

## UNIT OPERATING AGREEMENT

### TAOS TROUGH UNIT AREA

COUNTIES OF COLFAX, MORA AND TAOS

**STATE OF NEW MEXICO**

#### TABLE OF CONTENTS

	Page
Preliminary Recitals .....	1
<b>ARTICLE 1—DEFINITIONS</b>	
Section 1.1 Definitions .....	1
<b>ARTICLE 2—EXHIBITS</b>	
Section 2.1 Exhibits .....	2
<b>ARTICLE 3—INITIAL TEST WELL</b>	
Section 3.1 Location .....	2
Section 3.2 Costs of Drilling .....	2
<b>ARTICLE 4—SUBSEQUENT TEST WELLS</b>	
Section 4.1 Right to Drill .....	2
<b>ARTICLE 5—ESTABLISHMENT, REVISION, AND CONSOLIDATION OF PARTICIPATING AREAS</b>	
Section 5.1 Proposal .....	2
Section 5.2 Objections to Proposal .....	2
Section 5.3 Revised Proposal .....	2
Section 5.4 Rejection of Proposal .....	3
Section 5.5 Consolidation .....	3
<b>ARTICLE 6—APPORTIONMENT OF COSTS AND OWNERSHIP AND DISPOSITION OF PRODUCTION AND PROPERTY</b>	
Section 6.1 Apportionment and Ownership Within Participating Area ..	3
A. Costs .....	3
B. Production .....	3
C. Property .....	3
Section 6.2 Ownership and Costs Outside Participating Area .....	3
A. When All Drilling Block Parties Participate .....	3
B. When Less Than All Drilling Block Parties Participate .....	3
Section 6.3 Cost Liability of Subsequently Created Interests .....	3
Section 6.4 Taking in Kind .....	3
Section 6.5 Failure to Take in Kind .....	3
Section 6.6 Surplus Materials and Equipment .....	4
<b>ARTICLE 7—PLANS OF DEVELOPMENT</b>	
Section 7.1 Submittal of Plans .....	4
Section 7.2 Proposal .....	4
Section 7.3 Objections to Plan .....	4
Section 7.4 Revised Plan .....	4
Section 7.5 Rejection of Plan .....	4
Section 7.6 Notice of Approval or Disapproval .....	4
Section 7.7 Supplemental Plans .....	4
Section 7.8 Cessation of Operations Under the Plan .....	4



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BEFORE EXAMINER STOGNER

Oil CONSERVATION DIVISION

EXHIBIT NO. 5

DATE NO.

## ARTICLE 8—DEVELOPMENT WELLS

Section 8.1	Purpose and Procedure .....	4
Section 8.2	Drilling .....	4
	A. Approval Required .....	4
	B. Notice of Proposed Drilling .....	5
	C. Response to Notice .....	5
	D. Notice of Election to Proceed .....	5
	E. Subsequent Election .....	5
	F. Effect of Election .....	5
	G. Rights and Obligations of Drilling Party and Non-Drilling Party .....	5
Section 8.3	Attempted Completion .....	5
	A. Notice by Unit Operator .....	5
	B. Right to Attempt Completion .....	5
	C. Time and Manner of Initiating Proposal .....	5
	D. Election .....	5
	E. Effect of Election .....	5
	F. Rights and Obligations of Completing Party and Non-Completing Party .....	5
	G. Notice Prior to Plugging .....	5

## ARTICLE 9—EXPLORATORY WELLS

Section 9.1	Purpose and Procedure .....	6
Section 9.2	Drilling .....	6
	A. Notice of Proposed Drilling .....	6
	B. Basis of Participation .....	6
	C. Exclusion of Land From Proposed Drilling Block .....	6
	D. Preliminary Notice to Join in Drilling .....	6
	E. Notice of Election to Proceed .....	6
	F. Subsequent Election .....	6
	G. Effect of Election .....	6
	H. Rights and Obligations of Drilling Party and Non-Drilling Party .....	6
Section 9.3	Attempted Completion .....	6
	A. Notice by Unit Operator .....	6
	B. Right to Attempt Completion .....	6
	C. Time and Manner of Initiating Proposal .....	7
	D. Election .....	7
	E. Effect of Election .....	7
	F. Rights and Obligations of Completing Party and Non-Completing Party .....	7
	G. Notice Prior to Plugging .....	7

## ARTICLE 10—REQUIRED WELLS

Section 10.1	Definition .....	7
Section 10.2	Election to Drill .....	7
Section 10.3	Alternatives to Drilling .....	7
	A. Compensatory Royalties .....	7
	B. Contraction .....	7
	C. Termination .....	7
Section 10.4	Required Drilling .....	7
	A. Development Well .....	7
	B. Exploratory Well .....	7

## ARTICLE 11—DEEPENING, PLUGGING BACK, AND ABANDONMENT

Section 11.1	Attempted Deepening or Plugging Back .....	8
	A. Notice by Unit Operator .....	8
	B. Right to Initiate Proposal .....	8
	C. Right to Participate .....	8
	D. Time and Manner of Initiating Proposal .....	8
	E. Election .....	8
	F. Effect of Election .....	8
	G. Rights and Obligations of Participating Party and Non-Participating Party .....	8
Section 11.2	Deepening or Plugging Back to Participating Area .....	8
Section 11.3	Conflicts .....	8
Section 11.4	Attempted Completion .....	8
Section 11.5	Abandonment of Producing Wells .....	9
	A. Consent Required .....	9
	B. Abandonment Procedure .....	9

