shall promptly mail a copy thereof to

each of the other parties; if any such order is appealed, the party appealing shall give prompt written notice thereof to each of the other parties and upon final disposition of the appeal, Operator shall give each of the other parties prompt written notice of the results therefrom.

Any party desiring to drill or participate in the drilling of a required well shall give to Operator written notice thereof within 30 days after the order requiring such well becomes final, or within such lesser time as may be required by such order. If such notice is given within said period, Operator shall drill the required well for the account of the party or parties giving such notice who shall bear all costs incurred therein; the rights and obligations of such party or parties with respect to the ownership of such well, the operating rights therein, the production therefrom and the bearing of costs incurred therein shall be the same as if the well had been drilled for the account of such party or parties under Article 5.6 hereof.

If no party elects to drill a required well within the period allowed for such election and if any of the following alternatives is available, the first such alternative which is available shall be followed:

(a) Compensatory Royalties. If compensatory royalties may be paid in lieu of drilling a well and if payment thereof is authorized by the parties within said period, the operator shall pay such compensatory royalties; or

(b) Contraction. If the drilling of a well may be avoided without other penalty by a contraction of the unit area through exclusion of lands not then within a participating area, unit operator shall make a reasonable effort to effect such contraction with the approval of the Director and the Commissioner

of Public Lands; or

(c) Termination. If unitized substances have not theretofore been discovered in paying quantities within the unit area, the parties shall join in termination of the unit agreement in accordance with its provisions.

If none of the foregoing alternatives is available, unit operator shall drill the required well for the account of all the parties, each of whom shall bear their percentage of all costs incurred therein which is equal to its cost burden in subsequent wells as specified in Column 7, Page 3, of Exhibit "A".

ARTICLE VI

RENTALS AND SHUT-IN WELL PAYMENTS

6.1 Rentals. Each party holding the record title to an oil and gas lease subject to this agreement shall, before the due date, pay all rentals which may become due under the lease or leases contributed by it, and each party paying such rentals or royalties shall, within 10 days after the payment thereof but at least 10 days prior to the due date, notify the operator of such payment. Operator shall furnish similar information as to its leases to non-operators upon request. The financial burden of paying rentals shall fall entirely upon the party holding the record title and required to make the particular payment. Rental payments shall not be charged to the joint account, but any other party hereto, other than the record title holder, having an interest therein, shall reimburse the party paying such rentals for such party's proportionate part thereof. In the event of failure to make proper payment of any rental through mistake or oversight, where such payment is required to continue a lease

in force (it being understood that any such failure shall not be regarded as a title failure within the meaning of any other provisions of this agreement), there shall be no monetary liability on the part of the party charged with the responsibility of making such payment, but such party shall make a bona fide effort to secure (at its sole cost and expense) a new lease covering the same interest and in the event of failure to secure a new lease within 120 days the interests of the parties shall be revised so that the party or parties charged with the responsibility of bearing the particular payment will not be credited with the ownership of their lease which was lost because of failure properly to make a required rental payment.

6.2 Shut-in Well Payments: If any well is completed on the unit area pursuant to the unit agreement as a gas well and is shut-in due to the lack of a market or for any other reason, operator shall notify all of the parties hereto thereof and shall pay any shut-in royalties which may become due and payable on account of such well and charge the same to the joint account of the parties hereto in proportion to their respective rights to participate in the production from such well pursuant to the provisions of this agreement.

ARTICLE VII

RIGHT TO TAKE PRODUCTION IN KIND

7.1 Each party shall have the right to take in kind or separately dispose of its proportionate share of all oil and gas produced from the area exclusive of production which may be used in development and producing operations in preparing and treating oil for marketing purposes and production unavoidably

lost. Each party shall pay or deliver, or cause to be paid or delivered, all royalties, overriding royalties or other payments due on its share of such production and shall hold the other parties free from any liability therefor. Any extra expenditure incurred in taking in kind or separate disposition by any party of its proportionate share of the production shall be borne by such party.

Each party shall execute such division orders and contracts as may be required for the sale of its interest in production from the unit area, and shall be entitled to receive payment direct from the purchaser or purchasers thereof for its share of all production.

In the event any party should fail to make the arrangements necessary to take in kind or separately dispose of its proportionate part of unitized substances produced from the unit area, operator shall have the right, subject to revocation at will by the party owning it, but not the obligation, to purchase such unitized substances or to sell the same to others for the time being at not less than the market price prevailing in the area, which shall in no event be less than the price which operator receives for its portion of the unitized substances produced from the unit area; provided, however, if operator fails to exercise such right, any other party hereto shall have the right to do so. Any such purchase or sale by operator or any other party, as provided herein, shall always be subject to the right of the owner of the production to exercise at any time its right to take in kind or separately dispose of its share of unitized substances not previously delivered to a purchaser. Notwithstanding the foregoing, operator or any other party shall not make a sale into

interstate commerce of any party's share of gas production without first receiving approval of the party owning the same.

ARTICLE VIII

CHANGE OF OWNERSHIP

8.1 Maintenance of Unit Ownership: If any party creates the necessity for separate measurement facilities hereunder by transfer, mortgage or other encumbrance, except those set forth in Article V, such party shall alone bear the cost of purchase, installation and operation of such separate measurement facilities.

Every sale, encumbrance, transfer or other disposition made by any party shall be made expressly subject to this agreement and shall be made without prejudice to the rights of the other parties.

If at any time the interest of any party as set forth in Column 8, Page 3, of Exhibit "A" is divided among and owned by four or more co-owners, operator may, at its discretion, require such co-owners to appoint a single trustee or agent with full authority to receive notices, approve expenditures, receive billings for and approve and pay such party's share of the joint expense, and to deal generally with and with power to bind the co-owners of such party's interest within the scope of the operations embraced in this agreement; however, all such co-owners shall enter into and execute all contracts or agreements for the disposition of their respective shares of the oil and gas produced from the unit area and they shall have the right to receive, separately, payment of sale proceeds thereof.

Should a sale be made by operator of its rights and interests, the other parties shall have the right within sixty (60) days after the date of such sale, by majority vote in interest, to select a new operator. If a new operator is not so selected, the transferee of the present operator shall assume the duties of and act as operator. In either case, the retiring operator shall continue to serve as operator, and discharge its duties in that capacity under this agreement, until its successor operator is selected and begins to function, but the present operator shall not be obligated to continue the performance of its duties for more than 120 days after the sale of its rights and interests has been completed.

8.2 Termination of Interest and Withdrawal of Party: Should any party at any time desire to surrender any lease committed to the unit agreement and the other parties should not agree thereto, the party desiring to surrender shall assign, without express or implied warranty of title, subject to the approval of the Bureau of Land Management as to federal lands and the Commissioner of Public Lands as to state lands, all of such party's interest in such lease to the other parties hereto in proportion to the interests then severally held by them on an acreage basis in the unit area. If all of the parties are not willing to accept the assignment of such interest, the assignment shall be made to those willing to accept such interest in the proportions that their respective interests bear to the aggregate of their interests in the unit area on an acreage basis. Such assignment shall be free and clear of all liens and encumbrances except all lease burdens existing as of the effective date of the unit agreement, and upon delivery thereof the assigning party shall be relieved of all further obligations with respect to the lease or leases so assigned.

Likewise, if any party hereto so desires it may withdraw from this agreement by assigning, without warranty either express or implied, all of such party's interests committed to the unit agreement to the other parties hereto, or if all of said parties are not willing to accept the assignment, to those who are willing to accept such assignment upon the same terms and conditions as hereinabove set forth.

All assignments made pursuant to the provisions of this Section 8.2 shall include all of the assignor's interest in all wells, casing, material, equipment, fixtures and other personal property belonging to the joint account. Such assignment shall not relieve assignor from any obligation or liability accruing or incurred prior to the date thereof; provided, however, the assignees shall pay the assignor for its interest in such casing, material, equipment, fixtures and other personal property owned by the joint account on the basis of the salvage value thereof determined in accordance with the Accounting Prodedure attached hereto as Exhibit "B".

8.3 Subsequent Joinder: Prior to commencement of operations under the unit agreement, all owners of working interests in the unit area who have joined in the unit agreement shall be privileged to join in this agreement by subscribing to the unit agreement and this agreement. After commencement of operations under the unit agreement, however, subsequent joinder in the unit agreement and this agreement by any party owning a working interest in the unit area shall be on such reasonable terms and conditions as the parties who are then committed to the unit agreement and this agreement may require in view of the circumstances existing at the time such subsequent joinder is sought.

ARTICLE IX

MISCELLANEOUS PROVISIONS

9.1 Contributions Toward Drilling: Any contribution, either in money or property interest, toward the drilling of any well drilled on the unit area pursuant to the provisions of this agreement, other than the initial test well or the second test well in the event the participating parties should elect to drill the same in accordance with the provisions of Section 5.6 hereof, shall be shared by the parties hereto in proportion to their participating interests in such well; provided, however, participation in acreage contributions shall be optional with the respective parties.

9.2 Assignments of Partial Interests: Notwithstanding any of the provisions contained herein to the contrary, in executing any assignments pursuant to Sections 5.1, 5.7 and 8.2 hereof, where the interest to be assigned is only as to certain producing formations where state or federal lands are involved, and where such assignments are subject to approval by the Commissioner of Public Lands or the Director of the Bureau of Land Management, the interest to be assigned shall be conveyed by appropriate operating agreements or by any other valid instrument that will carry out the intention of such provision or provisions.

9.3 Provisions Conformed with Laws and Regulations: All of the provisions of this agreement are hereby expressly made subject to all valid, enforceable and applicable federal or state laws, orders, rules and regulations, and in the event this contract or any provisions hereof are found to be inconsistent with or contrary to any such law, order, rule or regulations, the latter shall be deemed to control, and this contract shall be regarded as modified accordingly and as so modified shall continue in full force and effect.

9.4 Notices: All notices authorized or required by any of the provisions of this agreement shall, unless otherwise specifically provided, be given in writing by United States mail or Western Union telegram, postage or charges prepaid, and addressed to the party to whom the notice is given at the addresses shown opposite the signatures of the respective parties hereto. The originating notice to be given under any provision hereof shall be deemed given only when received by the party to whom such notice is directed and the time for such party to give any notice in response thereto shall run from the date the originating notice is received. The second or any responsive notice shall be deemed given when deposited in the United States mail or with the Western Union Telegraph Company, with postage or charges prepaid. Each party shall havethe right to change its address at any time, and from time to time, by giving written notice thereof to all other parties.

9.5 Liability of Parties: The liability of the parties shall be several, not joint or collective. Each party shall be responsible only for its obligations, and shall be liable only for its proportionate share of the costs of developing and operating the unit area. Accordingly, the lien granted by each party to operator in Section 4.7 is given to secure only the debts of each severally. It is not the intention of the parties to create, nor shall this agreement be construed as creating, a mining or other partnership or association, or to render them liable as partners.

