

TXO PRODUCTION CORP.  
Case No. 8755  
11/21/85 Examiner Hearing  
Exhibit No. 5

A.A.P.L. FORM 610-1977

MODEL FORM OPERATING AGREEMENT

OPERATING AGREEMENT

DATED

September 23, 1985

OPERATOR TXO Production Corp.

CONTRACT AREA NW/4 NW/4 and NE/4 NW/4 and S/2 NW/4 Section 26,

T-18-S, R-32-E

COUNTY ~~OR TOWNSHIP~~ OF Lea STATE OF New Mexico

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OPERATING AGREEMENT

THIS AGREEMENT, entered into by and between TXO Production Corp., hereinafter designated and referred to as "Operator", and the signatory party or parties other than Operator, sometimes hereinafter referred to individually herein as "Non-Operator", and collectively as "Non-Operators",

WITNESSETH:

WHEREAS, the parties to this agreement are owners of oil and gas leases and or oil and gas interests in the land identified in Exhibit "A", and the parties hereto have reached an agreement to explore and develop these leases and or oil and gas interests for the production of oil and gas to the extent and as hereinafter provided:

NOW, THEREFORE, it is agreed as follows:

ARTICLE I. DEFINITIONS

As used in this agreement, the following words and terms shall have the meanings here ascribed to them:

A. The term "oil and gas" shall mean oil, gas, casinghead gas, gas condensate, and all other liquid or gaseous hydrocarbons and other marketable substances produced therewith, unless an intent to limit the inclusiveness of this term is specifically stated.

B. The terms "oil and gas lease", "lease" and "leasehold" shall mean the oil and gas leases covering tracts of land lying within the Contract Area which are owned by the parties to this agreement.

C. The term "oil and gas interests" shall mean unleased fee and mineral interests in tracts of land lying within the Contract Area which are owned by parties to this agreement.

D. The term "Contract Area" shall mean all of the lands, oil and gas leasehold interests and oil and gas interests intended to be developed and operated for oil and gas purposes under this agreement. Such lands, oil and gas leasehold interests and oil and gas interests are described in Exhibit "A".

E. The term "drilling unit" shall mean the area fixed for the drilling of one well by order or rule of any state or federal body having authority. If a drilling unit is not fixed by any such rule or order, a drilling unit shall be the drilling unit as established by the pattern of drilling in the Contract Area or as fixed by express agreement of the Drilling Parties.

F. The term "drillsite" shall mean the oil and gas lease or interest on which a proposed well is to be located.

G. The terms "Drilling Party" and "Consenting Party" shall mean a party who agrees to join in and pay its share of the cost of any operation conducted under the provisions of this agreement.

H. The terms "Non-Drilling Party" and "Non-Consenting Party" shall mean a party who elects not to participate in a proposed operation.

Unless the context otherwise clearly indicates, words used in the singular include the plural, the plural includes the singular, and the neuter gender includes the masculine and the feminine.

ARTICLE II. EXHIBITS

The following exhibits, as indicated below and attached hereto, are incorporated in and made a part hereof:

- [X] A. Exhibit "A", shall include the following information: (1) Identification of lands subject to agreement, (2) Restrictions, if any, as to depths or formations, (3) Percentages or fractional interests of parties to this agreement, (4) Oil and gas leases and or oil and gas interests subject to this agreement, (5) Addresses of parties for notice purposes. [X] B. Exhibit "B", Form of Lease. [X] C. Exhibit "C", Accounting Procedure. [X] D. Exhibit "D", Insurance. [X] E. Exhibit "E", Gas Balancing Agreement. [X] F. Exhibit "F", Non-Discrimination and Certification of Non-Segregated Facilities.

If any provision of any exhibit, except Exhibit "E", is inconsistent with any provision contained in the body of this agreement, the provisions in the body of this agreement shall prevail.

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ARTICLE III.  
INTERESTS OF PARTIES

A. Oil and Gas Interests:

If any party owns an unleased oil and gas interest in the Contract Area, that interest shall be treated for the purpose of this agreement and during the term hereof as if it were a leased interest under the form of oil and gas lease attached as Exhibit "B". As to such interest, the owner shall receive royalty on production as prescribed in the form of oil and gas lease attached hereto as Exhibit "B". Such party shall, however, be subject to all of the provisions of this agreement relating to lessees, to the extent that it owns the lessee interest.

B. Interest of Parties in Costs and Production:

Exhibit "A" lists all of the parties and their respective percentage or fractional interests under this agreement. Unless changed by other provisions, all costs and liabilities incurred in operations under this agreement shall be borne and paid, and all equipment and material acquired in operations on the Contract Area shall be owned by the parties as their interests are shown in Exhibit "A". All production of oil and gas from the Contract Area, subject to the payment of lessor's royalties ~~which shall be borne by the Joint Account~~, shall also be owned by the parties in the same manner during the term hereof; provided, however, this shall not be deemed an assignment or cross-assignment of interests covered hereby.

ARTICLE IV.  
TITLES

A. Title Examination:

Title examination shall be made on the drillsite of any proposed well prior to commencement of drilling operations or, if the Drilling Parties so request, title examination shall be made on the leases and or oil and gas interests included, or planned to be included, in the drilling unit around such well. The opinion will include the ownership of the working interest, minerals, royalty, overriding royalty and production payments under the applicable leases. At the time a well is proposed, each party contributing leases and or oil and gas interests to the drillsite, or to be included in such drilling unit, shall furnish to Operator all abstracts (including Federal Lease Status Reports), title opinions, title papers and curative material in its possession free of charge. All such information not in the possession of or made available to Operator by the parties, but necessary for the examination of title, shall be obtained by Operator. Operator shall cause title to be examined by attorneys on its staff or by outside attorneys. Copies of all title opinions shall be furnished to each party hereto. The cost incurred by Operator in this title program shall be borne as follows:

Option No. 1: Costs incurred by Operator in procuring abstracts and title examination (including preliminary, supplemental, shut-in gas royalty opinions and division order title opinions) shall be a part of the administrative overhead as provided in Exhibit "C" and shall not be a direct charge, whether performed by Operator's staff attorneys or by outside attorneys.

Option No. 2: Costs incurred by Operator in procuring abstracts and fees paid outside attorneys for title examination (including preliminary, supplemental, shut-in gas royalty opinions and division order title opinions) shall be borne by the Drilling Parties in the proportion that the interest of each Drilling Party bears to the total interest of all Drilling Parties as such interests appear in Exhibit "A". Operator shall make no charge for services rendered by its staff attorneys or other personnel in the performance of the above functions.

Each party shall be responsible for securing curative matter and pooling amendments or agreements required in connection with leases or oil and gas interests contributed by such party. The Operator shall be responsible for the preparation and recording of Pooling Designations or Declarations as well as the conduct of hearings before Governmental Agencies for the securing of spacing or pooling orders. This shall not prevent any party from appearing on its own behalf at any such hearing.

No well shall be drilled on the Contract Area until after (1) the title to the drillsite or drilling unit has been examined as above provided, or (2) the title has been approved by the examining attorney or title has been accepted by all of the parties who are to participate in the drilling of the well.

B. Loss of Title:

1. Failure of Title: Should any oil and gas interest or lease, or interest therein, be lost through failure of title, which loss results in a reduction of interest from that shown on Exhibit "A", this agreement, nevertheless, shall continue in force as to all remaining oil and gas leases and interests, and

(a) The party whose oil and gas lease or interest is affected by the title failure shall bear alone the entire loss and it shall not be entitled to recover from Operator or the other parties any development

1 or operating costs <sup>for</sup> which it may have theretofore <sup>been responsible</sup> ~~paid~~, but there shall be no monetary liability on its  
 2 part to the other parties hereto for drilling, development, operating or other similar costs by reason of  
 3 such title failure; and <sup>subsequently incurred</sup>

4 (b) There shall be no retroactive adjustment of expenses incurred or revenues received from the  
 5 operation of the interest which has been lost, but the interests of the parties shall be revised on an acre-  
 6 age basis, as of the time it is determined finally that title failure has occurred, so that the interest of  
 7 the party whose lease or interest is affected by the title failure will thereafter be reduced in the Contract  
 8 Area by the amount of the interest lost; and

9 (c) If the proportionate interest of the other parties hereto in any producing well theretofore drilled  
 10 on the Contract Area is increased by reason of the title failure, the party whose title has failed shall  
 11 receive the proceeds attributable to the increase in such interests (less costs and burdens attributable  
 12 thereto) until it has been reimbursed for unrecovered costs paid by it in connection with such well;  
 13 and

14 (d) Should any person not a party to this agreement, who is determined to be the owner of any in-  
 15 terest in the title which has failed, pay in any manner any part of the cost of operation, development,  
 16 or equipment, such amount shall be paid to the party or parties who bore the costs which are so refund-  
 17 ed; and

18 (e) Any liability to account to a third party for prior production of oil and gas which arises by  
 19 reason of title failure shall be borne by the party or parties <sup>whose title failed</sup> in the same proportions in which they shared  
 20 in such prior production; and