C. Rights and Obligations of Non-Abandoning Party .....	9
D. Option to Repurchase Materials .....	9
Section 11.6 Deepening or Plugging Back Abandoned Producing Wells .....	9

## ARTICLE 12—RIGHTS AND OBLIGATIONS OF DRILLING PARTY AND NON-DRILLING PARTY

Section 12.1 Use of Terms .....	9
Section 12.2 Scope of Article .....	9
Section 12.3 Relinquishment of Interest by Non-Drilling Party .....	9
Section 12.4 Reversion of Relinquished Interest .....	10
Section 12.5 Effect of Reversion .....	10
Section 12.6 Rights and Obligations of Drilling Party .....	10
Section 12.7 Accounting Due Non-Drilling Party .....	10
Section 12.8 Stand-By Rig Time .....	10
Section 12.9 Subsequently Created Lease Burdens .....	10

## ARTICLE 13—ADJUSTMENT ON ESTABLISHMENT OR CHANGE OF PARTICIPATING AREA

Section 13.1 When Adjustment Made .....	11
Section 13.2 Definitions .....	11
A. "Usable well" .....	11
B. "Intangible value" .....	11
C. "Tangible property" .....	11
D. "Value" .....	11
Section 13.3 Method of Adjustment on Establishment or Enlargement .....	11
Section 13.4 Method of Adjustment on Contraction .....	11
Section 13.5 Ownership of Wells and Tangible Property .....	12
Section 13.6 Relinquished Interest of Non-Drilling Parties .....	12

## ARTICLE 14—SUPERVISION OF OPERATIONS BY PARTIES

Section 14.1 Right of Supervision .....	13
Section 14.2 Voting Control .....	13
Section 14.3 Meetings .....	13
Section 14.4 Action Without Meeting .....	13
Section 14.5 Representatives .....	13
Section 14.6 Audits .....	13
Section 14.7 Extraneous Projects .....	13

## ARTICLE 15—UNIT OPERATOR'S POWERS AND RIGHTS

Section 15.1 In General .....	13
Section 15.2 Employees .....	13
Section 15.3 Non-Liability .....	13
Section 15.4 Force Majeure .....	13
Section 15.5 Lien .....	14
Section 15.6 Advances .....	14
Section 15.7 Use of Unit Operator's Drilling Equipment .....	14
Section 15.8 Rights as Party .....	14

## ARTICLE 16—UNIT OPERATOR'S DUTIES

Section 16.1 Specific Duties .....	14
A. Drilling of Wells .....	14
B. Compliance with Laws and Agreements .....	14
C. Consultation with Parties .....	14
D. Payment of Costs .....	14
E. Records .....	15
F. Information .....	15
G. Access to Unit Area .....	15
Section 16.2 Insurance .....	15
A. Unit Operator's .....	15
B. Contractors' .....	15
C. Automotive Equipment .....	15
Section 16.3 Non-Discrimination .....	15
Section 16.4 Drilling Contracts .....	15
Section 16.5 Uninsured Losses .....	15

## ARTICLE 17—LIMITATIONS ON UNIT OPERATOR

Section 17.1 Specific Limitations .....	15
A. Change in Operations .....	15
B. Limit on Expenditures .....	15
C. Partial Relinquishment .....	15

D. Settlement of Claims .....	16
E. Determinations .....	16

#### ARTICLE 18—TITLES

Section 18.1 Representation of Ownership .....	16
Section 18.2 Title Papers to be Furnished .....	16
A. Lease Papers .....	16
B. Title Papers for Initial Test Well .....	16
C. Title Papers for Subsequent Wells .....	16
D. Title Papers on Establishment or Enlargement of a Participating Area .....	16
Section 18.3 Title Examination .....	16
Section 18.4 Option for Additional Title Examination .....	16
Section 18.5 Approval of Titles Prior to Drilling .....	16
Section 18.6 Approval of Titles Prior to Inclusion of Land in a Participating Area .....	17
Section 18.7 Failure of Title to Committed Working Interest Before Approval .....	17
Section 18.8 Failure of Title to Committed Working Interest After Approval .....	17
Section 18.9 Joinder by True Owner .....	17
Section 18.10 Title Challenge .....	17

#### ARTICLE 19—UNLEASED INTERESTS

Section 19.1 Treated as Leased .....	17
Section 19.2 Execution of Lease .....	17

#### ARTICLE 20—RENTALS AND LEASE BURDENS

Section 20.1 Rentals .....	18
Section 20.2 Lease Burdens .....	18
Section 20.3 Loss of Committed Working Interest .....	18

#### ARTICLE 21—TAXES

Section 21.1 Payment .....	18
Section 21.2 Apportionment .....	18
Section 21.3 Transfer of Interests .....	18
Section 21.4 Notices and Returns .....	18