9.6 Income Tax Election, Subchapter K, of Chapter 1, Subtitle A, Internal Revenue Code: Notwithstanding any provisions herein that the rights and liabilities of the parties hereto are several and not joint or collective, or that this agreement and the operations hereunder shall not constitute a partnership, if

for federal income tax purposes this agreement and the operations hereunder are regarded as a partnership, then each of the parties hereto hereby elects that it be excluded from the application of all of the provisions of Subchapter K, Chapter 1, Subtitle A of the Internal Revenue Code of 1954, as permitted and authorized by Section 761 of said Code and the regulations promulgated thereunder. Operator is hereby authorized and directed to execute such evidence of this election as may be required by the Secretary of the Treasury of the United States or the Federal Internal Revenue Service, including specifically, but not by way of limitation, all of the returns, statements and data required by the Code and applicable regulations. Should there be any requirement that each party hereto further evidence this election, each party hereto agrees to execute such documents and furnish such other evidence as may be required by the Federal Internal Revenue Service as may be necessary to evidence this election. Each party hereto further agrees not to give any notices or take any other action inconsistent with the election made hereby. If any present or future income tax laws of the State of New Mexico, or any future income tax law of the United States, contain, or shall hereafter contain, provisions similar to those contained in Subchapter K, Chapter 1, Subtitle A, of the Internal Revenue Code of 1954, under which an election similar to that provided in Section 761 of said Subchapter K is permitted, each of the parties hereto hereby makes such election or agrees to make such election as may be permitted by such laws. In making this election, each of the parties hereto hereby states that the income derived by it from the operations under this agreement can be adequately determined without the computation of partnership taxable income.

9.7 Force Majeure: If any party is rendered unable,

wholly or in part, by force majeure to carry out its obligations under this agreement, other than the obligation to make money payments, that party shall give to all other parties prompt written notice of the force majeure with reasonably full particulars concerning it; thereupon, the obligations of the party fiving the notice, so far as they are affected by the force majeure, shall be suspended during, but no longer than, the continuance of the force majeure. The affected party shall use all possible diligence to remove the force majeure as quickly as possible.

The requirement that any force majeure shall be remedied with all reasonable dispatch shall not require the settlement of strikes, lockouts, or other labor difficulties by the party involved, contrary to its wishes; how all such difficulties shall be handled shall be entirely within the discretion of the party concerned.

The term "force majeure" as here employed shall mean an act of God, strike, lockout or other industrial distrubance, act of the public enemy, war, blockade, public riot, lightning, fire, store, flood, explosion, governmental restraint, unavailability of equipment, and any other case, whether of the kind specifically enumerated above or otherwise, which is not reasonably within the control of the party claiming suspension.

9.8 Nondiscrimination: In connection with the performance of work under this agreement, the operator agrees to comply with all of the provisions of Section 202 (1) to (7) inclusive of Executive Order 11246 (30 F.R. 12319), which are hereby incorporated by reference in this agreement.

9.9 Effective Date and Term: This agreement shall become effective as of the effective date of the unit agreement and shall remain in full force and effect during the term of said unit agree-

ment and any and all extensions or renewals thereof, and in the event of the termination of the unit agreement for any reason, this agreement shall continue in full force and effect as to all wells which have not been plugged and abandoned as of the time of the termination of the unit agreement, and the rights and interests of the parties hereto in such wells and their participation in the production therefrom and in the cost of the operation thereof shall be governed by the provisions hereof and this agreement with respect thereto shall remain in full force and effect so long as any such well is capable of producing oil or gas in paying quantities and thereafter until all accounts hereunder are closed.

9.10 Unleased Tract. If any of the parties hereto acquire an oil and gas lease on Tract 18 as described in the unit agreement, there shall be no right among the parties hereto to share in such acquisition, it being the intention that any owners of a lease on such tract will be governed by the provisions of Section 8.3 hereof.

9.11 Counterparts. This agreement may be executed in any number of counterparts, no one of which needs to be executed by all other working interest owners, or may be ratified or consented to by separate instrument in writing specifically referring hereto, but shall not be effective until all parties hereto have executed either the original or a counterpart hereof or joined by consent and ratification.

IN WITNESS WHEREOF, this agreement is executed by the undersigned parties hereto as of the day and year first hereinabove written.

ROBERTS, KOCH & CARTWRIGHT

Date: 8/21/73

Address:

[illegible] Bldg. of Southwest
Midland, Texas 79701

Ross D. Roberts

Charles E. Koch

Jack C. Cartwright
Unit Operator and Working
Interest Operator

WORKING INTEREST OWNERS

ATTEST:

_____

Date: _____

CITIES SERVICE OIL COMPANY

By _____

Address: _____

_____

ATTEST:

_____

Date: 2nd August, 1973

PETROLEUM, INC.

By _____

Address: 500 Colorado State Bank Bldg.
Denver, Co. 80202

ATTEST:

_____

Date: _____

AZTEC OIL AND GAS COMPANY

By _____

Address: _____

_____

ATTEST:

_____

Date: _____

UNION OIL COMPANY OF CALIFORNIA

By _____

Address: _____

_____

STATE OF _____)
: ss
COUNTY OF _____)

The foregoing instrument was acknowledged before me this _____ day of _____, 1973 by _____, _____, of CITIES SERVICE OIL COMPANY, a Delaware corporation, on behalf of said corporation.

My Commission Expires:

_____

_____
Notary Public

STATE OF Colorado)
City and
: ss
COUNTY OF Denver)

The foregoing instrument was acknowledged before me this 27th day of August, 1973 by Robert D. Cowdery, Vice-President, of PETROLEUM, INC., a Kansas corporation, on behalf of said corporation.

My Commission Expires:

July 12, 1977.

_____
Notary Public

WORKING INTEREST OWNERS

ATTEST:

_____

Date: _____

CITIES SERVICE OIL COMPANY

By _____

Address: _____

_____

ATTEST:

_____

Date: _____

PETROLEUM, INC.

By _____

Address: _____

_____

ATTEST:

Wanda M. Sanders
ASSISTANT SECRETARY

Date: September 13, 1973

AZTEC OIL AND GAS COMPANY

By Kenneth A. Swanson
Vice President

Address: 2000 First Nat'l Bank Bldg.
Dallas, Texas 75202

ATTEST:

_____

Date: _____

UNION OIL COMPANY OF CALIFORNIA

By _____

Address: _____

_____

STATE OF _____)
: ss
COUNTY OF _____)

The foregoing instrument was acknowledged before me this _____ day of _____, 1973 by _____, _____, of CITIES SERVICE OIL COMPANY, a Delaware corporation, on behalf of said corporation.

My Commission Expires:

_____

_____
Notary Public

STATE OF _____)
: ss
COUNTY OF _____)

The foregoing instrument was acknowledged before me this _____ day of _____, 1973 by _____, _____, of PETROLEUM, INC., a corporation, on behalf of said corporation.

My Commission Expires:

_____

_____
Notary Public

WORKING INTEREST OWNERS

~~ATTEST:~~

_____

Date: _____

CITIES SERVICE OIL COMPANY

By _____
Mark F. Payton Attorney-in-Fact

Address: P. O. Box 300

Tulsa, Oklahoma 74102

ATTEST:

_____

Date: _____

PETROLEUM, INC.

By _____

Address: _____

_____

ATTEST:

_____

Date: _____

AZTEC OIL AND GAS COMPANY

By _____

Address: _____

_____

ATTEST:

_____

Date: _____

UNION OIL COMPANY OF CALIFORNIA

By _____

Address: _____

_____

STATE OF Oklahoma)
: ss
COUNTY OF TULSA)

The foregoing instrument was acknowledged before me this 30th day of August, 1973 by Mark F. Payton, Attorney-in-Fact, of CITIES SERVICE OIL COMPANY, a Delaware corporation, on behalf of said corporation.

My Commission Expires:
JUL 25 1976

_____

Evelyn M. Schultz
Notary Public
Evelyn M. Schultz

STATE OF _____)
: ss
COUNTY OF _____)

The foregoing instrument was acknowledged before me this _____ day of _____, 1973 by _____, _____, of PETROLEUM, INC., a corporation, on behalf of said corporation.

My Commission Expires:

_____

_____
Notary Public

WORKING INTEREST OWNERS

ATTEST:

_____

Date: _____

CITIES SERVICE OIL COMPANY

By _____

Address: _____

_____

ATTEST:

_____

Date: _____

PETROLEUM, INC.

By _____

Address: _____

_____

ATTEST:

_____

Date: _____

AZTEC OIL AND GAS COMPANY

By _____

Address: _____

_____

~~ATTEST:~~

_____

Date: August 24, 1973

UNION OIL COMPANY OF CALIFORNIA

By _____
Attorney-in-Fact
SAMUEL C. TERRY

Address: P. O. Box 3100

Midland, Texas 79701

STATE OF _____)
: ss
COUNTY OF _____)

The foregoing instrument was acknowledged before me this _____ day of _____, 1973 by _____, _____, of CITIES SERVICE OIL COMPANY, a Delaware corporation, on behalf of said corporation.

My Commission Expires:

_____

_____
Notary Public

STATE OF _____)
: ss
COUNTY OF _____)

The foregoing instrument was acknowledged before me this _____ day of _____, 1973 by _____, _____, of PETROLEUM, INC., a corporation, on behalf of said corporation.

My Commission Expires:

_____

_____
Notary Public

STATE OF _____)
: ss
COUNTY OF _____)

The foregoing instrument was acknowledged before me this _____ day of _____, 1973 by _____, _____, of AZTEC OIL AND GAS COMPANY, a corporation, on behalf of said corporation.

My Commission Expires:

_____

_____
Notary Public

STATE OF _____)
: ss
COUNTY OF _____)

The foregoing instrument was acknowledged before me this _____ day of _____, 1973 by _____, _____, of UNION OIL COMPANY OF CALIFORNIA, a corporation, on behalf of said corporation.

My Commission Expires:

_____

_____
Notary Public

STATE OF TEXAS X

COUNTY OF MIDLAND X

The foregoing instrument was acknowledged before me this 21st day of August, 1973 by Ross D. Roberts, Charles E. Koch, and Jack C. Cartwright, partners, of ROBERTS, KOCH & CARTWRIGHT, a partnership.

Carolyn Hartzog
Notary Public

My Commission Expires:

6-1-75

STATE OF Texas)
: ss
COUNTY OF Dallas)

The foregoing instrument was acknowledged before me this 13th day of September, 1973 by Kenneth A. Swanson, Vice President, of AZTEC OIL AND GAS COMPANY, a corporation, on behalf of said corporation.