21 (f) No charge shall be made to the joint account for legal expenses, fees or salaries, in connection  
 22 with the defense of the interest claimed by any party hereto, it being the intention of the parties  
 23 hereto that each shall defend title to its interest and bear all expenses in connection therewith.  
 24

25 2. Loss by Non-Payment or Erroneous Payment of Amount Due: If, through mistake or oversight,  
 26 any rental, shut-in well payment, minimum royalty or royalty payment, is not paid or is erroneously  
 27 paid, and as a result a lease or interest therein terminates, there shall be no monetary liability against  
 28 the party who failed to make such payment. Unless the party who failed to make the required payment  
 29 secures a new lease covering the same interest within ninety (90) days from the discovery of the fail-  
 30 ure to make proper payment, which acquisition will not be subject to Article VIII.B., the interests of  
 31 the parties shall be revised on an acreage basis, effective as of the date of termination of the lease in-  
 32 volved, and the party who failed to make proper payment will no longer be credited with an interest in  
 33 the Contract Area on account of ownership of the lease or interest which has terminated. In the event  
 34 the party who failed to make the required payment shall not have been fully reimbursed, at the time of  
 35 the loss, from the proceeds of the sale of oil and gas attributable to the lost interest, calculated on an  
 36 acreage basis, for the development and operating costs theretofore paid on account of such interest, it  
 37 shall be reimbursed for unrecovered actual costs theretofore paid by it (but not for its share of the  
 38 cost of any dry hole previously drilled or wells previously abandoned) from so much of the following  
 39 as is necessary to effect reimbursement:

40 (a) Proceeds of oil and gas, less operating expenses, theretofore accrued to the credit of the lost  
 41 interest, on an acreage basis, up to the amount of unrecovered costs;

42 (b) Proceeds, less operating expenses, thereafter accrued attributable to the lost interest on an  
 43 acreage basis, of that portion of oil and gas thereafter produced and marketed (excluding production  
 44 from any wells thereafter drilled) which, in the absence of such lease termination, would be attributable  
 45 to the lost interest on an acreage basis, up to the amount of unrecovered costs, the proceeds of said  
 46 portion of the oil and gas to be contributed by the other parties in proportion to their respective in-  
 47 terests; and

48 (c) Any monies, up to the amount of unrecovered costs, that may be paid by any party who is, or  
 49 becomes, the owner of the interest lost, for the privilege of participating in the Contract Area or be-  
 50 coming a party to this agreement.  
 51

52 3. Other Losses: All losses incurred, other than those set forth in Articles IV.B.1. and IV.B.2.  
 53 above, shall not be considered failure of title but shall be joint losses and shall be borne by all parties  
 54 in proportion to their interests. There shall be no readjustment of interests in the remaining portion of  
 55 the Contract Area.  
 56

57 ARTICLE V.  
 58 OPERATOR

59  
 60 A. DESIGNATION AND RESPONSIBILITIES OF OPERATOR:

61  
 62 TXO Production Corp. shall be the  
 63 Operator of the Contract Area, and shall conduct and direct and have full control of all operations on  
 64 the Contract Area as permitted and required by, and within the limits of, this agreement. It shall con-  
 65 duct all such operations in a good and workmanlike manner, but it shall have no liability as Operator  
 66 to the other parties for losses sustained or liabilities incurred, except such as may result from gross  
 67 negligence or willful misconduct  
 68  
 69  
 70

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1 B. Resignation or Removal of Operator and Selection of Successor:

2  
3 1. Resignation or Removal of Operator: Operator may resign at any time by giving written notice  
4 thereof to Non-Operators. If Operator terminates its legal existence, no longer owns an interest in the  
5 Contract Area, or is no longer capable of serving as Operator, it shall cease to be Operator without any  
6 action by Non-Operator, except the selection of a successor. Operator may be removed if it fails or  
7 refuses to carry out its duties hereunder, or becomes insolvent, bankrupt or is placed in receivership,  
8 by the affirmative vote of two (2) or more Non-Operators owning a majority interest based on owner-  
9 ship as shown on Exhibit "A", and not on the number of parties remaining after excluding the voting  
10 interest of Operator. Such resignation or removal shall not become effective until 7:00 o'clock A.M.  
11 on the first day of the calendar month following the expiration of ninety (90) days after the giving of  
12 notice of resignation by Operator or action by the Non-Operators to remove Operator, unless a successor  
13 Operator has been selected and assumes the duties of Operator at an earlier date. Operator, after effect-  
14 ive date of resignation or removal, shall be bound by the terms hereof as a Non-Operator. A change of  
15 a corporate name or structure of Operator or transfer of Operator's interest to any single subsidiary,  
16 parent or successor corporation shall not be the basis for removal of Operator.

17  
18 2. Selection of Successor Operator: Upon the resignation or removal of Operator, a successor Op-  
19 erator shall be selected by the Parties. The successor Operator shall be selected from the parties owning  
20 an interest in the Contract Area at the time such successor Operator is selected. If the Operator that  
21 is removed fails to vote or votes only to succeed itself, the successor Operator shall be selected by the  
22 affirmative vote of two (2) or more parties owning a majority interest based on ownership as shown  
23 on Exhibit "A", and not on the number of parties remaining after excluding the voting interest of the  
24 Operator that was removed.

25  
26 C. Employees:

27  
28 The number of employees used by Operator in conducting operations hereunder, their selection,  
29 and the hours of labor and the compensation for services performed, shall be determined by Operator,  
30 and all such employees shall be the employees of Operator.

31  
32 D. Drilling Contracts:

33  
34 All wells drilled on the Contract Area shall be drilled on a competitive contract basis at the usual  
35 rates prevailing in the area. If it so desires, Operator may employ its own tools and equipment in the  
36 drilling of wells, but its charges therefor shall not exceed the prevailing rates in the area and the rate  
37 of such charges shall be agreed upon by the parties in writing before drilling operations are com-  
38 menced, and such work shall be performed by Operator under the same terms and conditions as are  
39 customary and usual in the area in contracts of independent contractors who are doing work of a sim-  
40 ilar nature.

41  
42 ARTICLE VI  
43 DRILLING AND DEVELOPMENT

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44  
45 A. Initial Well:

46  
47 ~~On or before the \_\_\_\_\_ day of \_\_\_\_\_, 19\_\_\_\_, Operator shall commence the drill-~~  
48 ~~ing of a well for oil and gas at the following location:~~

49  
50  
51  
52  
53 ~~and shall thereafter continue the drilling of the well with due diligence to~~

54  
55 The initial well was drilled pursuant to that certain Farmin Agreement  
56 dated January 30, 1985 by and between TXO Production Corp. and Petro Atlas  
57 Corporation. This Operating Agreement shall govern operations on the Farmout  
58 Area as provided for in Article IV of the aforementioned Farmin Agreement.  
59 ~~unless a change of other parties to the Farmin Agreement or completion of the well, which renders~~  
60 ~~further drilling impractical, is encountered at a lesser depth, or unless all parties agree to complete or~~  
61 ~~abandon the well at a lesser depth.~~

62  
63 Operator shall make reasonable tests of all formations encountered during drilling which give in-  
64 dication of containing oil and gas in quantities sufficient to test, unless this agreement shall be limited  
65 in its application to a specific formation or formations, in which event Operator shall be required to  
66 test only the formation or formations to which this agreement may apply.

67  
68 If, in Operator's judgment, the well will not produce oil or gas in paying quantities, and it wishes  
69 to plug and abandon the well as a dry hole, it shall first secure the consent of all parties and shall  
70 plug and abandon same as provided in Article VI E 1 hereof

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1 **B. Subsequent Operations:**

2  
 3 1. Proposed Operations: Should any party hereto desire to drill any well on the Contract Area  
 4 other than the well provided for in Article VI.A., or to rework, deepen or plug back a dry hole drilled  
 5 at the joint expense of all parties or a well jointly owned by all the parties and not then producing  
 6 in paying quantities, the party desiring to drill, rework, deepen or plug back such a well shall give the  
 7 other parties written notice of the proposed operation, specifying the work to be performed, the loca-  
 8 tion, proposed depth, objective formation and the estimated cost of the operation. The parties receiv-  
 9 ing such a notice shall have thirty (30) days after receipt of the notice within which to notify the  
 10 parties wishing to do the work whether they elect to participate in the cost of the proposed operation.  
 11 If a drilling rig is on location, notice of proposal to rework, plug back or drill deeper may be given  
 12 by telephone and the response period shall be limited to forty-eight (48) hours, exclusive of Saturday,  
 13 Sunday or legal holidays. Failure of a party receiving such notice to reply within the period above fixed  
 14 shall constitute an election by that party not to participate in the cost of the proposed operation. Any  
 15 notice or response given by telephone shall be promptly confirmed in writing.