#### ARTICLE 22—WITHDRAWAL OF TRACTS AND UNCOMMITTED INTERESTS

Section 22.1 Right of Withdrawal .....	18
Section 22.2 Non-Withdrawal .....	18

#### ARTICLE 23—COMPENSATORY ROYALTIES

Section 23.1 Notice .....	18
Section 23.2 Demand for Failure to Drill a Development Well .....	18
Section 23.3 Demand for Failure to Drill a Well Other Than a Development Well .....	19

#### ARTICLE 24—SEPARATE MEASUREMENT AND SALVAGE

Section 24.1 Separate Measurement .....	19
Section 24.2 Salvaged Materials .....	19

#### ARTICLE 25—ENHANCED RECOVERY AND PRESSURE MAINTENANCE

Section 25.1 Consent Required .....	19
Section 25.2 Above-Ground Facilities .....	19

#### ARTICLE 26—TRANSFERS OF INTEREST

Section 26.1 Sale by Unit Operator .....	19
Section 26.2 Assumption of Obligations .....	19
Section 26.3 Effective Date .....	19

#### ARTICLE 27—RELEASE FROM OBLIGATIONS AND SURRENDER

Section 27.1 Surrender or Release Within Participating Area .....	19
Section 27.2 Procedure on Surrender or Release Outside Participating Area .....	20
Section 27.3 Accrued Obligations .....	20

<b>ARTICLE 28—LIABILITY</b>	
Section 28.1 Liability .....	20
Section 28.2 No Partnership Created .....	20
Section 28.3 Election .....	20
<b>ARTICLE 29—NOTICES</b>	
Section 29.1 Giving and Receipt .....	20
Section 29.2 Addresses .....	20
<b>ARTICLE 30—EXECUTION</b>	
Section 30.1 Counterparts .....	20
Section 30.2 Ratification .....	20
Section 30.3 Effect of Signature .....	21
<b>ARTICLE 31—SUCCESSORS AND ASSIGNS</b>	
Section 31.1 Covenants .....	21
<b>ARTICLE 32—HEADINGS FOR CONVENIENCE</b>	
Section 32.1 Headings .....	21
<b>ARTICLE 33—RIGHT OF APPEAL</b>	
Section 33.1 Not Waived .....	21
<b>ARTICLE 34—SUBSEQUENT JOINDER</b>	
Section 34.1 Prior to the Commencement of Operations .....	21
Section 34.2 After Commencement of Operations .....	21
<b>ARTICLE 35—CARRIED INTERESTS</b>	
Section 35.1 Treatment of .....	21
<b>ARTICLE 36—EFFECTIVE DATE AND TERM</b>	
Section 36.1 Effective Date and Term .....	21
Section 36.2 Effect of Termination .....	21
<b>ARTICLE 37—OTHER PROVISIONS .....</b>	
<b>22</b>	
<b>EXHIBITS</b>	
Exhibit 1 Accounting Procedure	
Exhibit 2 Initial Test Well	
Exhibit 3 Insurance	
Exhibit 4 Non-Discrimination	
Exhibit 5 Oil and Gas Lease	

**NOTE:** Attention is called to pages 1, 6, 10, 11, 13, 14, 15, 16, and 19, which contain blanks to be filled in.

## UNIT OPERATING AGREEMENT

### TAOS TROUGH UNIT AREA

THIS AGREEMENT made as of the 2nd day of December, 1985,  
by and among the parties who execute or ratify this Agreement or a counterpart hereof,

#### WITNESSETH:

WHEREAS, the Parties have entered into that certain UNIT AGREEMENT FOR THE DEVELOPMENT AND OPERATION OF THE Taos Trough UNIT AREA, Counties of Colfax, Mora and Taos, State of New Mexico, dated as of the 2nd day of December, 1985, and hereinafter referred to as the "Unit Agreement", covering the lands described in EXHIBIT B thereto attached, which lands are referred to in the Unit Agreement and in this Agreement as the "Unit Area"; and

WHEREAS, the Parties enter into this Agreement pursuant to Section 7 of the Unit Agreement,  
NOW, THEREFORE, in consideration of the covenants herein contained, it is agreed as follows:

#### ARTICLE 1 DEFINITIONS

1.1 Definitions. The definitions contained in the Unit Agreement are adopted for all purposes of this Agreement. In addition, each term listed below shall have the meaning stated therefor, whenever used in this Agreement:

"Unit Operator" means Leonard Minerals Company and its successors, as the Unit Operator designated in accordance with the Unit Agreement, acting in that capacity and not as an owner of a Committed Working Interest.

"Party" means a party to this Agreement, including the Party acting as Unit Operator when acting as an owner of a Committed Working Interest.

"Drilling Party", "Completing Party", and "Participating Party" all mean the Party or Parties obligated to bear Costs incurred in the Drilling, Completing, or Deepening or Plugging Back, respectively, of a well at the commencement of such operation.

"Non-Drilling Party", "Non-Completing Party", and "Non-Participating Party" all mean the Party or Parties who had the optional right to participate in the Drilling, Completing, or Deepening or Plugging Back, respectively, of a well and who elected not to participate therein.

"Committed Working Interest" means a working interest which is shown on Exhibit B to the Unit Agreement as owned by a Party and which is committed to the Unit Agreement. Whenever reference is made to a Party "in" or "within" the Unit Area, a participating area, or other area designated pursuant to this Agreement, such reference shall mean a Party owning a Committed Working Interest in lands within such area.