My Commission Expires:

June 1, 1975

Peggy Stepp
Notary Public

PEGGY STEPP
NOTARY PUBLIC, DALLAS COUNTY, TEXAS
MY COMMISSION EXPIRES JUNE 1, 1975

STATE OF _____)
: ss
COUNTY OF _____)

The foregoing instrument was acknowledged before me this _____ day of _____, 1973 by _____, _____, of UNION OIL COMPANY OF CALIFORNIA, a corporation, on behalf of said corporation.

My Commission Expires:

_____

_____
Notary Public

STATE OF TEXAS)(

COUNTY OF MIDLAND)(

The foregoing instrument was acknowledged before me this _____ day of _____, 1973 by _____, Partner on behalf of ROBERTS, KOCH & CARTWRIGHT, a partnership.

_____
Notary Public

My Commission Expires:

_____

STATE OF _____)
: ss
COUNTY OF _____)

The foregoing instrument was acknowledged before me this _____ day of _____, 1973 by _____, _____, of AZTEC OIL AND GAS COMPANY, a corporation, on behalf of said corporation.

My Commission Expires:

_____

_____
Notary Public

STATE OF TEXAS)
: ss
COUNTY OF MIDLAND)

The foregoing instrument was acknowledged before me this 24th day of August, 1973 by SAMUEL C. TERRY, Attorney-in-Fact, of UNION OIL COMPANY OF CALIFORNIA, a corporation, on behalf of said corporation.

My Commission Expires:

June 1, 1975

Alice Monroe
Notary Public
Alice Monroe

STATE OF TEXAS)

COUNTY OF MIDLAND)

The foregoing instrument was acknowledged before me this _____ day of _____, 1973 by _____, Partner on behalf of ROBERTS, KOCH & CARTWRIGHT, a partnership.

_____
Notary Public

My Commission Expires:

_____

EXHIBIT "A"
TO
UNIT OPERATING AGREEMENT
DEER CANYON UNIT - EDDY COUNTY, NEW MEXICO

Working Interest Owners	Tract Nos.	Committed Acres and Percent		Royalty and Basic	Percent Excess	Net Working Interest Percent	Acres
Petroleum, Inc.	3	1481.37	15.14623	12.5	None	87.5	1296.20
Cities Service Oil Company	8	640.00		12.5	5%	82.5	528.00
	10	807.48		12.5	4%	83.5	674.25
	11	200.00		12.5	3%	84.5	169.00
	13	1000.00		12.5	3%	84.5	845.00
	16	160.00		12.5	None	87.5	140.00
		2807.48	28.70502				2356.25
Aztec Oil & Gas Company	15	729.20	7.45569	12.5	None	87.5	638.05
Union Oil Company of California	17	640.00	6.54367	12.5	None	87.5	560.00
Roberts, Koch & Cartwright	2	1080.00		12.5	3%	84.5	912.60
	4	371.28		12.5	5%	82.5	306.31
	5	1570.76		12.5	5%	82.5	1295.88
	6	40.00		12.5	3%	84.5	33.80
	7	40.00		12.5	3%	84.5	33.80
	9	700.36		12.5	5%	82.5	577.80
	12	40.00		12.5	5%	82.5	33.00
	14	280.00		12.5	5%	82.5	231.00
		4122.40	42.14939				3424.19
Total Acres Committed		9780.45					

Working Interest Owners	Tract Nos.	Committed Acres	and Percent	Royalty and Percent Basic	Excess	Net Working Interest Percent	Acres
Uncommitted Acreage							
Kerr-McGee Oil Corporation	1	760.00					
Unleased							
	18	80.00					
TOTAL ACRES IN UNIT		10620.45					8274.69

RECAPITULATION OF PARTIES AND INTERESTS IN UNIT AREA

	Col. 1	Col. 2	Col. 3	Col. 4	Col. 5	Col. 6	Col. 7	Col. 8
Working Interest Owners	Committed Acres	Percentage Committed	Net Beneficial Acres Before Drilling	Percentage Beneficial Interest Before Drilling	Percentage Cost Burden and Ownership of Equipment--Initial Test Well and Proration Unit Until Payout	Percentage Benefcial Ownership of Working Interest Production in Initial Test Well and Proration Unit Until Payout	Percentage Cost Burden and Equipment as to Unit Area Except Initial Proration Unit After Payout and as to Initial Proration Unit After Payout	Percentage Beneficial Ownership Working Interest Production as to Unit Area Except Initial Proration Unit and After Payout as to Initial Proration Unit
Cities Service Oil Company	2807.48	28.70502	2356.24581	28.47535	-0-	-0-	14.35251	14.23768
Roberts, Koch & Cartwright	4122.40	42.14939	3424.19000	41.38151	100.00000	100.00000*	71.07471	70.69074
Petroleum, Inc.	1481.37	15.14623	1296.19875	15.66464	-0-	-0-	7.57311	7.83232
Aztec Oil & Gas Company	729.20	7.45569	638.05000	7.71087	-0-	-0-	3.72784	3.85544
Union Oil Company of California	640.00	6.54367	560.00000	6.76763	-0-	-0-	3.27183	3.38382
	9780.45	100.00000	8274.68456	100.00000	100.00000	100.00000	100.00000	100.00000

* The interest of Roberts, Koch & Cartwright is subject to overriding royalties as set forth in Section 5.1 of the Unit Operating Agreement and assumes earning of interest pursuant to applicable farmout agreements from Cities Service Oil Company, Aztec Oil & Gas Company, Union Oil Company of California and Petroleum, Inc.

The contribution of acreage by Union Oil Company of California, Cities Service Oil Company, Aztec Oil & Gas Company and Petroleum, Inc. to Roberts, Koch & Cartwright applies only to depths as specified in Section 5.1 of this Operating Agreement. Therefore, the information as reflected in Columns 5, 6, 7 and 8 applies only to depths down to 100 feet below total depth as specified in said Section 5.1. However, this Operating Agreement shall apply as to deeper depths on the basis specified in Columns 1 through 4 hereof, to the end that all depths are covered by the Operating Agreement.

Kraftbilt 601 ROSS-MARTIN COMPANY TULSA, OKLAHOMA 74101

COPAS — 1968
Recommended by the Council of Petroleum Accountants Societies of North America

COPAS

EXHIBIT "B"

Attached to and made a part of Unit Operating Agreement, Deer Canyon Unit, Eddy County, New Mexico.

ACCOUNTING PROCEDURE
JOINT OPERATIONS

I. GENERAL PROVISIONS

1. Definitions

"Joint Account" shall mean the account showing the charges and credits accruing because of the Joint Operations and which are to be shared by the Parties.

"Joint Property" shall mean the real and personal property subject to the agreement to which this Accounting Procedure is attached.

"Joint Operations" shall mean all operations necessary or proper for the development, operation, protection and maintenance of the Joint Property.

"Operator" shall mean the party designated to conduct the Joint Operations.

"Non-Operators" shall mean the parties to this agreement other than the Operator.

"Parties" shall mean Operator and Non-Operators.

"Material" shall mean personal property, equipment or supplies acquired or held for use on the Joint Property.

"Controllable Material" shall be defined as set forth under the subparagraph selected below:

A. [X] Material which at the time is so classified in the Material Classification Manual as most recently recommended by the Council of Petroleum Accountants Societies of North America.

B. [ ] Material which is ordinarily so classified and controlled by Operator in the conduct of its operations. List shall be furnished Non-Operators upon request.

2. Statements and Billings

Operator shall bill Non-Operators on or before the last day of each month for their proportionate share of costs and expenses for the preceding month. Such bills will be accompanied by statements reflecting the total charges and credits as set forth under the subparagraph selected below:

A. [ ] Statement in detail of all charges and credits to the Joint Account.

B. [ ] Statement of all charges and credits to the Joint Account, summarized by appropriate classifications indicative of the nature thereof.

C. [X] Statement of all charges and credits to the Joint Account, summarized by appropriate classification indicative of the nature thereof, except that items of Controllable Material and unusual charges and credits shall be detailed.

3. Advances and Payments by Non-Operators

Unless otherwise provided for in the agreement, the Operator may require the Non-Operators to advance their share of estimated cash outlay for the succeeding month's operation. Operator shall adjust each monthly billing to reflect advances received from the Non-Operators.

Each Non-Operator shall pay its proportion of all bills within fifteen (15) days after receipt. If payment is not made within such time, the unpaid balance shall bear interest monthly at the rate of ten per cent (10%) per annum or the maximum contract rate permitted by the applicable usury laws in the state in which the Joint Property is located, whichever is the lesser.

4. Adjustments

Payment of any such bills shall not prejudice the right of any Non-Operator to protest or question the correctness thereof; provided however, all bills and statements rendered to Non-Operators by Operator during any calendar year shall conclusively be presumed to be true and correct after twenty-four (24) months following the end of any such calendar year, unless within the said twenty-four (24) month period a Non-Operator takes written exception thereto and makes claim on Operator for adjustment. No adjustment favorable to Operator shall be made unless it is made within the same prescribed period. The provisions of this paragraph shall not prevent adjustments resulting from a physical inventory of the Joint Property as provided for in Section VII.

5. Audits

A Non-Operator, upon notice in writing to Operator and all other Non-Operators, shall have the right to audit Operator's accounts and records relating to the accounting hereunder for any calendar year within the twenty-four (24) month period following the end of such calendar year; provided however, the making of an audit shall not extend the time for the taking of written exception to and the adjustments of accounts as provided for in Paragraph 4 of this Section I. Where there are two or more Non-Operators, the Non-Operators shall make every reasonable effort to conduct joint or simultaneous audits in a manner which will result in a minimum of inconvenience to the Operator. Operator shall bear no portion of the Non-Operators' audit cost incurred under this paragraph unless agreed to by the Operator.

6. Approval by Non-Operators

Where an approval or other agreement of Non-Operators is expressly required under Paragraphs 5A, 5B, ~~6A and 6B~~ of this Section I, Section V, Section VI, and Paragraph 4 of Section VII, of this Accounting Procedure and if the agreement to which this Accounting Procedure is attached contains no contrary provisions in regard thereto, the Operator shall notify all Non-Operators and the agreement or approval of a majority in interest of the Non-Operators shall be controlling on all Non-Operators.

II. DIRECT CHARGES

Operator shall charge the Joint Account with the following items:

1. Rentals and Royalties

Lease rentals and royalties paid by Operator for the Joint Operations.

2. Labor

A. (1) Salaries and wages of Operator's employees directly employed on the Joint Property in the conduct of Joint Operations.

(2) Salaries of first-level supervisors in the field if such charges are excluded from overhead rates in Option A of Section III.

(3) Salaries and wages of technical employees temporarily assigned to and directly employed on the Joint Property if such charges are excluded from overhead rates in Option B of Section III.