16  
 17 2. Operations by Less than All Parties: If any party receiving such notice as provided in Article  
 18 VI.B.1. or VI.E.1. elects not to participate in the proposed operation, then, in order to be entitled to  
 19 the benefits of this article, the party or parties giving the notice and such other parties as shall elect  
 20 to participate in the operation shall, within sixty (60) days after the expiration of the notice period of  
 21 thirty (30) days (or as promptly as possible after the expiration of the forty-eight (48) hour period  
 22 where the drilling rig is on location, as the case may be) actually commence work on the proposed  
 23 operation and complete it with due diligence. Operator shall perform all work for the account of the  
 24 Consenting Parties; provided, however, if no drilling rig or other equipment is on location, and if Op-  
 25 erator is a Non-Consenting Party, the Consenting Parties shall either: (a) request Operator to perform  
 26 the work required by such proposed operation for the account of the Consenting Parties, or (b) desig-  
 27 nate one (1) of the Consenting Parties as Operator to perform such work. Consenting Parties, when  
 28 conducting operations on the Contract Area pursuant to this Article VI.B.2., shall comply with all terms  
 29 and conditions of this agreement.

30  
 31 If less than all parties approve any proposed operation, the proposing party, immediately after the  
 32 expiration of the applicable notice period, shall advise the Consenting Parties of (a) the total interest  
 33 of the parties approving such operation, and (b) its recommendation as to whether the Consenting Par-  
 34 ties should proceed with the operation as proposed. Each Consenting Party, within forty-eight (48)  
 35 hours (exclusive of Saturday, Sunday or legal holidays) after receipt of such notice, shall advise the  
 36 proposing party of its desire to (a) limit participation to such party's interest as shown on Exhibit "A",  
 37 or (b) carry its proportionate part of Non-Consenting Parties' interest. \*The proposing party, at its  
 38 election, may withdraw such proposal if there is insufficient participation, and shall promptly notify  
 39 all parties of such decision. \*and failure so to advise the proposing party shall constitute  
 40 an election under (b)

41 The entire cost and risk of conducting such operations shall be borne by the Consenting Parties in  
 42 the proportions they have elected to bear same under the terms of the preceding paragraph. Consenting  
 43 Parties shall keep the leasehold estates involved in such operations free and clear of all liens and  
 44 encumbrances of every kind created by or arising from the operations of the Consenting Parties. If such  
 45 an operation results in a dry hole, the Consenting Parties shall plug and abandon the well at their sole  
 46 cost, risk and expense. If any well drilled, reworked, deepened or plugged back under the provisions  
 47 of this Article results in a producer of oil and or gas in paying quantities, the Consenting Parties shall  
 48 complete and equip the well to produce at their sole cost and risk, and the well shall then be turned  
 49 over to Operator and shall be operated by it at the expense and for the account of the Consenting Parties.  
 50 Upon commencement of operations for the drilling, reworking, deepening or plugging back of any such  
 51 well by Consenting Parties in accordance with the provisions of this Article, each Non-Consenting Party  
 52 shall be deemed to have relinquished to Consenting Parties, and the Consenting Parties shall own and  
 53 be entitled to receive, in proportion to their respective interests, all of such Non-Consenting Party's  
 54 interest in the well and share of production therefrom until the proceeds of the sale of such share,  
 55 calculated at the well, or market value thereof if such share is not sold (after deducting production  
 56 taxes, royalty, overriding royalty and other interests existing on the effective date hereof, payable out of  
 57 or measured by the production from such well accruing with respect to such interest until it reverts)  
 58 shall equal the total of the following:

59  
 60 (a) 300 of each such Non-Consenting Party's share of the cost of any newly acquired surface  
 61 equipment beyond the wellhead connections (including, but not limited to, stock tanks, separators,  
 62 treaters, pumping equipment and piping), plus 100% of each such Non-Consenting Party's share of the  
 63 cost of operation of the well commencing with first production and continuing until each such Non-  
 64 Consenting Party's relinquished interest shall revert to it under other provisions of this Article, it being  
 65 agreed that each Non-Consenting Party's share of such costs and equipment will be that interest which  
 66 would have been chargeable to each Non-Consenting Party had it participated in the well from the be-  
 67 ginning of the operation, and

68  
 69 (b) 400 of that portion of the costs and expenses of drilling, reworking, deepening, or plugging  
 70 back, testing and completing, after deducting any cash contributions received under Article VIII C, and

1 400 of that portion of the cost of newly acquired equipment in the well (to and including the well-  
 2 head connections), which would have been chargeable to such Non-Consenting Party if it had partici-  
 3 pated therein. \*See Article XV.G. for additional provisions  
 4

5 Gas production attributable to any Non - Consenting Party's relinquished interest upon such Party's  
 6 election, shall be sold to its purchaser, if available, under the terms of its existing gas sales con-  
 7 tract. Such Non - Consenting Party shall direct its purchaser to remit the proceeds receivable from  
 8 such sale direct to the Consenting Parties until the amounts provided for in this Article are recov-  
 9 ered from the Non - Consenting Party's relinquished interest. If such Non - Consenting Party has not  
 10 contracted for sale of its gas at the time such gas is available for delivery, or has not made the elec-  
 11 tion as provided above, the Consenting Parties shall own and be entitled to receive and sell such Non-  
 12 Consenting Party's share of gas as hereinabove provided during the recoupment period.  
 13

14 During the period of time Consenting Parties are entitled to receive Non-Consenting Party's share  
 15 of production, or the proceeds therefrom, Consenting Parties shall be responsible for the payment of  
 16 all production, severance, gathering and other taxes, and all royalty, overriding royalty and other  
 17 burdens applicable to Non-Consenting Party's share of production.  
 18

19 In the case of any reworking, plugging back or deeper drilling operation, the Consenting Parties shall  
 20 be permitted to use, free of cost, all casing, tubing and other equipment in the well, but the ownership of  
 21 all such equipment shall remain unchanged; and upon abandonment of a well after such reworking,  
 22 plugging back or deeper drilling, the Consenting Parties shall account for all such equipment to the  
 23 owners thereof, with each party receiving its proportionate part in kind or in value, less cost of  
 24 salvage.  
 25

26 Within sixty (60) days after the completion of any operation under this Article, the party con-  
 27 ducting the operations for the Consenting Parties shall furnish each Non-Consenting Party with an in-  
 28 ventory of the equipment in and connected to the well, and an itemized statement of the cost of drilling,  
 29 deepening, plugging back, testing, completing, and equipping the well for production; or, at its option,  
 30 the operating party, in lieu of an itemized statement of such costs of operation, may submit a detailed  
 31 statement of monthly billings. Each month thereafter, during the time the Consenting Parties are being  
 32 reimbursed as provided above, the Party conducting the operations for the Consenting Parties shall furn-  
 33 ish the Non-Consenting Parties with an itemized statement of all costs and liabilities incurred in the  
 34 operation of the well, together with a statement of the quantity of oil and gas produced from it and the  
 35 amount of proceeds realized from the sale of the well's working interest production during the preceding  
 36 month. In determining the quantity of oil and gas produced during any month, Consenting Parties  
 37 shall use industry accepted methods such as, but not limited to, metering or periodic well tests. Any  
 38 amount realized from the sale or other disposition of equipment newly acquired in connection with any  
 39 such operation which would have been owned by a Non-Consenting Party had it participated therein  
 40 shall be credited against the total unreturned costs of the work done and of the equipment purchased,  
 41 in determining when the interest of such Non-Consenting Party shall revert to it as above provided;  
 42 and if there is a credit balance, it shall be paid to such Non-Consenting party.  
 43

44 If and when the Consenting Parties recover from a Non-Consenting Party's relinquished interest  
 45 the amounts provided for above, the relinquished interests of such Non-Consenting Party shall auto-  
 46 matically revert to it, and, from and after such reversion, such Non-Consenting Party shall own the same  
 47 interest in such well, the material and equipment in or pertaining thereto, and the production there-  
 48 from as such Non-Consenting Party would have been entitled to had it participated in the drilling,  
 49 reworking, deepening or plugging back of said well. Thereafter, such Non-Consenting Party shall be  
 50 charged with and shall pay its proportionate part of the further costs of the operation of said well in  
 51 accordance with the terms of this agreement and the Accounting Procedure, attached hereto.  
 52

53 Notwithstanding the provisions of this Article VI.B.2., it is agreed that without the mutual consent  
 54 of all parties, no wells shall be completed in or produced from a source of supply from which a well  
 55 located elsewhere on the Contract Area is producing, unless such well conforms to the then-existing  
 56 well spacing pattern for such source of supply.  
 57

58 The provisions of this Article shall have no application whatsoever to the drilling of the initial  
 59 well described in Article VI.A, except (a) when Option 2, Article VII.D.1., has been selected, or (b)  
 60 to the reworking, deepening and plugging back of such initial well, if such well is or thereafter shall  
 61 prove to be a dry hole or non-commercial well, after having been drilled to the depth specified in Article  
 62 VI.A.  
 63

64 **C. Right to Take Production in Kind:**  
 65

66 Each party shall have the right to take in kind or separately dispose of its proportionate share of  
 67 all oil and gas produced from the Contract Area, exclusive of production which may be used in de-  
 68 velopment and producing operations and in preparing and treating oil for marketing purposes and  
 69 production unavoidably lost. Any extra expenditure incurred in the taking in kind or separate dispo-  
 70 sition by any party of its proportionate share of the production shall be borne by such party. Any

1 party taking its share of production in kind shall be required to pay for only its proportionate share  
 2 of such part of Operator's surface facilities which it uses.