"Acreage Basis", when used to describe the basis of participation by the Parties within the Unit Area, a participating area, or other area designated pursuant to this Agreement in voting, Costs, or Production, means participation by each such Party in the proportion that the acreage of its Committed Working Interests in such area bears to the total acreage of the Committed Working Interests of all such Parties therein. For the purposes of this definition, (a) the acreage of the Committed Working Interest in a tract within the Unit Area shall be the acreage of such tract as set forth in Exhibit B to the Unit Agreement, and (b) if there are two or more undivided Committed Working Interests in a tract, there shall be apportioned to each such Committed Working Interest that proportion of the acreage of the tract that such Committed Working Interest bears to the entire Committed Working Interest in the tract.

"Production" means all unitized substances produced and saved from the Unit Area except so much thereof as is used in the conduct of operations under the Unit Agreement and this Agreement.

"Costs" means all costs and expenses incurred in the development and operation of the Unit Area pursuant to this Agreement or the Unit Agreement and all other expenses that are herein made chargeable as Costs, determined in accordance with the Accounting Procedure attached hereto as Exhibit 1, which shall govern in all matters covered thereby, except that in the event of an inconsistency between said Accounting Procedure and this Agreement, this Agreement shall control.

"Lease Burdens" means the royalty reserved to the lessor in an oil and gas lease, an overriding royalty, a production payment, and any similar burden, but does not include a carried working interest, a net profits interest, or any other interest which is payable out of profits.

"Drill" means to perform all operations reasonably necessary and incident to the drilling of a well to its projected depth, including preparation of roads and drill site, testing, and logging, but excluding Completion operations.

"Complete" means to perform all operations reasonably necessary and incident to the completion of a well, commencing with the running and setting of the production pipe and, if productive of unitized substances, equipping through the wellhead connections, or plugging and abandoning, if dry.

"Equip" means to perform all operations reasonably necessary and incident to the equipping of a well for production beyond the wellhead connections.

"Deepen" or "Plug Back" means to perform all operations reasonably necessary and incident to Drilling a well below its original projected depth or plugging back a well to a depth above its original projected depth, testing, and logging, but excluding Completing and Equipping operations.

"Initial Test Well" means the test well or wells provided for in Section 9 of the Unit Agreement and in Exhibit 2 attached hereto.

"Subsequent Test Well" means a test well Drilled after the Drilling of the Initial Test Well and before discovery of unitized substances in paying quantities in the Unit Area.

"Development Well" means a well Drilled within a participating area and projected to the pool or zone for which the participating area was established.

"Exploratory Well" means a well (other than a Development Well) Drilled after discovery of unitized substances in paying quantities in the Unit Area.

"Approval of the Parties" or "Direction of the Parties" means an approval, authorization, or direction which receives the affirmative vote of the Parties entitled to vote on the giving of such Approval or Direction, as specified in Section 14.2.

"Salvage Value" of a well means the value of the materials and equipment in or appurtenant to the well, determined in accordance with Exhibit 1, less the reasonably estimated Costs of salvaging the same and plugging and abandoning the well.

"BLM" means the Bureau of Land Management including any person acting under the authority thereof.

"Paying quantities" means paying quantities as defined in Section 9 of the Unit Agreement.

## ARTICLE 2 EXHIBITS

2.1 Exhibits. The following Exhibits are incorporated herein by reference:

- Exhibit 1. Accounting Procedure.
- Exhibit 2. Initial Test Well.
- Exhibit 3. Insurance.
- Exhibit 4. Non-Discrimination.
- Exhibit 5. Oil and Gas Lease.

In the event of a conflict or inconsistency between the provisions of an Exhibit and the provisions of this Agreement, the provisions of this Agreement shall control.

## ARTICLE 3 INITIAL TEST WELL

3.1 Location. Unit Operator shall begin to Drill the Initial Test Well within the time required by Section 9 of the Unit Agreement, or any extension thereof, at the location specified in Exhibit 2.

3.2 Costs of Drilling. Subject to the investment adjustment provisions of Article 13, the Costs of Drilling the Initial Test Well shall be shared by the Parties in the manner and in the proportions specified in Exhibit 2.

## ARTICLE 4 SUBSEQUENT TEST WELLS

4.1 Right to Drill. The Drilling of any Subsequent Test Well shall be upon such terms and conditions as may be agreed to by the Parties; provided, however, that in the absence of agreement, such well may be Drilled under the provisions of Article 9.

## ARTICLE 5 ESTABLISHMENT, REVISION, AND CONSOLIDATION OF PARTICIPATING AREAS

5.1 Proposal. Unit Operator shall initiate each proposal for the establishment or revision of a participating area by submitting the proposal in writing to each Party at least twenty (20) days before filing the same with the BLM. The date of proposed filing must be shown in the proposal. If, within the 20-day period above provided, the proposal receives the Approval of the Parties within the proposed participating area or no written objections are received, then such proposal shall be filed on the date specified.

5.2 Objections to Proposal. Prior to the proposed filing date any Party may submit to all other Parties written objections to such proposal. If, despite such objections, the proposal receives the Approval of the Parties within the proposed participating area, then the Party making the objections may renew the same before the BLM.