~~(4) Salaries and wages of technical employees either temporarily or permanently assigned to and directly employed in the operation of the Joint Property if such charges are excluded from overhead rates in Option A of Section III~~

B. Operator's cost of holiday, vacation, sickness and disability benefits and other customary allowances paid to the employees whose salaries and wages are chargeable to the Joint Account under Paragraph 2A of this Section II and Paragraph 1A of Section III; except that in the case of those employees only a pro rata portion of whose salaries and wages are chargeable to the Joint Account under Paragraph 1A of Section III, not more than the same pro rata portion of the benefits and allowances herein provided for shall be charged to the Joint Account. Cost under this Paragraph 2B may be charged on a "when and as paid basis" or by "percentage assessment" on the amount of salaries and wages chargeable to the Joint Account under Paragraph 2A of this Section II and Paragraph 1A of Section III. If percentage assessment is used, the rate shall be based on the Operator's cost experience.

C. Expenditures or contributions made pursuant to assessments imposed by governmental authority which are applicable to Operator's labor cost of salaries and wages chargeable to the Joint Account under Paragraphs 2A and 2B of this Section II and Paragraph 1A of Section III.

D. Reasonable personal expenses of those employees whose salaries and wages are chargeable to the Joint Account under Paragraph 2A of this Section II and for which expenses the employees are reimbursed under Operator's usual practice.

3. Employee Benefits

Operator's current cost of established plans for employees' group life insurance, hospitalization, pension, retirement, stock purchase, thrift, bonus, and other benefit plans of a like nature, applicable to Operator's labor cost chargeable to the Joint Account under Paragraphs 2A and 2B of this Section II and Paragraph 1A of Section III shall be chargeable as indicated in the subparagraph selected below:

A. [ ] Operator's actual cost.

B. [X] Operator's actual cost not to exceed fifteen per cent (15%).

4. Material

Material purchased or furnished by Operator for use on the Joint Property as provided under Section IV. So far as it is reasonably practical and consistent with efficient and economical operation, only such Material shall be purchased for or transferred to the Joint Property as may be required for immediate use; and the accumulation of surplus stocks shall be avoided.

5. Transportation

Transportation of employees and Material necessary for the Joint Operations but subject to the following limitations:

A. If Material is moved to the Joint Property from the Operator's warehouse or other properties, no charge shall be made to the Joint Account for a distance greater than the distance from the nearest reliable supply store, recognized barge terminal, or railway receiving point where like material is normally available, unless agreed to by Operator and Non-Operators.

B. If surplus Material is moved to Operator's warehouse or other storage point, no charge shall be made to the Joint Account for a distance greater than the distance to the nearest reliable supply store, recognized barge terminal, or railway receiving point unless agreed to by Operators and Non-Operators. No charge shall be made to the Joint Account for moving Material to other properties belonging to Operator, unless agreed to by Operator and Non-Operators.

C. In the application of Subparagraphs A and B above, there shall be no equalization of actual gross trucking costs of $100 or less.

6. Services

A. The cost of contract services and utilities procured from outside sources other than services covered by Paragraph 8 of this Section II and Paragraph 1B of Section III. The cost of professional consultant services shall not be charged to the Joint Account unless agreed to by Operator and Non-Operators.

B. Use and service of equipment and facilities furnished by Operator as provided in Paragraph 5 of Section IV.

7. Damages and Losses to Joint Property

All costs or expenses necessary for the repair or replacement of Joint Property made necessary because of damages or losses incurred by fire, flood, storm, theft, accident, or other cause, except to the extent that the damage or loss could have been avoided through the exercise of reasonable diligence on the part of Operator. Operator shall furnish Non-Operators written notice of damages or losses incurred as soon as practicable after a report thereof has been received by Operator.

8. Legal Expense

All costs and expenses of handling, investigating, and settling litigation or claims arising by reason of the Joint Operations or necessary to protect or recover the Joint Property, including, but not limited to, attorney's fees, court costs, cost of investigation or procuring evidence and amounts paid in settlement or satisfaction of any such litigation or claims; provided, (a) no charge shall be made for the services of Operator's legal staff or other regularly employed personnel (such services being considered to be Administrative Overhead under Section III), unless agreed to by Operator and Non-Operators, and (b) no charge shall be made for the fees and expenses of outside attorneys unless the employment of such attorneys is agreed to by Operator and Non-Operators.

9. Taxes

All taxes of every kind and nature assessed or levied upon or in connection with the Joint Property, the operation thereof, or the production therefrom, and which taxes have been paid by the Operator for the benefit of the Parties.

10. Insurance

Net premiums paid for insurance required to be carried on the Joint Property for the protection of the Parties.

In the event Joint Operations are conducted in a state in which Operator may act as self-insurer for Workmen's Compensation and/or Employers Liability under the respective state's laws, Operator may, at its election, include the risk under its self-insurance program and in that event, Operator shall include a charge therefor on the following basis:

.....

.....

.....

11. Other Expenditures

Any other expenditure not covered or dealt with in the foregoing provisions of this Section II, or in Section III, and which is incurred by the Operator for the necessary and proper conduct of the Joint Operations.

III. INDIRECT CHARGES

Operator may charge the Joint Account for indirect costs either by use of an allocation of district expense items plus the rate for administrative overhead, and plus the warehousing charges, all as provided for in Paragraph 1 of this Section III or by combining all three of said items under the rates provided for in Paragraph 2 or 3 of this Section III, as indicated next below:

OPERATOR SHALL CHARGE INDIRECT COSTS TO THE JOINT ACCOUNT UNDER THE TERMS OF:

[ ] Paragraph 1. (District Expense, Administrative Overhead and Warehousing)
[X] Paragraph 2. (Combined Rates - Well Basis)
[ ] Paragraph 3. (Combined Rates - Percentage Basis)

The cost and expense of services from outside sources in connection with matters of taxation, traffic, accounting or matters before or involving governmental agencies shall be considered as included in the overhead rates provided for in the above selected Paragraph of this Section III unless such cost and expense are agreed to by Operator and Non-Operators as a direct charge to the Joint Account.

THE OVERHEAD RATES PROVIDED FOR IN ANY OF THE PARAGRAPHS SELECTED ABOVE

A. [X] shall [ ] shall not include salaries and personal expenses of first-level supervisors in the field.

B. [X] shall [ ] shall not include salaries, wages and personal expenses of technical employees temporarily assigned to and directly employed on the Joint Property.

~~[X] shall [ ] shall not include salaries, wages and personal expenses of technical employees temporarily assigned to and directly employed on the Joint Property.~~

1. District Expense, Administrative Overhead and Warehousing

A. District Expense

Operator shall charge the Joint Account with a pro rata portion of the salaries, wages and expenses of Operator's production superintendent and other employees serving the Joint Property and other properties of the Operator in the same operating area, whose time is not allocated directly to the properties, and a pro rata portion of the cost of maintaining and operating a production office known as Operator's ..... office located at or near ..... (or a comparable office if location changed); and necessary sub-offices (if any), maintained for the convenience of the above-described office, and all necessary camps, including housing facilities for employees if required, used in connection with the operations of the Joint Property and other properties in the same operating area. The expense of, less any revenue from, such facilities may, at the option of Operator, include depreciation of investment or a fair monthly rental in lieu of depreciation. Such charges shall be apportioned to all properties served on some equitable basis consistent with Operator's accounting practice.

B. Administrative Overhead

Operator shall charge administrative overhead to the Joint Account at the following rates, which charge shall be in lieu of the cost and expense of all offices of the Operator not covered by Paragraph 1A of this Section III, including salaries, wages and expenses of personnel assigned to such offices. Such charge shall be in addition to the salaries, wages and expenses of employees of Operator authorized to be charged direct as provided in Paragraphs 2 and 8 of Section II. Such charge shall be made on the basis indicated below, either (1) well basis or (2) percentage basis, at the rates shown thereunder.

(1) [ ] Well Basis

RATE PER WELL PER MONTH

	DRILLING WELL RATE (Use Total Depth)	PRODUCING WELL RATE (Use Current Producing Depth)		
Well Depth	Each Well	First Five	Next Five	All Wells Over Ten

(2) [ ] Percentage Basis

PERCENTAGE BASIS

Development:

..... Percent (%) of the cost of development of the Joint Property exclusive of costs provided under Paragraph 8 of Section II and all salvage credits.

Operating:

..... Percent (%) of the cost of operating the Joint Property exclusive of costs provided under Paragraphs 1 and 8 of Section II, all salvage credits, the value of injected substances purchased for secondary recovery and all taxes and assessments which are levied, assessed and paid upon the mineral interest in and to the Joint Property.

C. Operator's Warehouse Operating and Maintenance Expense

[ ] Included in district expense

[X] No charge either direct or indirect

[ ] Percentage basis (describe fully) .....

.....

.....

2. Combined Rates - Well Basis

Operator shall charge the Joint Account for the services covered by Paragraph 1 of this Section III on the basis indicated below:

RATE PER WELL PER MONTH

Well Depth	DRILLING WELL RATE (Use Total Depth) Each Well	All Wells	PRODUCING WELL RATE (Use Current Producing Depth)	
All depths	1460.00	205.00		

3. Combined Rates - Percentage Basis

Operator shall charge the Joint Account for the services covered by Paragraph 1 of this Section III on the basis indicated below:

PERCENTAGE BASIS

A. Development:

..... Percent (%) of the cost of development of the Joint Property exclusive of costs provided under Paragraph 8 of Section II and all salvage credits.

B. Operating:

..... Percent (%) of the cost of operating the Joint Property exclusive of costs provided under Paragraphs 1 and 8 of Section II, all salvage credits, the value of injected substances purchased for secondary recovery and all taxes and assessments which are levied, assessed and paid upon the mineral interest in and to the Joint Property.

4. Application of Administrative Overhead or Combined Rates - Well Basis

The following limitations, instructions and charges shall apply in the application of the rates as provided under either Paragraph 1B (1) or Paragraph 2 of this Section III.

A. Charges for drilling wells shall begin on the date each well is spudded and terminate on the date the drilling or completion rig is released, whichever is later, except that no charge shall be made during the suspension of drilling operations for fifteen (15) or more consecutive days.

B. The status of wells shall be as follows:

(1) Producing gas wells, injection wells for recovery operations, water supply wells utilized for waterflooding operations and salt water disposal wells shall be considered the same as producing oil wells.

(2) Wells permanently shut down but on which plugging operations are deferred shall be dropped from the well schedule at the time the shutdown is effected. Any well being plugged or produced during any portion of the month shall be considered as a producing well for the entire month.

(3) Wells being plugged back, drilled deeper, converted to a source or input well, or which are undergoing any type of workover that requires the use of a drilling rig or workover rig capable of drilling shall be considered the same as drilling wells.