3  
 4 Each party shall execute such division orders and contracts as may be necessary for the sale of its  
 5 interest in production from the Contract Area, and, except as provided in Article VII.B., shall be entitled  
 6 to receive payment direct from the purchaser thereof for its share of all production.

7  
 8 In the event any party shall fail to make the arrangements necessary to take in kind or separately  
 9 dispose of its proportionate share of the oil and gas produced from the Contract Area, Operator shall have  
 10 the right, subject to the revocation at will by the party owning it, but not the obligation, to purchase such  
 11 oil and gas or sell it to others at any time and from time to time, for the account of the non-taking  
 12 party at the best price obtainable in the area for such production. Any such purchase or sale by Op-  
 13 erator shall be subject always to the right of the owner of the production to exercise at any time its  
 14 right to take in kind, or separately dispose of, its share of all oil and gas not previously delivered to a  
 15 purchaser. Any purchase or sale by Operator of any other party's share of oil and gas shall be only for  
 16 such reasonable periods of time as are consistent with the minimum needs of the industry under the  
 17 particular circumstances, but in no event for a period in excess of one (1) year. Notwithstanding the  
 18 foregoing, Operator shall not make a sale, including one into interstate commerce, of any other party's  
 19 share of gas production without first giving such other party thirty (30) days notice of such intended  
 20 sale.  
 21 prior written

22 In the event one or more parties' separate disposition of its share of the gas causes split-stream de-  
 23 liveries to separate pipelines and or deliveries which on a day-to-day basis for any reason are not  
 24 exactly equal to a party's respective proportionate share of total gas sales to be allocated to it, the  
 25 balancing or accounting between the respective accounts of the parties shall be in accordance with  
 26 any Gas Balancing Agreement between the parties hereto, whether such Agreement is attached as  
 27 Exhibit "E", or is a separate Agreement.

28  
 29 **D. Access to Contract Area and Information:**

30  
 31 Each party shall have access to the Contract Area at all reasonable times, at its sole risk to inspect  
 32 or observe operations, and shall have access at reasonable times to information pertaining to the de-  
 33 velopment or operation thereof, including Operator's books and records relating thereto. Operator, upon  
 34 request, shall furnish each of the other parties with copies of all forms or reports filed with govern-  
 35 mental agencies, daily drilling reports, well logs, tank tables, daily gauge and run tickets and reports  
 36 of stock on hand at the first of each month, and shall make available samples of any cores or cuttings  
 37 taken from any well drilled on the Contract Area. The cost of gathering and furnishing information to  
 38 Non-Operator, other than that specified above, shall be charged to the Non-Operator that requests the  
 39 information.

40  
 41 **E. Abandonment of Wells:**

42  
 43 1. Abandonment of Dry Holes: Except for any well drilled pursuant to Article VI.B.2., any well  
 44 which has been drilled under the terms of this agreement and is proposed to be completed as a dry hole  
 45 shall not be plugged and abandoned without the consent of all parties. Should Operator, after diligent  
 46 effort, be unable to contact any party, or should any party fail to reply within forty-eight (48) hours  
 47 (exclusive of Saturday, Sunday or legal holidays) after receipt of notice of the proposal to plug and  
 48 abandon such well, such party shall be deemed to have consented to the proposed abandonment. All  
 49 such wells shall be plugged and abandoned in accordance with applicable regulations and at the cost,  
 50 risk and expense of the parties who participated in the cost of drilling of such well. Any party who ob-  
 51 jects to the plugging and abandoning such well shall have the right to take over the well and conduct  
 52 further operations in search of oil and or gas subject to the provisions of Article VI.B.

53  
 54 2. Abandonment of Wells that have Produced: Except for any well which has been drilled or re-  
 55 worked pursuant to Article VI.B.2. hereof for which the Consenting Parties have not been fully reim-  
 56 bursed as therein provided, any well which has been completed as a producer shall not be plugged and  
 57 abandoned without the consent of all parties. If all parties consent to such abandonment, the well shall  
 58 be plugged and abandoned in accordance with applicable regulations and at the cost, risk and expense  
 59 of all the parties hereto. If, within thirty (30) days after receipt of notice of the proposed abandonment  
 60 of such well, all parties do not agree to the abandonment of any well, those wishing to continue its op-  
 61 eration shall tender to each of the other parties its proportionate share of the value of the well's salvable  
 62 material and equipment, determined in accordance with the provisions of Exhibit "C", less the estimated  
 63 cost of salvaging and the estimated cost of plugging and abandoning. Each abandoning party shall  
 64 assign to the non-abandoning parties, without warranty, express or implied, as to title or as to quantity,  
 65 quality, or fitness for use of the equipment and material, all of its interest in the well and related equip-  
 66 ment, together with its interest in the leasehold estate as to, but only as to, the interval or intervals of the  
 67 formation or formations then open to production. If the interest of the abandoning party is or includes  
 68 an oil and gas interest, such party shall execute and deliver to the non-abandoning party or parties an  
 69 oil and gas lease, limited to the interval or intervals of the formation or formations then open to produc-  
 70 tion, for a term of one year and so long thereafter as oil and or gas is produced from the interval or inter-

1 vals of the formation or formations covered thereby, such lease to be on the form attached as Exhibit  
 2 "B". The assignments or leases so limited shall encompass the "drilling unit" upon which the well is  
 3 located. The payments by, and the assignments or leases to, the assignees shall be in a ratio based upon  
 4 the relationship of their respective percentages of participation in the Contract Area to the aggregate of  
 5 the percentages of participation in the Contract Area of all assignees. There shall be no readjustment  
 6 of interest in the remaining portion of the Contract Area.  
 7

8 Thereafter, abandoning parties shall have no further responsibility, liability, or interest in the op-  
 9 eration of or production from the well in the interval or intervals then open other than the royalties  
 10 retained in any lease made under the terms of this Article. Upon request, Operator shall continue to  
 11 operate the assigned well for the account of the non-abandoning parties at the rates and charges con-  
 12 templated by this agreement, plus any additional cost and charges which may arise as the result of  
 13 the separate ownership of the assigned well.  
 14

## 15 ARTICLE VII. 16 EXPENDITURES AND LIABILITY OF PARTIES

### 17 A. Liability of Parties:

18  
 19  
 20 The liability of the parties shall be several, not joint or collective. Each party shall be responsible  
 21 only for its obligations, and shall be liable only for its proportionate share of the costs of developing  
 22 and operating the Contract Area. Accordingly, the liens granted among the parties in Article VII.B. are  
 23 given to secure only the debts of each severally. It is not the intention of the parties to create, nor shall  
 24 this agreement be construed as creating, a mining or other partnership or association, or to render the  
 25 parties liable as partners.  
 26

### 27 B. Liens and Payment Defaults:

28  
 29 Each Non-Operator grants to Operator a lien upon its oil and gas rights in the Contract Area, and a  
 30 security interest in its share of oil and or gas when extracted and its interest in all equipment, to secure  
 31 payment of its share of expense, together with interest thereon at the rate provided in the Accounting  
 32 Procedure attached hereto as Exhibit "C". To the extent that Operator has a security interest under the  
 33 Uniform Commercial Code of the State, Operator shall be entitled to exercise the rights and remedies  
 34 of a secured party under the Code. The bringing of a suit and the obtaining of judgment by Operator  
 35 for the secured indebtedness shall not be deemed an election of remedies or otherwise affect the lien  
 36 rights or security interest as security for the payment thereof. In addition, upon default by any Non-  
 37 Operator in the payment of its share of expense, Operator shall have the right, without prejudice to  
 38 other rights or remedies, to collect from the purchaser the proceeds from the sale of such Non-Operator's  
 39 share of oil and or gas until the amount owed by such Non-Operator, plus interest has been paid. Each  
 40 purchaser shall be entitled to rely upon Operator's written statement concerning the amount of any de-  
 41 fault. Operator grants a like lien and security interest to the Non-Operators to secure payment of Op-  
 42 erator's proportionate share of expense.  
 43

44 If any party fails or is unable to pay its share of expense within sixty (60) days after rendition of  
 45 a statement therefor by Operator, the non-defaulting parties, including Operator, shall, upon request by  
 46 Operator, pay the unpaid amount in the proportion that the interest of each such party bears to the in-  
 47 terest of all such parties. Each party so paying its share of the unpaid amount shall, to obtain reimburse-  
 48 ment thereof, be subrogated to the security rights described in the foregoing paragraph.  
 49

### 50 C. Payments and Accounting:

51  
 52 Except as herein otherwise specifically provided, Operator shall promptly pay and discharge expenses  
 53 incurred in the development and operation of the Contract Area pursuant to this agreement and shall  
 54 charge each of the parties hereto with their respective proportionate shares upon the expense basis pro-  
 55 vided in the Accounting Procedure attached hereto as Exhibit "C". Operator shall keep an accurate  
 56 record of the joint account hereunder, showing expenses incurred and charges and credits made and  
 57 received.  
 58

59 Operator, at its election, shall have the right from time to time to demand and receive from the  
 60 other parties payment in advance of their respective shares of the estimated amount of the expense to  
 61 be incurred in operations hereunder during the next succeeding month, which right may be exercised only  
 62 by submission to each such party of an itemized statement of such estimated expense, together with  
 63 an invoice for its share thereof. Each such statement and invoice for the payment in advance of esti-  
 64 mated expense shall be submitted on or before the 20th day of the next preceding month. Each party  
 65 shall pay to Operator its proportionate share of such estimate within fifteen (15) days after such es-  
 66 timate and invoice is received. If any party fails to pay its share of said estimate within said time, the  
 67 amount due shall bear interest as provided in Exhibit "C" until paid. Proper adjustment shall be  
 68 made monthly between advances and actual expense to the end that each party shall bear and pay its  
 69 proportionate share of actual expenses incurred, and no more.  
 70

**ILLEGIBLE****D. Limitation of Expenditures:**

1. Drill or Deepen: Without the consent of all parties, no well shall be drilled or deepened, except any well drilled or deepened pursuant to the provisions of Article VI.B.2. of this Agreement, it being understood that the consent to the drilling or deepening shall include:

Option No. 1: All necessary expenditures for the drilling or deepening, testing, completing and equipping of the well, including necessary tankage and or surface facilities.