5.3 Revised Proposal. If the proposal does not receive the Approval of the Parties within the proposed participating area, and Unit Operator receives written objections thereto, then Unit Operator shall submit to the Parties a revised proposal, taking into account the objections made to the first proposal. If no proposal receives the Approval of the Parties within sixty (60) days from submission of the

first proposal, then Unit Operator shall file with the BLM a proposal reflecting as nearly as practicable the various views expressed by the Parties.

**5.4 Rejection of Proposal.** If a proposal filed by Unit Operator as above provided is rejected by the BLM, Unit Operator shall initiate a new proposal in the same manner as provided in Section 5.1, and the procedure with respect thereto shall be the same as in the case of an initial proposal.

**5.5 Consolidation.** Two or more participating areas may be combined as provided in the Unit Agreement.

## ARTICLE 6 APPORTIONMENT OF COSTS AND OWNERSHIP AND DISPOSITION OF PRODUCTION AND PROPERTY

**6.1 Apportionment and Ownership Within Participating Area.** Except as otherwise provided in Articles 8, 9, 11, and 12:

**A. Costs.** All Costs incurred in the development and operation of a participating area for or in connection with production of unitized substances from any pool or zone for which such participating area is established shall be borne by the Parties within such participating area on an Acreage Basis, determined as of the time such Costs are incurred.

**B. Production.** All Production from a participating area shall be allocated on an Acreage Basis to the tracts of unitized land within such participating area. That portion of such Production which is allocated to any such tract shall be owned by the Party or Parties having Committed Working Interest or Interests therein in the same manner and subject to the same conditions as if actually produced from such tract through a well thereon and as if this Agreement and the Unit Agreement had not been executed.

**C. Property.** All materials, equipment, and other property, whether real or personal, the cost of which is chargeable as Costs and which have been acquired in connection with the development or operation of a participating area, shall be owned by the Parties within such participating area on an Acreage Basis.

**6.2 Ownership and Costs Outside Participating Area.** If a well Drilled (including the Deepening or Plugging Back thereof) within a Drilling Block established under the provisions of either Article 9 or Article 10 is completed as a producer but not included within a participating area, then the following provisions shall be applicable:

**A. When All Drilling Block Parties Participate.** If all Parties within the Drilling Block shall have elected to participate in Drilling and Completing such well, then said well, the Production therefrom, and the materials and equipment therein or appurtenant thereto shall be owned by such Parties; and all Costs incurred in the operation of such well and all Lease Burdens payable in respect of Production from such well shall be borne and paid by said Parties. Apportionment among said Parties of ownership, Costs, and Lease Burdens shall be in the same proportions in which Costs incurred in Drilling the well were borne.

**B. When Less Than All Drilling Block Parties Participate.** If any Party within the Drilling Block shall have elected not to participate in Drilling or Completing such well, then the provisions of Article 12 shall be applicable thereto; and the relinquished interest of the Non-Drilling Party shall revert to it in the same manner and under the same conditions as provided in Section 12.4 with respect to a well which results in the establishment or enlargement of a participating area, except that the proceeds ~~of market value~~ to be used in determining when such reversion shall occur shall be the proceeds ~~of market value~~ (after making the deductions provided for in Section 12.4) of that portion of the Production obtained from the well which, had the Non-Drilling Party elected to participate in the Drilling or Completing thereof, would have been allocable, on an Acreage Basis within the Drilling Block, to the Non-Drilling Party. Upon reversion of the relinquished interest of the Non-Drilling Party in such well, the provisions of Section 12.5 shall become applicable.

**6.3 Cost Liability of Subsequently Created Interests.** Anything herein to the contrary notwithstanding, if, subsequent to the date of this Agreement, any Party shall create an overriding royalty, production payment, net proceeds interest, carried interest, or any other interest out of its Committed Working Interest (hereinafter called "Subsequently Created Interest"), such Subsequently Created Interest shall be made expressly subject to the terms and provisions of this Section 6.3 and of Section 12.9. If the Party which created such Subsequently Created Interest fails to pay, when due, its share of Costs and the proceeds from its share of Production are insufficient to cover such Costs, then the Subsequently Created Interest shall be chargeable with a pro rata share of such Costs as if such Subsequently Created Interest were a Committed Working Interest; and Unit Operator shall have the right to enforce against such Subsequently Created Interest the lien and all other rights granted in Section 15.5 for the purpose of collecting Costs chargeable to the Subsequently Created Interest.

**6.4 Taking in Kind.** Each Party shall currently, as produced, take in kind or separately dispose of its share of Production and pay Unit Operator for any extra expenditure necessitated thereby. Except as otherwise provided in Section 15.5, each Party shall be entitled to receive directly all proceeds from the sale of its share of Production. Unit Operator shall timely make all permitted governmental filings relative to the price to be charged for gas; however, Unit Operator shall not be liable if, through mistake or oversight, it should fail to make any such filing or should make erroneous filings.

**6.5 Failure to Take in Kind.** Should any Party fail to take in kind or separately dispose of its share of Production, the Party acting as Unit Operator shall have the right, revocable at will by the Party owning such share, to purchase such share for its own account at not less than the market price



prevailing in the area for Production of like kind and quality, or to sell such share to others at not less than the price which it receives for its own share of Production; provided that all such sales shall be only for such reasonable periods of time as are consistent with the minimum needs of the industry under the circumstances, but not to exceed one (1) year. Notwithstanding the foregoing, Unit Operator shall not sell or commit any Party's share of gas Production to a sale without first giving such Party not less than ninety (90) days' written notice.