(4) Temporarily shut-down wells, which are not produced or worked upon for a period of a full calendar month, shall not be included in the well schedule, provided however, wells shut in by governmental regulatory body shall be included in the well schedule only in the event the allowable production is transferred to some other well or wells on the Joint Property. In the event of a unit allowable, shut-in wells shall be counted in determining the charge hereunder for such month if said wells contribute allowable production that is actually produced during such month from one or more unit wells as a result of allowable transfer, inclusion in the unit allowable or other circumstances, but the total shut-in well count shall be limited to the minimum number of shut-in wells necessary to provide the contributed allowable actually produced during the month.

(5) Gas wells shall be included in the well schedule if directly connected to a permanent sales outlet even though temporarily shut in due to overproduction or failure of purchaser to take the allowed production.

(6) Wells completed in multiple horizons, shall be considered as a producing well for each separately producing horizon, providing each completion is considered a separate well by governmental or other statewide regulatory authority.

C. The well rates for producing wells shall be applied to the individual leases; provided that, whenever leases covered by this agreement are operated as a unitized project, the well rates shall be applied to the total number of producing wells, irrespective of individual leases.

D. The well rates shall be adjusted as of the first day of April each year following the effective date of the agreement to which this Accounting Procedure is attached. The adjustment shall be computed by multiplying the rate currently in use by the percentage increase or decrease in the average weekly earnings of Crude Petroleum and Gas Production Workers for the last calendar year compared to the preceding calendar year as shown by "The Index of Average Weekly Earnings of Crude Petroleum and Gas Production Workers" as published by the United States Department of Labor, Bureau of Labor Statistics, or the equivalent Canadian Index as published by the Dominion Bureau of Statistics, as applicable. The adjusted rates shall be the rates currently in use, plus or minus the computed adjustment.

5. Application of Administrative Overhead or Combined Rates - Percentage Basis

For the purpose of determining charges on a Percentage Basis under Paragraph 1B (2) or Paragraph 3 of this Section III, Development shall include all costs in connection with drilling, redrilling, deepening or any remedial operations on any or all wells involving the use of drilling crew and equipment; also, preliminary expenditures necessary in preparation for drilling and expenditures incurred in abandoning when well is not completed as a producer; and original cost of construction or installation of fixed assets, the expansion of fixed assets and any other project clearly discernible as a fixed asset, except Major Construction as defined in Paragraph 6 of this Section III. All other costs shall be considered as Operating.

6. Major Construction Overhead

For the construction of compressor plants, water stations, secondary recovery systems, drilling and production platforms, salt water disposal facilities, and other such projects, as distinguished from the more usual drilling

and producing operations, Operator in addition to the Administrative Overhead or Combined Rates provided for in Paragraph 1, 2 or 3 of this Secton III shall either negotiate a rate prior to beginning of construction or shall charge the Joint Account with an additional overhead charge as follows:

A. Total cost less than $25,000, no charge.

B. Total cost more than $25,000, but less than $100,000, 3 % of total cost.

C. Total cost of $100,000 or more, 3 % of the first $100,000 plus 2 % of all over $100,000 of total cost.

Total cost shall mean the total gross cost of any one project. For the purpose of this paragraph the component parts of a single project shall not be treated separately and the cost of drilling wells shall be excluded.

7. Amendment of Rates

The specific rates provided for in this Section III may be amended from time to time by mutual agreement between the Parties hereto if, in practice, the rates are found to be insufficient or excessive.

IV. BASIS OF CHARGES TO JOINT ACCOUNT

Subject to the further provisions of this Section IV, Operator will procure all Material and services for the Joint Property. At the Operator's option, Non-Operators may supply Material or services for the Joint Property.

1. Purchases

Material purchased and service procured shall be charged at the price paid by Operator after deduction of all discounts actually received.

2. Material furnished from Operator's Warehouse or Other Properties

A. New Material (Condition "A")

(1) Tubular goods, except line pipe, shall be priced on a maximum carload and/or barge load weight basis regardless of quantity transferred and equalized to the lowest prevailing price f.o.b. railway receiving point or recognized barge terminal nearest the Joint Property where such Material is normally available effective at date of transfer.

(2) Line pipe shall be priced at the current replacement cost effective at date of transfer from a reliable supply store nearest the Joint Property where such Material is normally available if the movement is less than 30,000 pounds. If the movement is 30,000 pounds or more, it shall be priced on the same basis as casing and tubing under Subparagraph (1) of this paragraph.

(3) When the Operator has equalized actual hauling costs as provided for in Paragraph 5 of Section II, Operator is permitted to include ten cents (10¢) per hundred-weight on all tubular goods furnished from his stocks in lieu of loading and unloading costs sustained.

(4) Other Material shall be priced at the current replacement cost of the same kind of Material, effective at date of movement and f.o.b. the supply store or railway receiving point nearest the Joint Property where Material of the same kind is normally available.

(5) The Joint Account shall not be credited with cash discounts applicable to prices provided for in this Paragraph 2 of Section IV.

B. Used Material (Condition "B" and "C")

(1) Material in sound and serviceable condition and suitable for reuse without reconditioning, shall be classified as Condition "B" and priced at seventy-five per cent (75%) of the current price of new Material.

(2) Material which is not suitable for its original function until after reconditioning shall be furnished to the Joint Account under one of the two methods defined below:

(a) Classified as Condition "B" and priced at seventy-five per cent (75%) of the current price of new Material. The cost of reconditioning shall be absorbed by the Operator of the transferring property.

(b) Classified as Condition "C" and priced at fifty per cent (50%) of current price of new Material. The cost of reconditioning also shall be charged to the receiving property, provided Condition "C" value, plus cost of reconditioning, does not exceed Condition "B" value.

(3) Obsolete Material or Material which cannot be classified as Condition "B" or Condition "C" shall be priced at a value commensurate with its use. Material no longer suitable for its original purpose but usable for some other purpose, shall be priced on a basis comparable with that of items normally used for such other purpose.

(4) Material involving erection costs shall be charged at applicable percentage of the current knocked-down price of new Material.

3. Premium Prices

Whenever Material is not readily obtainable at prices specified in Paragraphs 1 and 2 of this Section IV because of national emergencies, strikes or other unusual causes over which the Operator has no control, the Operator may charge the Joint Account for the required Material at the Operator's actual cost incurred in procuring such Material, in making it suitable for use, and in moving it to the Joint Property, provided, that notice in writing is furnished to Non-Operators of the proposed charge prior to billing Non-Operators for such Material. Each Non-Operator shall have the right, by so electing and notifying Operator within 10 days after receiving notice from Operator, to furnish in kind all or part of his share of such Material suitable for use and acceptable to Operator.

4. Warranty of Material Furnished by Operator

Operator does not warrant the Material furnished. In case of defective Material, credit shall not be passed to the Joint Account until adjustment has been received by Operator from the manufacturers or their agents.

5. Equipment and Facilities Furnished by Operator

A. Operator shall charge the Joint Account for use of equipment and facilities at rates commensurate with cost of ownership and operation. Such rates shall include cost of maintenance, repairs, other operating expense, insurance, taxes, depreciation, and interest on investment not to exceed six per cent (6%) per annum, provided such rates shall not exceed those currently prevailing in the immediate area within which the Joint Property is located. In lieu of rates based on costs of ownership and operation of equipment, other than automotive, Operator may elect to use commercial rates prevailing in the area of the Joint Property less 20%; for automotive equipment, rates as published by the Petroleum Motor Transport Association may be used. Rates for laboratory services shall not exceed those currently prevailing if performed by

outside service laboratories. Rates for trucks, tractors and well service units may include wages and expenses of operator.

B. Whenever requested, Operator shall inform Non-Operators in advance of the rates it proposes to charge.

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

V. DISPOSAL OF MATERIAL

The Operator may purchase, but shall be under no obligation to purchase, interest of Non-Operators in surplus Condition "A" or "B" Material. The disposition of surplus Controllable Material, not purchased by Operator, shall be agreed to by Operator and Non-Operators, provided Operator shall dispose of normal accumulations of junk and scrap Material either by transfer or sale from Joint Property.

1. **Material Purchased by the Operator or Non-Operators.**
   Material purchased by either the Operator or Non-Operators shall be credited by the Operator to the Joint Account for the month in which the Material is removed by the purchaser.
2. **Division in Kind**
   Division of Material in kind, if made between Operator and Non-Operators, shall be in proportion to the respective interests in such Material. The Parties will thereupon be charged individually with the value of the Material received or receivable. Proper credits shall be made by the Operator to the Joint Account.
3. **Sales to Outsiders**
   Sales to outsiders of Material from the Joint Property shall be credited by Operator to the Joint Account at the net amount collected by Operator from vendee. Any claim by vendee related to such sale shall be charged back to the Joint Account if and when paid by Operator.

VI. BASIS OF PRICING MATERIAL TRANSFERRED FROM JOINT ACCOUNT

Material purchased by either Operator or Non-Operators or divided in kind, unless agreed to by Operator and Non-Operators shall be priced on the following basis:

1. **New Price Defined**
   New price as used in this Section VI shall be the price specified for new Material in Section IV.
2. **New Material**
   New Material (Condition "A"), being new Material procured for the Joint Property but never used, at one hundred per cent (100%) of current new price (plus sales tax if any).
3. **Good Used Material**
   Good used Material (Condition "B"), being used Material in sound and serviceable condition, suitable for reuse without reconditioning:
   A. At seventy-five per cent (75%) of current new price if Material was charged to Joint Account as new, or
   B. At sixty-five per cent (65%) of current new price if Material was originally charged to the Joint Account as secondhand at seventy-five per cent (75%) of new price.
4. **Other Used Material**
   Used Material (Condition "C"), at fifty per cent (50%) of current new price, being used Material which:
   A. Is not in sound and serviceable condition but suitable for reuse after reconditioning, or
   B. Is serviceable for original function but not suitable for reconditioning.
5. **Bad-Order Material**
   Material (Condition "D"), no longer suitable for its original purpose without excessive repair cost but usable for some other purpose at a price comparable with that of items normally used for such other purpose.
6. **Junk Material**
   Junk Material (Condition "E"), being obsolete and scrap Material, at prevailing prices.
7. **Temporarily Used Material**
   When the use of Material is temporary and its service to the Joint Property does not justify the reduction in price as provided for in Paragraph 3B of this Section VI, such Material shall be priced on a basis that will leave a net charge to the Joint Account consistent with the value of the service rendered.

VII. INVENTORIES

The Operator shall maintain detailed records of Controllable Material.