Option No. 2: All necessary expenditures for the drilling or deepening and testing of the well. When such well has reached its authorized depth, and all tests have been completed, Operator shall give immediate notice to the Non-Operators who have the right to participate in the completion costs. The parties receiving such notice shall have forty-eight (48) hours (exclusive of Saturday, Sunday and legal holidays) in which to elect to participate in the setting of casing and the completion attempt. Such election, when made, shall include consent to all necessary expenditures for the completing and equipping of such well, including necessary tankage and or surface facilities. Failure of any party receiving such notice to reply within the period above fixed shall constitute an election by that party not to participate in the cost of the completion attempt. If one or more, but less than all of the parties, elect to set pipe and to attempt a completion, the provisions of Article VI.B.2. hereof (the phrase "reworking, deepening or plugging back" as contained in Article VI.B.2. shall be deemed to include "completing") shall apply to the operations thereafter conducted by less than all parties.

2. Rework or Plug Back: Without the consent of all parties, no well shall be reworked or plugged back except a well reworked or plugged back pursuant to the provisions of Article VI.B.2. of this agreement, it being understood that the consent to the reworking or plugging back of a well shall include consent to all necessary expenditures in conducting such operations and completing and equipping of said well, including necessary tankage and or surface facilities.

3. Other Operations: Operator shall not undertake any single project reasonably estimated to require an expenditure in excess of Fifteen thousand----- Dollars (\$ 15,000.00 ) except in connection with a well, the drilling, reworking, deepening, completing, recompleting, or plugging back of which has been previously authorized by or pursuant to this agreement; provided, however, that, in case of explosion, fire, flood or other sudden emergency, whether of the same or different nature, Operator may take such steps and incur such expenses as in its opinion are required to deal with the emergency to safeguard life and property but Operator, as promptly as possible, shall report the emergency to the other parties. If Operator prepares "Authority for Expenditures" for its own use, Operator, upon request, shall furnish copies of its "Authority for Expenditures" for any single project costing in excess of Fifteen thousand----- Dollars (\$ 15,000.00 ).

**E. Royalties, Overriding Royalties and Other Payments:**

Each party shall pay or deliver, or cause to be paid or delivered, all royalties to the extent of one-eighth (1/8) due on its share of production and shall hold the other parties free from any liability therefor. If the interest of any party in any oil and gas lease covered by this agreement is subject to any royalty, overriding royalty, production payment, or other charge over and above the aforesaid royalty, such party shall assume and alone bear all such obligations and shall account for or cause to be accounted for, such interest to the owners thereof.

No party shall ever be responsible, on any price basis higher than the price received by such party, to any other party's lessor or royalty owner; and if any such other party's lessor or royalty owner should demand and receive settlements on a higher price basis, the party contributing such lease shall bear the royalty burden insofar as such higher price is concerned.

**F. Rentals, Shut-in Well Payments and Minimum Royalties:**

Rentals, shut-in well payments and minimum royalties which may be required under the terms of any lease shall be paid by the party or parties who subjected such lease to this agreement at its or their expense. In the event two or more parties own and have contributed interests in the same lease to this agreement, such parties may designate one of such parties to make said payments for and on behalf of all such parties. Any party may request, and shall be entitled to receive, proper evidence of all such payments. In the event of failure to make proper payment of any rental, shut-in well payment or minimum royalty through mistake or oversight where such payment is required to continue the lease in force, any loss which results from such non-payment shall be borne in accordance with the provisions of Article IV.B.2.

Operator shall notify Non-Operator of the anticipated completion of a shut-in gas well, or the shutting in or return to production of a producing gas well, at least five (5) days (excluding Saturday, Sunday and holidays), or at the earliest opportunity permitted by circumstances, prior to taking such action, but assumes no liability for failure to do so. In the event of failure by Operator to so notify Non-Operator, the loss of any lease contributed hereto by Non-Operator for failure to make timely payments

1 of any shut-in well payment shall be borne jointly by the parties hereto under the provisions of Article  
2 IV.B.3.

3  
4 **G. Taxes:**

5  
6 Beginning with the first calendar year after the effective date hereof, Operator shall render for ad  
7 valorem taxation all property subject to this agreement which by law should be rendered for such  
8 taxes, and it shall pay all such taxes assessed thereon before they become delinquent. Prior to the ren-  
9 dition date, each Non-Operator shall furnish Operator information as to burdens (to include, but not be  
10 limited to, royalties, overriding royalties and production payments) on leases and oil and gas interests con-  
11 tributed by such Non-Operator. If the assessed valuation of any leasehold estate is reduced by reason of its  
12 being subject to outstanding excess royalties, overriding royalties or production payments, the reduction in  
13 ad valorem taxes resulting therefrom shall inure to the benefit of the owner or owners of such leasehold  
14 estate, and Operator shall adjust the charge to such owner or owners so as to reflect the benefit of such  
15 reduction. Operator shall bill other parties for their proportionate share of all tax payments in the man-  
16 ner provided in Exhibit "C". See Article XV.D. for additional provisions

17  
18 If Operator considers any tax assessment improper, Operator may, at its discretion, protest within  
19 the time and manner prescribed by law, and prosecute the protest to a final determination, unless all  
20 parties agree to abandon the protest prior to final determination. During the pendency of administrative  
21 or judicial proceedings, Operator may elect to pay, under protest, all such taxes and any interest and  
22 penalty. When any such protested assessment shall have been finally determined, Operator shall pay  
23 the tax for the joint account, together with any interest and penalty accrued, and the total cost shall then  
24 be assessed against the parties, and be paid by them, as provided in Exhibit "C".

25  
26 Each party shall pay or cause to be paid all production, severance, gathering and other taxes im-  
27 posed upon or with respect to the production or handling of such party's share of oil and or gas pro-  
28 duced under the terms of this agreement.

29  
30 **H. Insurance:**

31  
32 At all times while operations are conducted hereunder, Operator shall comply with the Workmen's  
33 Compensation Law of the State where the operations are being conducted; provided, however, that Op-  
34 erator may be a self-insurer for liability under said compensation laws in which event the only charge  
35 that shall be made to the joint account shall be an amount equivalent to the premium which would have  
36 been paid had such insurance been obtained. Operator shall also carry or provide insurance for the  
37 benefit of the joint account of the parties as outlined in Exhibit "D", attached to and made a part hereof.  
38 Operator shall require all contractors engaged in work on or for the Contract Area to comply with the  
39 Workmen's Compensation Law of the State where the operations are being conducted and to maintain  
40 such other insurance as Operator may require.

41  
42 In the event Automobile Public Liability Insurance is specified in said Exhibit "D", or subsequently  
43 receives the approval of the parties, no direct charge shall be made by Operator for premiums paid for  
44 such insurance for Operator's fully owned automotive equipment.

45  
46 **ARTICLE VIII.**  
47 **ACQUISITION, MAINTENANCE OR TRANSFER OF INTEREST**

48  
49 **A. Surrender of Leases:**

50  
51 The leases covered by this agreement, insofar as they embrace acreage in the Contract Area, shall  
52 not be surrendered in whole or in part unless all parties consent thereto.