6.6 Surplus Materials and Equipment. Materials and equipment owned by the Parties or by any of them pursuant to this Agreement may be classified as surplus by Unit Operator when deemed by it to be no longer needed in operations hereunder, by giving to each Party owning an interest therein notice thereof. Such surplus materials and equipment shall be disposed of as follows:

A. Each Party owning an interest therein shall have the right to take in kind its share of surplus tubular goods and other surplus items which are susceptible of division in kind, by notice given to Unit Operator within thirty (30) days after classification thereof as surplus, except that such right shall not apply to junk or to any item (other than tubular goods) having a replacement cost of less than Seven Thousand Five Hundred Dollars (\$7,500.00).

B. Surplus materials and equipment not divided in kind, other than junk and any item (other than tubular goods) having a replacement cost of less than Seven Thousand Five Hundred Dollars (\$7,500.00), shall be sold to the highest bidder or bidders.

C. Surplus materials and equipment not disposed of in accordance with the preceding provisions of this Section shall be disposed of as provided in Exhibit 1.

#### ARTICLE 7 PLANS OF DEVELOPMENT

7.1 Submittal of Plans. Each plan for the development and operation of the Unit Area shall be submitted by Unit Operator to the BLM in accordance with the Unit Agreement and the further provisions of this Article.

7.2 Proposal. Unit Operator shall initiate each proposed plan by submitting the same in writing to each Party at least thirty (30) days before filing the same with the BLM. If, within the 30-day period above provided, such plan receives the Approval of the Parties or no written objections are received, then such plan shall be filed.

7.3 Objections to Plan. Within the 30-day period above provided, any Party may submit to Unit Operator written objections to such plan. If, despite such objections, the plan receives the Approval of the Parties, then the Party making the objection may renew the same before the BLM.

7.4 Revised Plan. If such plan does not receive the Approval of the Parties, and Unit Operator receives written objections thereto, then Unit Operator shall submit to the Parties a revised plan, taking into account the objections made to the first plan. If no plan receives the Approval of the Parties within sixty (60) days from submission of the first plan, then Unit Operator shall file with the BLM a plan reflecting as nearly as practicable the various views expressed by the Parties.

7.5 Rejection of Plan. If a plan filed by Unit Operator as above provided is rejected by the BLM, Unit Operator shall initiate a new plan in the same manner as provided in Section 7.2, and the procedure with respect thereto shall be the same as in the case of an initial plan.

7.6 Notice of Approval or Disapproval. If and when a plan has been approved or disapproved by the BLM, Unit Operator shall give prompt notice thereto to each Party.

7.7 Supplemental Plans. If any Party or Parties have elected to proceed with a Drilling, Deepening, or Plugging Back operation in accordance with the provisions of this Agreement, and such operation is not provided for in the then current plan of development approved by the BLM, Unit Operator shall either (a) submit to the BLM for approval a supplemental plan providing for the conduct of such operation or (b) request the BLM to consent to such operation, if such consent is sufficient.

7.8 Cessation of Operations Under the Plan. If any plan approved by the BLM provides for the cessation of any Drilling or other operation therein provided for in the happening of a contingency and such contingency occurs, Unit Operator shall promptly cease such Drilling or other operation and shall not incur any additional Costs in connection therewith unless and until such Drilling or other operation is again authorized, in accordance with this Agreement, by the Parties chargeable with such Costs and the BLM.

#### ARTICLE 8 DEVELOPMENT WELLS

8.1 Purpose and Procedure. It is the purpose of this Article to set forth the procedure for Drilling and Completing a Development Well.

8.2 Drilling. The Drilling of a Development Well shall be pursuant to the procedure herein set forth.

A. Approval Required. The Drilling of a Development Well shall be subject to such Drilling receiving the Approval of the Parties, unless the Drilling of the proposed well is necessary to prevent the loss of a Committed Working Interest in the tract of land on which the proposed well is to be Drilled. Vote by any Party in favor of the Drilling of any such well shall not, however, be deemed an election by such Party to participate in the Costs thereof but shall mean only that such Party

considers the Drilling of the well to be consistent with the efficient and economic development of the participating area involved and has no objection to the Drilling thereof.

**B. Notice of Proposed Drilling.** Subject to the provisions of Subdivision A of this Section 8.2, any Party within a participating area may propose the Drilling of a Development Well therein by giving to each of the other Parties within the participating area notice, specifying the location, depth, and estimated cost of the proposed well, which location shall conform to any applicable spacing pattern then existing or an approved exception thereto.

**C. Response to Notice.** Within thirty (30) days after receipt of such notice, each Party within such participating area shall advise all other Parties therein whether or not it wishes to participate in Drilling the proposed well. If any Party fails to give such advice within said 30-day period, it shall be deemed to have elected not to participate in Drilling the proposed well. If all Parties within such participating area advise that they wish to participate in Drilling the proposed well, then Unit Operator shall Drill the well for the account of all such Parties.