1. **Periodic Inventories, Notice and Representation**
   At reasonable intervals, inventories shall be taken by Operator of the Joint Account Controllable Material. Written notice of intention to take inventory shall be given by Operator at least thirty (30) days before any inventory is to begin so that Non-Operators may be represented when any inventory is taken. Failure of Non-Operators to be represented at an inventory shall bind Non-Operators to accept the inventory taken by Operator.
2. **Reconciliation and Adjustment of Inventories**
   Reconciliation of inventory with the Joint Account shall be made, and a list of overages and shortages shall be furnished to the Non-Operators. Inventory adjustments shall be made by Operator with the Joint Account for overages and shortages, but Operator shall be held accountable to Non-Operators only for shortages due to lack of reasonable diligence.
3. **Special Inventories**
   Special Inventories may be taken whenever there is any sale or change of interest in the Joint Property. It shall be the duty of the party selling to notify all other Parties as quickly as possible after the transfer of interest takes place. In such cases, both the seller and the purchaser shall be governed by such inventory.
4. **Expense of Conducting Periodic Inventories**
   The expense of conducting periodic inventories shall not be charged to the Joint Account unless agreed to by Operator and Non-Operators.

EXHIBIT "C"
UNIT OPERATING AGREEMENT
DEER CANYON UNIT
EDDY COUNTY, NEW MEXICO

Insurance

(A) At all times while operations are being conducted hereunder, Operator shall maintain in force the following policies of insurance:

(1) Workmen's Compensation Insurance in accordance with the laws of the jurisdiction in which work is performed.

(2) Employers Liability coverage with limits of $100,000 for all liability arising out of one accident.

(3) Coverages (1) and (2) above shall not include Non-Operators as additional insureds but shall waive subrogation against Non-Operators.

(4) General Comprehensive Liability coverage, except automobile coverage, with minimum limits of Bodily Injury $100,000 each person and $300,000 each occurrence, including contractual liability and completed operations, but excluding blowout, pollution liability and damage to underground resources.

(5) Automobile Liability coverage, including owned, hired, and non-owned vehicles, with minimum limits the same as paragraph (4) above. No premium charges shall be billed Non-Operators in connection with Operator's fully-owned equipment--this premium not to be charged directly to the Joint Account, but will instead be covered by the flat rate charges assessed the Unit for use of such equipment.

(6) Coverages (4) and (5) above shall include Non-Operators as Additional Insureds.

(B) Such policies shall contain a waiver of territorial restrictions so that the insurance coverage thereof will apply to the proposed area of operations hereunder. The premiums for all insurance policies under this Article shall be allocated among the various Operating Joint Accounts of the parties hereto, and Operator, upon written request, shall furnish Non-Operators with evidence that such insurance is in effect prior to the commencement of any operations hereunder. No insurance other than that specified above shall be purchased for any Operating Joint Account except by mutual consent of the parties.

(C) Operator will determine the insurance requirements for contractors and subcontractors or third parties performing operations on or in connection with the Leased Lands; however, the requirements will be reviewed with Non-Operators at any time, upon request, for mutual determination of any necessary changes. When negotiating contracts hereunder, Operator shall attempt to hold contractor solely responsible for damage to contractor's equipment and shall attempt to obtain a waiver of contractor's right of recovery against parties hereto in connection with any such damage. Upon request, Operator will advise Non-Operators as to insurance requirements in use under this provision in order that Non-Operators may acquire any additional insurance for Non-Operators' account and protection not purchased by Operator for an Operating Joint Account.

FORM 610 ROCSHARTIN COMPANY TULSA, OKLAHOMA 74101

Recommended by the Council of Petroleum Accountants Societies of North America

COPAS

EXHIBIT "B"

Attached to and made a part of Unit Operating Agreement, Deer Canyon Unit, Eddy County, New Mexico.

ACCOUNTING PROCEDURE
JOINT OPERATIONS

I. GENERAL PROVISIONS

1. Definitions

"Joint Account" shall mean the account showing the charges and credits accruing because of the Joint Operations and which are to be shared by the Parties.

"Joint Property" shall mean the real and personal property subject to the agreement to which this Accounting Procedure is attached.

"Joint Operations" shall mean all operations necessary or proper for the development, operation, protection and maintenance of the Joint Property.

"Operator" shall mean the party designated to conduct the Joint Operations.

"Non-Operators" shall mean the parties to this agreement other than the Operator.

"Parties" shall mean Operator and Non-Operators.

"Material" shall mean personal property, equipment or supplies acquired or held for use on the Joint Property.

"Controllable Material" shall be defined as set forth under the subparagraph selected below:

A. [X] Material which at the time is so classified in the Material Classification Manual as most recently recommended by the Council of Petroleum Accountants Societies of North America.

B. [ ] Material which is ordinarily so classified and controlled by Operator in the conduct of its operations. List shall be furnished Non-Operators upon request.

2. Statements and Billings

Operator shall bill Non-Operators on or before the last day of each month for their proportionate share of costs and expenses for the preceding month. Such bills will be accompanied by statements reflecting the total charges and credits as set forth under the subparagraph selected below:

A. [ ] Statement in detail of all charges and credits to the Joint Account.

B. [ ] Statement of all charges and credits to the Joint Account, summarized by appropriate classifications indicative of the nature thereof.

C. [X] Statement of all charges and credits to the Joint Account, summarized by appropriate classification indicative of the nature thereof, except that items of Controllable Material and unusual charges and credits shall be detailed.

3. Advances and Payments by Non-Operators

Unless otherwise provided for in the agreement, the Operator may require the Non-Operators to advance their share of estimated cash outlay for the succeeding month's operation. Operator shall adjust each monthly billing to reflect advances received from the Non-Operators.

Each Non-Operator shall pay its proportion of all bills within fifteen (15) days after receipt. If payment is not made within such time, the unpaid balance shall bear interest monthly at the rate of ten per cent (10%) per annum or the maximum contract rate permitted by the applicable usury laws in the state in which the Joint Property is located, whichever is the lesser.

4. Adjustments

Payment of any such bills shall not prejudice the right of any Non-Operator to protest or question the correctness thereof; provided however, all bills and statements rendered to Non-Operators by Operator during any calendar year shall conclusively be presumed to be true and correct after twenty-four (24) months following the end of any such calendar year, unless within the said twenty-four (24) month period a Non-Operator takes written exception thereto and makes claim on Operator for adjustment. No adjustment favorable to Operator shall be made unless it is made within the same prescribed period. The provisions of this paragraph shall not prevent adjustments resulting from a physical inventory of the Joint Property as provided for in Section VII.

5. Audits

A Non-Operator, upon notice in writing to Operator and all other Non-Operators, shall have the right to audit Operator's accounts and records relating to the accounting hereunder for any calendar year within the twenty-four (24) month period following the end of such calendar year; provided however, the making of an audit shall not extend the time for the taking of written exception to and the adjustments of accounts as provided for in Paragraph 4 of this Section I. Where there are two or more Non-Operators, the Non-Operators shall make every reasonable effort to conduct joint or simultaneous audits in a manner which will result in a minimum of inconvenience to the Operator. Operator shall bear no portion of the Non-Operators' audit cost incurred under this paragraph unless agreed to by the Operator.

6. Approval by Non-Operators

Where an approval or other agreement of Non-Operators is expressly required under Paragraphs 5A, 5B, 5C, 5D, 5E, 5F, 5G, 5H, 5I, 5J, Section V, Section VI, and Paragraph 4 of Section VII, of this Accounting Procedure and if the agreement to which this Accounting Procedure is attached contains no contrary provisions in regard thereto, the Operator shall notify all Non-Operators and the agreement or approval of a majority in interest of the Non-Operators shall be controlling on all Non-Operators.

II. DIRECT CHARGES

Operator shall charge the Joint Account with the following items:

1. **Rentals and Royalties**

   Lease rentals and royalties paid by Operator for the Joint Operations.

2. **Labor**

   A. (1) Salaries and wages of Operator's employees directly employed on the Joint Property in the conduct of Joint Operations.

   (2) Salaries of first-level supervisors in the field if such charges are excluded from overhead rates in Option A of Section III.

   (3) Salaries and wages of technical employees temporarily assigned to and directly employed on the Joint Property if such charges are excluded from overhead rates in Option B of Section III.

   (4) Salaries and wages of Operator's employees directly employed on the Joint Property in the conduct of Joint Operations if such charges are excluded from overhead rates in Option C of Section III.

   B. Operator's cost of holiday, vacation, sickness and disability benefits and other customary allowances paid to the employees whose salaries and wages are chargeable to the Joint Account under Paragraph 2A of this Section II and Paragraph 1A of Section III; except that in the case of those employees only a pro rata portion of whose salaries and wages are chargeable to the Joint Account under Paragraph 1A of Section III, not more than the same pro rata portion of the benefits and allowances herein provided for shall be charged to the Joint Account. Cost under this Paragraph 2B may be charged on a "when and as paid basis" or by "percentage assessment" on the amount of salaries and wages chargeable to the Joint Account under Paragraph 2A of this Section II and Paragraph 1A of Section III. If percentage assessment is used, the rate shall be based on the Operator's cost experience.

   C. Expenditures or contributions made pursuant to assessments imposed by governmental authority which are applicable to Operator's labor cost of salaries and wages chargeable to the Joint Account under Paragraphs 2A and 2B of this Section II and Paragraph 1A of Section III.

   D. Reasonable personal expenses of those employees whose salaries and wages are chargeable to the Joint Account under Paragraph 2A of this Section II and for which expenses the employees are reimbursed under Operator's usual practice.

3. **Employee Benefits**

   Operator's current cost of established plans for employees' group life insurance, hospitalization, pension, retirement, stock purchase, thrift, bonus, and other benefit plans of a like nature, applicable to Operator's labor cost chargeable to the Joint Account under Paragraphs 2A and 2B of this Section II and Paragraph 1A of Section III shall be chargeable as indicated in the subparagraph selected below:

   A. [ ] Operator's actual cost.

   B. [X] Operator's actual cost not to exceed fifteen per cent (15%).

4. **Material**

   Material purchased or furnished by Operator for use on the Joint Property as provided under Section IV. So far as it is reasonably practical and consistent with efficient and economical operation, only such Material shall be purchased for or transferred to the Joint Property as may be required for immediate use; and the accumulation of surplus stocks shall be avoided.

5. **Transportation**

   Transportation of employees and Material necessary for the Joint Operations but subject to the following limitations:

   A. If Material is moved to the Joint Property from the Operator's warehouse or other properties, no charge shall be made to the Joint Account for a distance greater than the distance from the nearest reliable supply store, recognized barge terminal, or railway receiving point where like material is normally available, unless agreed to by Operator and Non-Operators.

   B. If surplus Material is moved to Operator's warehouse or other storage point, no charge shall be made to the Joint Account for a distance greater than the distance to the nearest reliable supply store, recognized barge terminal, or railway receiving point unless agreed to by Operators and Non-Operators. No charge shall be made to the Joint Account for moving Material to other properties belonging to Operator, unless agreed to by Operator and Non-Operators.

   C. In the application of Subparagraphs A and B above, there shall be no equalization of actual gross trucking costs of $100 or less.

6. **Services**

   A. The cost of contract services and utilities procured from outside sources other than services covered by Paragraph 8 of this Section II and Paragraph 1B of Section III. The cost of professional consultant services shall not be charged to the Joint Account unless agreed to by Operator and Non-Operators.