53  
54 However, should any party desire to surrender its interest in any lease or in any portion thereof, and  
55 other parties do not agree or consent thereto, the party desiring to surrender shall assign, without express  
56 or implied warranty of title, all of its interest in such lease, or portion thereof, and any well, material and  
57 equipment which may be located thereon and any rights in production thereafter secured, to the parties  
58 not desiring to surrender it. If the interest of the assigning party includes an oil and gas interest, the as-  
59 signing party shall execute and deliver to the party or parties not desiring to surrender an oil and gas  
60 lease covering such oil and gas interest for a term of one year and so long thereafter as oil and or gas  
61 is produced from the land covered thereby, such lease to be on the form attached hereto as Exhibit "B".  
62 Upon such assignment, the assigning party shall be relieved from all obligations thereafter accruing,  
63 but not theretofore accrued, with respect to the acreage assigned and the operation of any well thereon,  
64 and the assigning party shall have no further interest in the lease assigned and its equipment and pro-  
65 duction other than the royalties retained in any lease made under the terms of this Article. The parties  
66 assignee shall pay to the party assignor the reasonable salvage value of the latter's interest in any wells  
67 and equipment on the assigned acreage. The value of all material shall be determined in accordance  
68 with the provisions of Exhibit "C", less the estimated cost of salvaging and the estimated cost of plug-  
69 ging and abandoning. If the assignment is in favor of more than one party, the assigned interest shall  
70

1 be shared by the parties assignee in the proportions that the interest of each bears to the interest of all  
 2 parties assignee.

3  
 4 Any assignment or surrender made under this provision shall not reduce or change the assignor's or  
 5 surrendering parties' interest, as it was immediately before the assignment, in the balance of the Contract  
 6 Area; and the acreage assigned or surrendered, and subsequent operations thereon, shall not thereafter  
 7 be subject to the terms and provisions of this agreement.

8  
 9 **B. Renewal or Extension of Leases:**

10  
 11 If any party secures a renewal of any oil and gas lease subject to this Agreement, all other parties  
 12 shall be notified promptly, and shall have the right for a period of thirty (30) days following receipt  
 13 of such notice in which to elect to participate in the ownership of the renewal lease, insofar as such  
 14 lease affects lands within the Contract Area, by paying to the party who acquired it their several proper  
 15 proportionate shares of the acquisition cost allocated to that part of such lease within the Contract Area,  
 16 which shall be in proportion to the interests held at that time by the parties in the Contract Area.

17  
 18 If some, but less than all, of the parties elect to participate in the purchase of a renewal lease, it  
 19 shall be owned by the parties who elect to participate therein, in a ratio based upon the relationship of  
 20 their respective percentage of participation in the Contract Area to the aggregate of the percentages  
 21 of participation in the Contract Area of all parties participating in the purchase of such renewal lease.  
 22 Any renewal lease in which less than all parties elect to participate shall not be subject to this agreement.

23  
 24 Each party who participates in the purchase of a renewal lease shall be given an assignment of its  
 25 proportionate interest therein by the acquiring party.

26  
 27 The provisions of this Article shall apply to renewal leases whether they are for the entire interest  
 28 covered by the expiring lease or cover only a portion of its area or an interest therein. Any renewal lease  
 29 taken before the expiration of its predecessor lease, or taken or contracted for within six (6) months after  
 30 the expiration of the existing lease shall be subject to this provision; but any lease taken or contracted  
 31 for more than six (6) months after the expiration of an existing lease shall not be deemed a renewal  
 32 lease and shall not be subject to the provisions of this agreement.

33  
 34 The provisions in this Article shall apply also and in like manner to extensions of oil and gas  
 35 leases. See Article XV.E for additional provisions.

36  
 37 **C. Acreage or Cash Contributions:**

38  
 39 While this agreement is in force, if any party contracts for a contribution of cash toward the drilling  
 40 of a well or any other operation on the Contract Area, such contribution shall be paid to the party who  
 41 conducted the drilling or other operation and shall be applied by it against the cost of such drilling or  
 42 other operation. If the contribution be in the form of acreage, the party to whom the contribution is  
 43 made shall promptly tender an assignment of the acreage, without warranty of title, to the Drilling  
 44 Parties in the proportions said Drilling Parties shared the cost of drilling the well. If all parties hereto  
 45 are Drilling Parties and accept such tender, such acreage shall become a part of the Contract Area and  
 46 be governed by the provisions of this agreement. If less than all parties hereto are Drilling Parties and  
 47 accept such tender, such acreage shall not become a part of the Contract Area. Each party shall prompt-  
 48 ly notify all other parties of all acreage or money contributions it may obtain in support of any well or  
 49 any other operation on the Contract Area.

50  
 51 If any party contracts for any consideration relating to disposition of such party's share of substances  
 52 produced hereunder, such consideration shall not be deemed a contribution as contemplated in this  
 53 Article VIII.C.

54  
 55 **D. Subsequently Created Interest:**

56  
 57 Notwithstanding the provisions of Article VIII.E and VIII.G., if any party hereto shall, subsequent  
 58 to execution of this agreement, create an overriding royalty, production payment, or net proceeds inter-  
 59 est, which such interests are hereinafter referred to as "subsequently created interest", such subsequently  
 60 created interest shall be specifically made subject to all of the terms and provisions of this agreement, as  
 61 follows:

62  
 63 1. If non-consent operations are conducted pursuant to any provision of this agreement, and the  
 64 party conducting such operations becomes entitled to receive the production attributable to the interest  
 65 out of which the subsequently created interest is derived, such party shall receive same free and clear  
 66 of such subsequently created interest. The party creating same shall bear and pay all such subsequently  
 67 created interests and shall indemnify and hold the other parties hereto free and harmless from any and  
 68 all liability resulting therefrom.

69  
 70

2. If the owner of the interest from which the subsequently created interest is derived (1) fails to pay, when due, its share of expenses chargeable hereunder, or (2) elects to abandon a well under provisions of Article VI.E. hereof, or (3) elects to surrender a lease under provisions of Article VIII.A. hereof, the subsequently created interest shall be chargeable with the pro rata portion of all expenses hereunder in the same manner as if such interest were a working interest. For purposes of collecting such chargeable expenses, the party or parties who receive assignments as a result of (2) or (3) above shall have the right to enforce all provisions of Article VII.B. hereof against such subsequently created interest.

**E. Maintenance of Uniform Interest:**

For the purpose of maintaining uniformity of ownership in the oil and gas leasehold interests covered by this agreement, and notwithstanding any other provisions to the contrary, no party shall sell, encumber, transfer or make other disposition of its interest in the leases embraced within the Contract Area and in wells, equipment and production unless such disposition covers either:

1. the entire interest of the party in all leases and equipment and production; or
2. an equal undivided interest in all leases and equipment and production in the Contract Area.

Every such 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 right of the other parties.

If, at any time the interest of any party is divided among and owned by four or more co-owners, Operator, at its discretion, may 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 expenses, and to deal generally with, and with power to bind, the co-owners of such party's interests within the scope of the operations embraced in this agreement; however, all such co-owners shall have the right to enter into and execute all contracts or agreements for the disposition of their respective shares of the oil and gas produced from the Contract Area and they shall have the right to receive, separately, payment of the sale proceeds hereof.

**F. Waiver of Right to Partition:**

If permitted by the laws of the state or states in which the property covered hereby is located, each party hereto owning an undivided interest in the Contract Area waives any and all rights it may have to partition and have set aside to it in severalty its undivided interest therein.

~~**G. Preferential Right to Purchase:**~~

~~Should any party desire to sell all or any part of its interest under this agreement or its rights and interests in the Contract Area, it shall promptly give written notice to the other parties, with full information concerning the proposed sale, which shall include the name and address of the prospective purchaser (who must be ready, willing and able to purchase), the purchase price and all other terms of the offer. The other parties shall then have an optional prior right, for a period of ten (10) days after receipt of the notice, to purchase on the same terms and conditions the interest which the other party proposes to sell; and, if this optional right is exercised, the purchasing parties shall share the purchased interest in the proportions that the interest of each bears to the total interest of all purchasing parties. However, there shall be no preferential right to purchase in those cases where any party wishes to mortgage its interests, or to dispose of its interests by merger, reorganization, consolidation, or sale of all or substantially all of its assets to a subsidiary or parent company or to a subsidiary of a parent company, or to any company in which it has an interest.~~

**ARTICLE IX.  
INTERNAL REVENUE CODE ELECTION**

This agreement is not intended to create, and shall not be construed to create, a relationship of partnership or an association for profit between or among the parties hereto. Notwithstanding any provisions herein that the rights and liabilities hereunder are several and not joint or collective, or that this agreement and operations hereunder shall not constitute a partnership, if, for Federal income tax purposes, this agreement and the operations hereunder are regarded as a partnership, each party hereby affected elects to 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 the Code and the regulations promulgated thereunder. Operator is authorized and directed to execute on behalf of each party hereby affected 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 the data required by Federal Regulations 1.761. Should there be any requirement that each party hereby affected give further evidence of this election, each such party shall execute such documents and furnish such other evidence as may be required by the Federal Internal Revenue Service or as may be necessary to evidence this election. No

1 such party shall give any notices or take any other action inconsistent with the election made hereby.  
2 If any present or future income tax laws of the state or states in which the Contract Area is located or  
3 any future income tax laws of the United States contain provisions similar to those in Subchapter "K",  
4 Chapter I, Subtitle "A", of the Internal Revenue Code of 1954, under which an election similar to that  
5 provided by Section 761 of the Code is permitted, each party hereby affected shall make such election as  
6 may be permitted or required by such laws. In making the foregoing election, each such party states that  
7 the income derived by such party from Operations hereunder can be adequately determined without the  
8 computation of partnership taxable income.