**D. Notice of Election to Proceed.** Unless all Parties within the participating area agree to participate in Drilling such well, then, within fifteen (15) days after expiration of the 30-day period specified in Subdivision C of this Section 8.2, each Party within the participating area then desiring to have the proposed well Drilled shall give to all other Parties therein notice of its election to proceed with the Drilling of said well. Failure to give such notice shall be deemed an election not to participate in Drilling the well.

**E. Subsequent Election.** If election to Drill the proposed well is made, any Party within the participating area who had not previously elected to participate therein may do so by notice given to Unit Operator at any time before the well is spudded, in which event such Party shall be included in the Drilling Party. However, such Party shall be bound by any and all Directions and Approvals theretofore given by the Drilling Party concerning the Drilling of the well.

**F. Effect of Election.** If one or more, but not all, of the Parties within the participating area elect to proceed with the Drilling of the well, Unit Operator shall Drill the well for the account of such Party or Parties, who shall constitute the Drilling Party, on an Acreage Basis among themselves, or on such other basis as said Parties may specify.

**G. Rights and Obligations of Drilling Party and Non-Drilling Party.** Whenever a Development Well is Drilled otherwise than for the account of all Parties within the participating area involved, the provisions of Article 12 shall be applicable to such operation.

**8.3 Attempted Completion.** The attempted Completion of Development Wells Drilled to their projected depths shall be governed by the following provisions:

**A. Notice by Unit Operator.** After a Development Well has reached its projected depth and been tested, logged, and logs furnished to each Drilling Party, but before production pipe has been set, Unit Operator shall give notice thereof to each Drilling Party.

**B. Right to Attempt Completion.** Each Drilling Party shall have the right to initiate a proposal to attempt the Completion of such well and also shall be entitled to participate in the Completion attempt.

**C. Time and Manner of Initiating Proposal.** A period of twenty-four (24) hours (exclusive of Saturdays, Sundays, and holidays) from and after receipt of the notice given pursuant to Subdivision A of this Section 8.3 shall be allowed within which a Party entitled to do so may initiate a proposal to Complete. Any such proposal shall be initiated by giving notice thereof to Unit Operator and to each Drilling Party. If no such proposal is initiated within said period and no other proposal is initiated pursuant to Article 11, Unit Operator shall plug and abandon the well for the account of the Drilling Party.

**D. Election.** If a proposal to Complete is initiated, each Drilling Party shall have a period of twenty-four (24) hours (exclusive of Saturdays, Sundays, and holidays) from and after receipt of such proposal within which to notify Unit Operator whether or not it elects to participate in the Completion attempt. The failure of a Party to signify its election within said 24-hour period shall be deemed an election not to participate in the Completion attempt.

**E. Effect of Election.** The Party or Parties electing to participate in an attempt to Complete a well as above provided shall constitute the Completing Party for such operation. Each Party who was entitled to make such election but failed to do so as above provided shall be a Non-Completing Party with respect to such operation. Such operation shall be conducted by Unit Operator for the account of the Party or Parties constituting the Completing Party, on an Acreage Basis among themselves, or on such other basis as the Completing Party may specify. Such operation, if successful, shall include Equipping the well for production.

**F. Rights and Obligations of Completing Party and Non-Completing Party.** Upon the commencement of a Completion operation otherwise than for the account of all Drilling Parties, the provisions of Article 12 shall be applicable to such operation.

**G. Notice Prior to Plugging.** Before plugging and abandoning any Development Well which was Drilled to its projected depth and not completed as a producer of unitized substances, Unit Operator shall give the notice specified in Section 11.1 A, unless every Party entitled to the notice has consented to the plugging and abandonment of such well, in which event Unit Operator shall plug and abandon the well for the account of the Completing Party. Upon the giving of such notice, the provisions of Article 11 shall apply.

## ARTICLE 9 EXPLORATORY WELLS

**9.1 Purpose and Procedure.** It is the purpose of this Article to set forth the procedure for Drilling and Completing an Exploratory Well.

**9.2 Drilling.** The Drilling of an Exploratory Well shall be pursuant to the procedure herein set forth.

**A. Notice of Proposed Drilling.** Any Party desiring the Drilling of an Exploratory Well on land in which it owns a Committed Working Interest shall designate an area, herein called a Drilling Block, not to exceed 960 acres, which, on the basis of available geological information, will, in its judgment, be proved productive by the Drilling of such well. Unit Operator and each Party within the Drilling Block shall be furnished with a plat and description of the area so designated, together with notice of the location, objective formation, estimated depth, and estimated cost of the proposed well. The location of the proposed well shall conform to any applicable spacing pattern then existing or an approved exception thereto. The Drilling Block shall include no land in an established participating area for the objective formation for the well to be Drilled thereon nor any land included in a proposal therefor filed with the BLM nor any land within an active, previously designated Drilling Block for such formation. The Drilling Block shall be considered active for ninety (90) days after the designation thereof and, if the actual Drilling of a well is commenced thereon within such period, until either:

- (1) the Completion of the well, if it is completed otherwise than as a producer of unitized substances in paying quantities, either at its original projected depth or, if Deepening or Plugging Back operations are conducted, at any other projected depth; or
- (2) the filing with the BLM of a proposal for the establishment or revision of a participating area if the Completion of the well results in the filing of such proposal.