   B. Use and service of equipment and facilities furnished by Operator as provided in Paragraph 5 of Section IV.

7. **Damages and Losses to Joint Property**

   All costs or expenses necessary for the repair or replacement of Joint Property made necessary because of damages or losses incurred by fire, flood, storm, theft, accident, or other cause, except to the extent that the damage or loss could have been avoided through the exercise of reasonable diligence on the part of Operator. Operator shall furnish Non-Operators written notice of damages or losses incurred as soon as practicable after a report thereof has been received by Operator.

8. **Legal Expense**

   All costs and expenses of handling, investigating, and settling litigation or claims arising by reason of the Joint Operations or necessary to protect or recover the Joint Property, including, but not limited to, attorney's fees, court costs, cost of investigation or procuring evidence and amounts paid in settlement or satisfaction of any such litigation or claims; provided, (a) no charge shall be made for the services of Operator's legal staff or other regularly employed personnel (such services being considered to be Administrative Overhead under Section III), unless agreed to by Operator and Non-Operators, and (b) no charge shall be made for the fees and expenses of outside attorneys unless the employment of such attorneys is agreed to by Operator and Non-Operators.

9. **Taxes**

   All taxes of every kind and nature assessed or levied upon or in connection with the Joint Property, the operation thereof, or the production therefrom, and which taxes have been paid by the Operator for the benefit of the Parties.

10. Insurance

Net premiums paid for insurance required to be carried on the Joint Property for the protection of the Parties. In the event Joint Operations are conducted in a state in which Operator may act as self-insurer for Workmen's Compensation and/or Employers Liability under the respective state's laws, Operator may, at its election, include the risk under its self-insurance program and in that event, Operator shall include a charge therefor on the following basis:

.....

.....

.....

11. Other Expenditures

Any other expenditure not covered or dealt with in the foregoing provisions of this Section II, or in Section III, and which is incurred by the Operator for the necessary and proper conduct of the Joint Operations.

III. INDIRECT CHARGES

Operator may charge the Joint Account for indirect costs either by use of an allocation of district expense items plus the rate for administrative overhead, and plus the warehousing charges, all as provided for in Paragraph 1 of this Section III or by combining all three of said items under the rates provided for in Paragraph 2 or 3 of this Section III, as indicated next below:

OPERATOR SHALL CHARGE INDIRECT COSTS TO THE JOINT ACCOUNT UNDER THE TERMS OF:

[ ] Paragraph 1. (District Expense, Administrative Overhead and Warehousing)

[X] Paragraph 2. (Combined Rates - Well Basis)

[ ] Paragraph 3. (Combined Rates - Percentage Basis)

The cost and expense of services from outside sources in connection with matters of taxation, traffic, accounting or matters before or involving governmental agencies shall be considered as included in the overhead rates provided for in the above selected Paragraph of this Section III unless such cost and expense are agreed to by Operator and Non-Operators as a direct charge to the Joint Account.

THE OVERHEAD RATES PROVIDED FOR IN ANY OF THE PARAGRAPHS SELECTED ABOVE

A. [X] shall [ ] shall not include salaries and personal expenses of first-level supervisors in the field.

B. [X] shall [ ] shall not include salaries, wages and personal expenses of technical employees temporarily assigned to and directly employed on the Joint Property.

~~[X] shall [ ] shall not include salaries, wages and personal expenses of technical employees temporarily assigned to and directly employed on the Joint Property.~~

1. District Expense, Administrative Overhead and Warehousing

A. District Expense

Operator shall charge the Joint Account with a pro rata portion of the salaries, wages and expenses of Operator's production superintendent and other employees serving the Joint Property and other properties of the Operator in the same operating area, whose time is not allocated directly to the properties, and a pro rata portion of the cost of maintaining and operating a production office known as Operator's ..... office located at or near ..... (or a comparable office if location changed); and necessary sub-offices (if any), maintained for the convenience of the above-described office, and all necessary camps, including housing facilities for employees if required, used in connection with the operations of the Joint Property and other properties in the same operating area. The expense of, less any revenue from, such facilities may, at the option of Operator, include depreciation of investment or a fair monthly rental in lieu of depreciation. Such charges shall be apportioned to all properties served on some equitable basis consistent with Operator's accounting practice.

B. Administrative Overhead

Operator shall charge administrative overhead to the Joint Account at the following rates, which charge shall be in lieu of the cost and expense of all offices of the Operator not covered by Paragraph 1A of this Section III, including salaries, wages and expenses of personnel assigned to such offices. Such charge shall be in addition to the salaries, wages and expenses of employees of Operator authorized to be charged direct as provided in Paragraphs 2 and 8 of Section II. Such charge shall be made on the basis indicated below, either (1) well basis or (2) percentage basis, at the rates shown thereunder.

(1) [ ] Well Basis

RATE PER WELL PER MONTH

	DRILLING WELL RATE (Use Total Depth)	PRODUCING WELL RATE (Use Current Producing Depth)		
Well Depth	Each Well	First Five	Next Five	All Wells Over Ten

(2) [ ] Percentage Basis

PERCENTAGE BASIS

Development:

..... Percent (%) of the cost of development of the Joint Property exclusive of costs provided under Paragraph 8 of Section II and all salvage credits.

Operating:

..... Percent (%) of the cost of operating the Joint Property exclusive of costs provided under Paragraphs 1 and 8 of Section II, all salvage credits, the value of injected substances purchased for secondary recovery and all taxes and assessments which are levied, assessed and paid upon the mineral interest in and to the Joint Property.

C. Operator's Warehouse Operating and Maintenance Expense

[ ] Included in district expense

[X] No charge either direct or indirect

[ ] Percentage basis (describe fully) .....

.....

.....

2. **Combined Rates - Well Basis**

Operator shall charge the Joint Account for the services covered by Paragraph 1 of this Section III on the basis indicated below:

RATE PER WELL PER MONTH

Well Depth	DRILLING WELL RATE (Use Total Depth) Each Well	All Wells	PRODUCING WELL RATE (Use Current Producing Depth)	
All depths	1460.00	205.00		

3. **Combined Rates - Percentage Basis**

Operator shall charge the Joint Account for the services covered by Paragraph 1 of this Section III on the basis indicated below:

PERCENTAGE BASIS

A. Development:

..... Percent (%) of the cost of development of the Joint Property exclusive of costs provided under Paragraph 8 of Section II and all salvage credits.

B. Operating:

..... Percent (%) of the cost of operating the Joint Property exclusive of costs provided under Paragraphs 1 and 8 of Section II, all salvage credits, the value of injected substances purchased for secondary recovery and all taxes and assessments which are levied, assessed and paid upon the mineral interest in and to the Joint Property.

4. **Application of Administrative Overhead or Combined Rates - Well Basis**

The following limitations, instructions and charges shall apply in the application of the rates as provided under either Paragraph 1B (1) or Paragraph 2 of this Section III.

A. Charges for drilling wells shall begin on the date each well is spudded and terminate on the date the drilling or completion rig is released, whichever is later, except that no charge shall be made during the suspension of drilling operations for fifteen (15) or more consecutive days.

B. The status of wells shall be as follows:

(1) Producing gas wells, injection wells for recovery operations, water supply wells utilized for waterflooding operations and salt water disposal wells shall be considered the same as producing oil wells.

(2) Wells permanently shut down but on which plugging operations are deferred shall be dropped from the well schedule at the time the shutdown is effected. Any well being plugged or produced during any portion of the month shall be considered as a producing well for the entire month.

(3) Wells being plugged back, drilled deeper, converted to a source or input well, or which are undergoing any type of workover that requires the use of a drilling rig or workover rig capable of drilling shall be considered the same as drilling wells.

(4) Temporarily shut-down wells, which are not produced or worked upon for a period of a full calendar month, shall not be included in the well schedule, provided however, wells shut in by governmental regulatory body shall be included in the well schedule only in the event the allowable production is transferred to some other well or wells on the Joint Property. In the event of a unit allowable, shut-in wells shall be counted in determining the charge hereunder for such month if said wells contribute allowable production that is actually produced during such month from one or more unit wells as a result of allowable transfer, inclusion in the unit allowable or other circumstances, but the total shut-in well count shall be limited to the minimum number of shut-in wells necessary to provide the contributed allowable actually produced during the month.

(5) Gas wells shall be included in the well schedule if directly connected to a permanent sales outlet even though temporarily shut in due to overproduction or failure of purchaser to take the allowed production.

(6) Wells completed in multiple horizons, shall be considered as a producing well for each separately producing horizon, providing each completion is considered a separate well by governmental or other statewide regulatory authority.

C. The well rates for producing wells shall be applied to the individual leases; provided that, whenever leases covered by this agreement are operated as a unitized project, the well rates shall be applied to the total number of producing wells, irrespective of individual leases.

D. The well rates shall be adjusted as of the first day of April each year following the effective date of the agreement to which this Accounting Procedure is attached. The adjustment shall be computed by multiplying the rate currently in use by the percentage increase or decrease in the average weekly earnings of Crude Petroleum and Gas Production Workers for the last calendar year compared to the preceding calendar year as shown by "The Index of Average Weekly Earnings of Crude Petroleum and Gas Production Workers" as published by the United States Department of Labor, Bureau of Labor Statistics, or the equivalent Canadian Index as published by the Dominion Bureau of Statistics, as applicable. The adjusted rates shall be the rates currently in use, plus or minus the computed adjustment.

5. **Application of Administrative Overhead or Combined Rates - Percentage Basis**

For the purpose of determining charges on a Percentage Basis under Paragraph 1B (2) or Paragraph 3 of this Section III, Development shall include all costs in connection with drilling, redrilling, deepening or any remedial operations on any or all wells involving the use of drilling crew and equipment; also, preliminary expenditures necessary in preparation for drilling and expenditures incurred in abandoning when well is not completed as a producer; and original cost of construction or installation of fixed assets, the expansion of fixed assets and any other project clearly discernible as a fixed asset, except Major Construction as defined in Paragraph 6 of this Section III. All other costs shall be considered as Operating.

6. **Major Construction Overhead**

For the construction of compressor plants, water stations, secondary recovery systems, drilling and production platforms, salt water disposal facilities, and other such projects, as distinguished from the more usual drilling

and producing operations, Operator in addition to the Administrative Overhead or Combined Rates provided for in Paragraph 1, 2 or 3 of this Section III shall either negotiate a rate prior to beginning of construction or shall charge the Joint Account with an additional overhead charge as follows:

A. Total cost less than $25,000, no charge.

B. Total cost more than $25,000, but less than $100,000, 3 % of total cost.

C. Total cost of $100,000 or more, 3 % of the first $100,000 plus 2 % of all over $100,000 of total cost.

Total cost shall mean the total gross cost of any one project. For the purpose of this paragraph the component parts of a single project shall not be treated separately and the cost of drilling wells shall be excluded.