9  
10 **ARTICLE X.**  
11 **CLAIMS AND LAWSUITS**  
12

13 Operator may settle any single damage claim or suit arising from operations hereunder if the ex-  
14 penditure does not exceed Four thousand----- Dollars  
15 (\$ 4,000.00 ) and if the payment is in complete settlement of such claim or suit. If the amount  
16 required for settlement exceeds the above amount, the parties hereto shall assume and take over the  
17 further handling of the claim or suit, unless such authority is delegated to Operator. All costs and ex-  
18 pense of handling, settling, or otherwise discharging such claim or suit shall be at the joint expense  
19 of the parties. If a claim is made against any party or if any party is sued on account of any matter  
20 arising from operations hereunder over which such individual has no control because of the rights given  
21 Operator by this agreement, the party shall immediately notify Operator, and the claim or suit shall  
22 be treated as any other claim or suit involving operations hereunder.

23  
24 **ARTICLE XI.**  
25 **FORCE MAJEURE**  
26

27 If any party is rendered unable, wholly or in part, by force majeure to carry out its obligations  
28 under this agreement, other than the obligation to make money payments, that party shall give to all  
29 other parties prompt written notice of the force majeure with reasonably full particulars concerning it;  
30 thereupon, the obligations of the party giving the notice, so far as they are affected by the force majeure,  
31 shall be suspended during, but no longer than, the continuance of the force majeure. The affected party  
32 shall use all reasonable diligence to remove the force majeure situation as quickly as practicable.

33  
34 The requirement that any force majeure shall be remedied with all reasonable dispatch shall not  
35 require the settlement of strikes, lockouts, or other labor difficulty by the party involved, contrary to its  
36 wishes; how all such difficulties shall be handled shall be entirely within the discretion of the party  
37 concerned.

38  
39 The term "force majeure", as here employed, shall mean an act of God, strike, lockout, or other  
40 industrial disturbance, act of the public enemy, war, blockade, public riot, lightning, fire, storm, flood,  
41 explosion, governmental action, governmental delay, restraint or inaction, unavailability of equipment,  
42 and any other cause, whether of the kind specifically enumerated above or otherwise, which is not  
43 reasonably within the control of the party claiming suspension.

44  
45 **ARTICLE XII.**  
46 **NOTICES**  
47

48 All notices authorized or required between the parties, and required by any of the provisions of  
49 this agreement, unless otherwise specifically provided, shall be given in writing by United States mail  
50 or Western Union telegram, postage or charges prepaid, or by teletype, and addressed to the party to  
51 whom the notice is given at the addresses listed on Exhibit "A". The originating notice given under any  
52 provision hereof shall be deemed given only when received by the party to whom such notice is directed,  
53 and the time for such party to give any notice in response thereto shall run from the date the originat-  
54 ing notice is received. The second or any responsive notice shall be deemed given when deposited in  
55 the United States mail or with the Western Union Telegraph Company, with postage or charges prepaid,  
56 or when sent by teletype. Each party shall have the right to change its address at any time, and from  
57 time to time, by giving written notice hereof to all other parties.

58  
59 **ARTICLE XIII.**  
60 **TERM OF AGREEMENT**  
61

62 This agreement shall remain in full force and effect as to the oil and gas leases and/or oil and gas in-  
63 terests subjected hereto for the period of time selected below; provided, however, no party hereto shall  
64 ever be construed as having any right, title or interest in or to any lease, or oil and gas interest con-  
65 tributed by any other party beyond the term of this agreement.

66  
67 Option No. 1: So long as any of the oil and gas leases subject to this agreement remain or are con-  
68 tinued in force as to any part of the Contract Area, whether by production, extension, renewal or other-  
69 wise, and/or so long as oil and/or gas production continues from any lease or oil and gas interest,  
70

1  Option No. 2: In the event the well described in Article VI.A., or any subsequent well drilled  
 2 under any provision of this agreement, results in production of oil and or gas in paying quantities, this  
 3 agreement shall continue in force so long as any such well or wells produce, or are capable of produc-  
 4 tion, and for an additional period of 120 days from cessation of all production; provided, however,  
 5 if, prior to the expiration of such additional period, one or more of the parties hereto are engaged in  
 6 drilling or reworking a well or wells hereunder, this agreement shall continue in force until such op-  
 7 erations have been completed and if production results therefrom, this agreement shall continue in  
 8 force as provided herein. In the event the well described in Article VI.A., or any subsequent well  
 9 drilled hereunder, results in a dry hole, and no other well is producing, or capable of producing oil  
 10 and or gas from the Contract Area, this agreement shall terminate unless drilling or reworking opera-  
 11 tions are commenced within 120 days from the date of abandonment of said well.  
 12

13 It is agreed, however, that the termination of this agreement shall not relieve any party hereto from  
 14 any liability which has accrued or attached prior to the date of such termination.  
 15

16 **ARTICLE XIV.**  
 17 **COMPLIANCE WITH LAWS AND REGULATIONS**  
 18

19 **A. Laws, Regulations and Orders:**  
 20

21 This agreement shall be subject to the conservation laws of the state in which the committed  
 22 acreage is located, to the valid rules, regulations, and orders of any duly constituted regulatory body of  
 23 said state; and to all other applicable federal, state, and local laws, ordinances, rules, regulations, and  
 24 orders.  
 25

26 **B. Governing Law:**  
 27

28 The essential validity of this agreement and all matters pertaining thereto, including, but not lim-  
 29 ited to, matters of performance, non-performance, breach, remedies, procedures, rights, duties and in-  
 30 terpretation or construction, shall be governed and determined by the law of the state in which the  
 31 Contract Area is located. If the Contract Area is in two or more states, the law of the state where most  
 32 of the land in the Contract Area is located shall govern.  
 33

34 **ARTICLE XV.**  
 35 **OTHER PROVISIONS**  
 36

37 **A. Sale of Gas Production:**  
 38

39 It is recognized by the parties hereto that in addition to each party's share  
 40 of working interest production as shown in Exhibit "A", such party shall have the  
 41 right, subject to existing contracts, to market the royalty gas attributable to  
 42 each lease which it contributes to the Contract Area and to receive payments due  
 43 for such royalty gas produced from or allocated to such lease or leases. It is  
 44 agreed that, regardless of whether each party markets or contracts for its share  
 45 of gas, including the royalty gas under the leases which it contributed to the  
 46 Contract Area, such party agrees to pay or cause to be paid to the royalty owners  
 47 under its lease or leases the proceeds attributable to their respective royalty  
 48 interest and to hold all other parties hereto harmless for its failure to do so.  
 49

50 **B. Billing Additional Interests:**  
 51

52 Notwithstanding the provisions of this agreement and of the accounting procedure  
 53 attached as Exhibit "C", the Parties to this agreement specifically agree that in  
 54 no event during the term of this contract shall Operator be required to make more  
 55 than one billing for the entire interest credited to each Party on Exhibit "A". It  
 56 is further agreed that if any Party to this agreement (hereinafter referred to as  
 57 "Selling Party") disposes of part of the interest credited to it on Exhibit "A", the  
 58 Selling Party shall be solely responsible for billing its assignee or assignees,  
 59 and shall remain primarily liable to the other parties for the interest or interests  
 60 assigned and shall make prompt payment to Operator for the entire amount of state-  
 61 ments and billing rendered to it. It is further understood and agreed that if Selling  
 62 Party disposes of all its interest as set out on Exhibit "A", whether to one or  
 63 several assignees, Operator shall continue to issue statements and billings to the  
 64 Selling Party for the interest conveyed until such time as Selling Party has  
 65 designated and qualified one assignee to receive the billing for the entire  
 66 interest. In order to qualify one assignee to receive the billing for the entire  
 67 interest credited to Selling Party on Exhibit "A", Selling Party shall furnish  
 68 to Operator the following:  
 69  
 70

1. Written notice of the conveyance and photostatic or certified copies of the assignments by which the transfer was made.

2. The name of the assignee to be billed and a written statement signed by the assignee to be billed in which it consents to receive statements and billings for the entire interest credited to Selling Party on Exhibit "A" hereof; and, further, consents to handle any necessary sub-billings in the event it does not own the entire interest credited to Selling Party on Exhibit "A".

C. Disbursement of Royalties:

If a purchaser of any oil, gas or other hydrocarbons produced from the Contract Area declines to make disbursements of all royalties, overriding royalties, working interests, and other payments out of, or with respect to, production revenues which are payable on the Contract Area, Operator may, at its option, from time to time, make disbursements on behalf of any Non-Operator who requests in writing that Operator do so. Each Non-Operator for whom such disbursement is made shall furnish Operator with the following:

1. Such documents as may be necessary in the opinion of Operator to enable Operator to receive all payments for oil, gas or other hydrocarbons directly from the purchaser thereof.

2. An initial list of names, addresses, and interest (to a seven place decimal), on a tract, unit, purchase contract, or other such basis as, in the opinion of Operator, is necessary for efficient administration, for all royalty, overriding royalty and other interest owners who are entitled to proceeds from the sale of production attributable to such Non-Operator's interest. Also, any changes to the initial list shall be furnished promptly to Operator in writing.