7. Amendment of Rates

The specific rates provided for in this Section III may be amended from time to time by mutual agreement between the Parties hereto if, in practice, the rates are found to be insufficient or excessive.

IV. BASIS OF CHARGES TO JOINT ACCOUNT

Subject to the further provisions of this Section IV, Operator will procure all Material and services for the Joint Property. At the Operator's option, Non-Operators may supply Material or services for the Joint Property.

1. Purchases

Material purchased and service procured shall be charged at the price paid by Operator after deduction of all discounts actually received.

2. Material furnished from Operator's Warehouse or Other Properties

A. New Material (Condition "A")

(1) Tubular goods, except line pipe, shall be priced on a maximum carload and/or barge load weight basis regardless of quantity transferred and equalized to the lowest prevailing price f.o.b. railway receiving point or recognized barge terminal nearest the Joint Property where such Material is normally available effective at date of transfer.

(2) Line pipe shall be priced at the current replacement cost effective at date of transfer from a reliable supply store nearest the Joint Property where such Material is normally available if the movement is less than 30,000 pounds. If the movement is 30,000 pounds or more, it shall be priced on the same basis as casing and tubing under Subparagraph (1) of this paragraph.

(3) When the Operator has equalized actual hauling costs as provided for in Paragraph 5 of Section II, Operator is permitted to include ten cents (10¢) per hundred-weight on all tubular goods furnished from his stocks in lieu of loading and unloading costs sustained.

(4) Other Material shall be priced at the current replacement cost of the same kind of Material, effective at date of movement and f.o.b. the supply store or railway receiving point nearest the Joint Property where Material of the same kind is normally available.

(5) The Joint Account shall not be credited with cash discounts applicable to prices provided for in this Paragraph 2 of Section IV.

B. Used Material (Condition "B" and "C")

(1) Material in sound and serviceable condition and suitable for reuse without reconditioning, shall be classified as Condition "B" and priced at seventy-five per cent (75%) of the current price of new Material.

(2) Material which is not suitable for its original function until after reconditioning shall be furnished to the Joint Account under one of the two methods defined below:

(a) Classified as Condition "B" and priced at seventy-five per cent (75%) of the current price of new Material. The cost of reconditioning shall be absorbed by the Operator of the transferring property.

(b) Classified as Condition "C" and priced at fifty per cent (50%) of current price of new Material. The cost of reconditioning also shall be charged to the receiving property, provided Condition "C" value, plus cost of reconditioning, does not exceed Condition "B" value.

(3) Obsolete Material or Material which cannot be classified as Condition "B" or Condition "C" shall be priced at a value commensurate with its use. Material no longer suitable for its original purpose but usable for some other purpose, shall be priced on a basis comparable with that of items normally used for such other purpose.

(4) Material involving erection costs shall be charged at applicable percentage of the current knocked-down price of new Material.

3. Premium Prices

Whenever Material is not readily obtainable at prices specified in Paragraphs 1 and 2 of this Section IV because of national emergencies, strikes or other unusual causes over which the Operator has no control, the Operator may charge the Joint Account for the required Material at the Operator's actual cost incurred in procuring such Material, in making it suitable for use, and in moving it to the Joint Property, provided, that notice in writing is furnished to Non-Operators of the proposed charge prior to billing Non-Operators for such Material. Each Non-Operator shall have the right, by so electing and notifying Operator within 10 days after receiving notice from Operator, to furnish in kind all or part of his share of such Material suitable for use and acceptable to Operator.

4. Warranty of Material Furnished by Operator

Operator does not warrant the Material furnished. In case of defective Material, credit shall not be passed to the Joint Account until adjustment has been received by Operator from the manufacturers or their agents.

5. Equipment and Facilities Furnished by Operator

A. Operator shall charge the Joint Account for use of equipment and facilities at rates commensurate with cost of ownership and operation. Such rates shall include cost of maintenance, repairs, other operating expense, insurance, taxes, depreciation, and interest on investment not to exceed six per cent (6%) per annum, provided such rates shall not exceed those currently prevailing in the immediate area within which the Joint Property is located. In lieu of rates based on costs of ownership and operation of equipment, other than automotive, Operator may elect to use commercial rates prevailing in the area of the Joint Property less 20%; for automotive equipment, rates as published by the Petroleum Motor Transport Association may be used. Rates for laboratory services shall not exceed those currently prevailing if performed by

outside service laboratories. Rates for trucks, tractors and well service units may include wages and expenses of operator.

B. Whenever requested, Operator shall inform Non-Operators in advance of the rates it proposes to charge.

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

V. DISPOSAL OF MATERIAL

The Operator may purchase, but shall be under no obligation to purchase, interest of Non-Operators in surplus Condition "A" or "B" Material. The disposition of surplus Controllable Material, not purchased by Operator, shall be agreed to by Operator and Non-Operators, provided Operator shall dispose of normal accumulations of junk and scrap Material either by transfer or sale from Joint Property.

1. **Material Purchased by the Operator or Non-Operators.**
   Material purchased by either the Operator or Non-Operators shall be credited by the Operator to the Joint Account for the month in which the Material is removed by the purchaser.
2. **Division in Kind**
   Division of Material in kind, if made between Operator and Non-Operators, shall be in proportion to the respective interests in such Material. The Parties will thereupon be charged individually with the value of the Material received or receivable. Proper credits shall be made by the Operator to the Joint Account.
3. **Sales to Outsiders**
   Sales to outsiders of Material from the Joint Property shall be credited by Operator to the Joint Account at the net amount collected by Operator from vendee. Any claim by vendee related to such sale shall be charged back to the Joint Account if and when paid by Operator.

VI. BASIS OF PRICING MATERIAL TRANSFERRED FROM JOINT ACCOUNT

Material purchased by either Operator or Non-Operators or divided in kind, unless agreed to by Operator and Non-Operators shall be priced on the following basis:

1. **New Price Defined**
   New price as used in this Section VI shall be the price specified for new Material in Section IV.
2. **New Material**
   New Material (Condition "A"), being new Material procured for the Joint Property but never used, at one hundred per cent (100%) of current new price (plus sales tax if any).
3. **Good Used Material**
   Good used Material (Condition "B"), being used Material in sound and serviceable condition, suitable for reuse without reconditioning:
   A. At seventy-five per cent (75%) of current new price if Material was charged to Joint Account as new, or
   B. At sixty-five per cent (65%) of current new price if Material was originally charged to the Joint Account as secondhand at seventy-five per cent (75%) of new price.
4. **Other Used Material**
   Used Material (Condition "C"), at fifty per cent (50%) of current new price, being used Material which:
   A. Is not in sound and serviceable condition but suitable for reuse after reconditioning, or
   B. Is serviceable for original function but not suitable for reconditioning.
5. **Bad-Order Material**
   Material (Condition "D"), no longer suitable for its original purpose without excessive repair cost but usable for some other purpose at a price comparable with that of items normally used for such other purpose.
6. **Junk Material**
   Junk Material (Condition "E"), being obsolete and scrap Material, at prevailing prices.
7. **Temporarily Used Material**
   When the use of Material is temporary and its service to the Joint Property does not justify the reduction in price as provided for in Paragraph 3B of this Section VI, such Material shall be priced on a basis that will leave a net charge to the Joint Account consistent with the value of the service rendered.

VII. INVENTORIES

The Operator shall maintain detailed records of Controllable Material.

1. **Periodic Inventories, Notice and Representation**
   At reasonable intervals, inventories shall be taken by Operator of the Joint Account Controllable Material. Written notice of intention to take inventory shall be given by Operator at least thirty (30) days before any inventory is to begin so that Non-Operators may be represented when any inventory is taken. Failure of Non-Operators to be represented at an inventory shall bind Non-Operators to accept the inventory taken by Operator.
2. **Reconciliation and Adjustment of Inventories**
   Reconciliation of inventory with the Joint Account shall be made, and a list of overages and shortages shall be furnished to the Non-Operators. Inventory adjustments shall be made by Operator with the Joint Account for overages and shortages, but Operator shall be held accountable to Non-Operators only for shortages due to lack of reasonable diligence.
3. **Special Inventories**
   Special Inventories may be taken whenever there is any sale or change of interest in the Joint Property. It shall be the duty of the party selling to notify all other Parties as quickly as possible after the transfer of interest takes place. In such cases, both the seller and the purchaser shall be governed by such inventory.
4. **Expense of Conducting Periodic Inventories**
   The expense of conducting periodic inventories shall not be charged to the Joint Account unless agreed to by Operator and Non-Operators.

EXHIBIT "C"
UNIT OPERATING AGREEMENT
DEER CANYON UNIT
EDDY COUNTY, NEW MEXICO

Insurance

(A) At all times while operations are being conducted hereunder, Operator shall maintain in force the following policies of insurance:

(1) Workmen's Compensation Insurance in accordance with the laws of the jurisdiction in which work is performed.

(2) Employers Liability coverage with limits of $100,000 for all liability arising out of one accident.

(3) Coverages (1) and (2) above shall not include Non-Operators as additional insureds but shall waive subrogation against Non-Operators.

(4) General Comprehensive Liability coverage, except automobile coverage, with minimum limits of Bodily Injury $100,000 each person and $300,000 each occurrence, including contractual liability and completed operations, but excluding blowout, pollution liability and damage to underground resources.

(5) Automobile Liability coverage, including owned, hired, and non-owned vehicles, with minimum limits the same as paragraph (4) above. No premium charges shall be billed Non-Operators in connection with Operator's fully-owned equipment--this premium not to be charged directly to the Joint Account, but will instead be covered by the flat rate charges assessed the Unit for use of such equipment.

(6) Coverages (4) and (5) above shall include Non-Operators as Additional Insureds.

(B) Such policies shall contain a waiver of territorial restrictions so that the insurance coverage thereof will apply to the proposed area of operations hereunder. The premiums for all insurance policies under this Article shall be allocated among the various Operating Joint Accounts of the parties hereto, and Operator, upon written request, shall furnish Non-Operators with evidence that such insurance is in effect prior to the commencement of any operations hereunder. No insurance other than that specified above shall be purchased for any Operating Joint Account except by mutual consent of the parties.

(C) Operator will determine the insurance requirements for contractors and subcontractors or third parties performing operations on or in connection with the Leased Lands; however, the requirements will be reviewed with Non-Operators at any time, upon request, for mutual determination of any necessary changes. When negotiating contracts hereunder, Operator shall attempt to hold contractor solely responsible for damage to contractor's equipment and shall attempt to obtain a waiver of contractor's right of recovery against parties hereto in connection with any such damage. Upon request, Operator will advise Non-Operators as to insurance requirements in use under this provision in order that Non-Operators may acquire any additional insurance for Non-Operators' account and protection not purchased by Operator for an Operating Joint Account.