Operator will use its best efforts to make disbursements correctly, but will be liable for incorrect disbursement only in the event of gross negligence or willful misconduct. Any Non-Operator for whom such disbursements are made hereby agrees to indemnify and hold harmless Operator for any loss, including court costs and attorney's fees, which may be incurred as a result of Operator's making such disbursements in the manner prescribed by Non-Operator.

D. Article VII.G., Addition:

If the Operator is required hereunder to pay ad valorem taxes based in whole or in part upon separate valuations of each party's working interest, then notwithstanding anything to the contrary herein, charges to the joint account shall be made and paid by the parties hereto in accordance with the percentage of tax value generated by each party's working interest.

E. Article VIII.B., Addition:

Notwithstanding anything to the contrary contained herein, each party committing a lease or leases to this agreement shall have the option upon the expiration of each lease to renew or extend such lease and to bear the renewal or extension costs and expenses and thereby retain its original interest and title in said lease. By exercising such option, the parties' working interests shall remain unchanged. If the original lease owner does not exercise its option within sixty (60) days after the expiration date of the original lease, the renewal or extension lease will then be subject to the terms of this article as written above. If any working interest owner other than the original lease owner renews or extends the lease, the renewing or extending party shall furnish the original lease owner an itemized statement of the complete renewal or extension costs and expenses of such lease. The original lease owner shall have sixty (60) days after the receipt of such itemized statement to reimburse the renewing or extending party in full. Failure of the original lease owner to do so shall result in the forfeiture of its option hereunder. The provisions hereof shall only apply to leases or portions of leases located in the Contract Area.

F. As between the interest of TXO and FINA, this Agreement shall be subject and subordinate to that Certain Oil & Gas Lease Acquisition and Development Agreement dated October 22, 1982, between TXO PRODUCTION CORP. and APCOT-FINADEL JOINT VENTURE. In the event of a conflict between this agreement and the Oil & Gas Lease Acquisition and Development Agreement, the terms of the Oil and Gas Lease Acquisition and Development Agreement shall prevail. Upon termination of the Oil & Gas Lease Acquisition and Development Agreement, this Agreement shall be amended as between TXO and FINA in the manner provided in Article XXI of the Oil & Gas Lease Acquisition and Development Agreement.

G. As between APCOT-FINADEL JOINT VENTURE and any other party hereto the non-consent penalties specified in Article VI.B.2(a) shall be 100%/100%; and the non-consent penalties specified in Article VI.B.2(b) shall be 300%/300% as to all wells drilled to a depth of 10,000 feet subsurface or less, and 400%/400% as to all wells drilled to a depth greater than 10,000 feet subsurface.

H. It is understood by all parties that the Sprinkle Federal #2 well, is to be a reentry and deepening of the Walker Federal #1 well which was a dry hole drilled to a total depth of 4,270 feet by John H. Hill, Operator. It is further understood and agreed to by all parties hereto that, should TXO encounter impenetrable conditions or mechanical problems during the reentry and deepening of the said well and be required to move the rig and commence the drilling of a new well at a location within a 100' radius of the initial location, TXO shall notify all non-operators of its intention to move the rig and commence the drilling of a new well along with the estimated cost to drill and complete said well. This notice may be given by telephone and all non-operators shall be limited to a response period of 48 hours exclusive of Saturday, Sunday, or legal holidays. Failure of a party receiving such notice to reply within period above fixed shall constitute an election by that party not to participate in the cost of the drilling and completing of the new well, and any non-participating interest shall be subject to the non-consent penalties specified in Article VI.B.2(a) and (b). Any notice or response given by telephone shall be promptly confirmed in writing.

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ARTICLE XVI  
MISCELLANEOUS

This agreement shall be binding upon and shall inure to the benefit of the parties hereto and to their respective heirs, devisees, legal representatives, successors and assigns.

This instrument may be executed in any number of counterparts, each of which shall be considered an original for all purposes.

IN WITNESS WHEREOF, this agreement shall be effective as of \_\_\_\_\_ day of \_\_\_\_\_, 19\_\_\_\_.

OPERATOR

TXO PRODUCTION CORP.

By: *John D. Huppler* *RTH*  
John D. Huppler  
Senior Vice President

NON-OPERATORS

ATTEST:

*R. Michael Casler*  
Secretary

PETRO ATLAS CORPORATION

By: *James L. Harden III*  
James L. Harden III  
Title: President

THE STATE OF TEXAS §

COUNTY OF MIDLAND §

The foregoing instrument was acknowledged before me this 24<sup>th</sup> day of September, 1985, by JOHN D. HUPPLER, Senior Vice President, of TXO PRODUCTION CORP., a Delaware corporation, on behalf of said corporation.

My Commission Expires:

7-29-87

David M. Handley  
Notary Public in and for  
The State of Texas

STATE OF COLORADO §

COUNTY OF DENVER §

The foregoing instrument was acknowledged before me on this 25th day of September, 1985, by James L. Harden III, President of Petro Atlas Corporation a Colorado corporation, on behalf of said corporation.

My Commission Expires:

December 16, 1985

\_\_\_\_\_  
Notary Public in and for  
Denver County, Colorado

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ARTICLE XVI  
MISCELLANEOUS

This agreement shall be binding upon and shall inure to the benefit of the parties hereto and to their respective heirs, devisees, legal representatives, successors and assigns.

This instrument may be executed in any number of counterparts, each of which shall be considered an original for all purposes.

IN WITNESS WHEREOF, this agreement shall be effective as of \_\_\_\_\_ day of \_\_\_\_\_, 19\_\_\_\_.

OPERATOR

TXO PRODUCTION CORP.

By: *[Signature]* *DMH*  
John D. Huppler  
Senior Vice President

NON-OPERATORS

PETRO ATLAS CORPORATION

By: \_\_\_\_\_

Title: \_\_\_\_\_

THE STATE OF TEXAS §

COUNTY OF MIDLAND §

The foregoing instrument was acknowledged before me this 24<sup>th</sup> day of September, 1985, by JOHN D. HUPPLER, Senior Vice President, of TXO PRODUCTION CORP., a Delaware corporation, on behalf of said corporation.

My Commission Expires:

7-29-87

David M. Hundley  
Notary Public in and for  
The State of Texas

STATE OF \_\_\_\_\_ §

COUNTY OF \_\_\_\_\_ §

The foregoing instrument was acknowledged before me on this \_\_\_\_\_ day of \_\_\_\_\_, 198\_\_\_\_, by \_\_\_\_\_, \_\_\_\_\_ of Petro Atlas Corporation a \_\_\_\_\_ corporation, on behalf of said corporation.

My Commission Expires:

\_\_\_\_\_

\_\_\_\_\_  
Notary Public in and for  
\_\_\_\_\_ County, \_\_\_\_\_

EXHIBIT "A"

Attached to and made a part of that certain Joint Operating Agreement dated September 23, 1985 by and between TXO Production Corp., Operator and Petro Atlas, Non-Operator.

TRACT I:

CONTRACT AREA:

NW/4 NW/4 Section 26, T-18-S, R-32-E  
Lea County, New Mexico

DEPTH LIMITATIONS:

From 4825' below the surface to 13,450'

TRACT II:

CONTRACT AREA:

NE/4 NW/4 and S/2 NW/4 Section 26, T-18-S, R-32-E, Lea County, New Mexico

DEPTH LIMITATIONS:

From 4825' below the surface to 8800' or a depth sufficient to test the Bone Spring formation

NAMES, ADDRESSES AND PERCENTAGES OF THE PARTIES:

TRACT I:	<u>Before Payout</u>	<u>*After Payout*</u>
TXO Production Corp. et al 900 Wilco Bldg. Midland, TX 79701	1.0000000	.953125
Petro Atlas Corporation 999 18th Street, Suite 2908 Denver, Colorado 80207	-0-	.046875
Total	1.0000000	1.0000000

  

TRACT 2:	<u>Before Payout</u>	<u>After Payout</u>
TXO Production Corp. 900 Wilco Bldg. Midland, Texas 79701	.953125	.953125
Petro Atlas Corporation 999 18th Street, Suite 2908 Denver, Colorado 80533	.046875	.046875
Total	1.0000000	1.0000000

OIL AND GAS LEASE SUBJECT TO THIS AGREEMENT:

NM 40452

Lessor: United States - Department of the Interior - BLM

Lessor: Thomas Curran

Effective dated: January 1, 1973

Description: NM 40452 segregated out of NM 17235

T-18-S, R-32-E, N.M.P.M.

Section 1: SE/4 NE/4

Section 11: N/2 SW/4; SW/4 SW/4; SW/4 SE/4

Section 12: SE/4 NW/4; SE/4

Section 14: N/2; NE/4 SW/4; SE/4

Section 15: N/2 N/2; S/2 NE/4

Section 26: NW/4

Section 31: Lot 1

1,361.18 acres

Recorded: Book 284, Page 620, Oil & Gas Lease Records  
Lea County, New Mexico

\*Assuming Petro Atlas Corporation elects to convert its overriding royalty interest to a working interest at payout of the Sprinkle Federal #1 well.