**B. Basis of Participation.** Each Party within the Drilling Block shall be entitled to participate in the Costs of Drilling the proposed well on an Acreage Basis but shall be required to do so only if it notifies the other Parties within the Drilling Block of its willingness so to participate, as hereinafter in this Article 9 provided.

**C. Exclusion of Land From Proposed Drilling Block.** Within thirty (30) days after receipt of such notice, any part of the land included in the proposed Drilling Block may be excluded therefrom at the Direction of the Parties therein. In such event the proposed Drilling Block, as reduced by the exclusion of such land, shall be established as the Drilling Block. In the absence of any such Direction, then, at the expiration of said 30-day period, the proposed Drilling Block shall be established as the Drilling Block.

**D. Preliminary Notice to Join in Drilling.** Within ten (10) days after the establishment of the Drilling Block, each Party within such Drilling Block shall advise all other Parties therein whether or not it wishes to participate in Drilling the proposed well. If any Party fails to give such advice within said 10-day period, it shall be deemed to have elected not to participate in Drilling the proposed well. If all Parties within the Drilling Block advise that they wish to participate in Drilling the proposed well, then Unit Operator shall Drill the well for the account of all such Parties.

**E. Notice of Election to Proceed.** Unless all Parties within the Drilling Block agree to participate in Drilling such well, then, within fifteen (15) days after expiration of the 10-day period specified in Subdivision D of this Section 9.2, each Party within the Drilling Block then desiring to have the proposed well Drilled shall give to all other Parties therein notice of its election to proceed with the Drilling of said well. Failure to give such notice shall be deemed an election not to participate in Drilling the well.

**F. Subsequent Election.** If election to Drill the proposed well is made, any Party within the Drilling Block who had not previously elected to participate therein may do so by notice given to all other Parties within the Drilling Block at any time before the well is spudded, in which event such Party shall be included in the Drilling Party. However, such Party shall be bound by any and all Directions and Approvals theretofore given by the Drilling Party concerning the Drilling of the well.

**G. Effect of Election.** If one or more, but not all, of the Parties within the Drilling Block elect to proceed with the Drilling of the well, Unit Operator shall Drill the well for the account of such Party or Parties, who shall constitute the Drilling Party, on an Acreage Basis among themselves, or on such other basis as said Parties may specify.

**H. Rights and Obligations of Drilling Party and Non-Drilling Party.** Whenever an Exploratory Well is Drilled otherwise than for the account of all Parties within the Drilling Block involved, the provisions of Article 12 shall be applicable to such operation.

**9.3 Attempted Completion.** The attempted Completion of Exploratory Wells Drilled to their projected depths shall be governed by the following provisions:

**A. Notice by Unit Operator.** After an Exploratory Well has reached its projected depth and has been tested, logged, and logs furnished to each Drilling Party, but before production pipe has been set, Unit Operator shall give notice thereof to each Drilling Party.

**B. Right to Attempt Completion.** Each Drilling Party shall have the right to initiate a proposal to attempt the Completion of such well and also shall be entitled to participate in the Completion attempt.

**C. Time and Manner of Initiating Proposal.** A period of twenty-four (24) hours (exclusive of Saturdays, Sundays, and holidays) from and after receipt of the notice given pursuant to Subdivision A of this Section 9.3 shall be allowed within which a Party entitled to do so may initiate a proposal to Complete. Any such proposal shall be initiated by giving notice thereof to Unit Operator and to each Drilling Party. If no such proposal is initiated within said period and no other proposal is initiated pursuant to Article 11, Unit Operator shall plug and abandon the well for the account of the Drilling Party.

**D. Election.** If a proposal to Complete is initiated, each Party entitled to participate in the Completion attempt shall have a period of twenty-four (24) hours (exclusive of Saturdays, Sundays, and holidays) from and after receipt of such proposal within which to notify Unit Operator whether or not it elects to participate in the Completion attempt. The failure of a Party to signify its election within said 24-hour period shall be deemed an election not to participate in the Completion attempt.

**E. Effect of Election.** The Party or Parties electing to participate in an attempt to Complete a well as above provided shall constitute the Completing Party for such operation. Each Party who was entitled to make such election but failed to do so as above provided shall be a Non-Completing Party with respect to such operation. Such operation shall be conducted by Unit Operator for the account of the Party or Parties constituting the Completing Party, on an Acreage Basis among themselves, or on such other basis as the Completing Party may specify. Such operation, if successful, shall include Equipping the well for production.

**F. Rights and Obligations of Completing Party and Non-Completing Party.** Upon the commencement of a Completion operation otherwise than for the account of all Drilling Parties, the provisions of Article 12 shall be applicable to such operation.

**G. Notice Prior to Plugging.** Before plugging and abandoning any Exploratory Well which was Drilled to its projected depth and not completed as a producer of unitized substances, Unit Operator shall give the notice specified in Section 11.1 A, unless every Party entitled to the notice has consented to the plugging and abandonment of such well, in which event Unit Operator shall plug and abandon the well for the account of the Completing Party. Upon the giving of such notice, the provisions of Article 11 shall apply.

## ARTICLE 10 REQUIRED WELLS

**10.1 Definition.** For the purpose of this Article, a well shall be deemed a Required Well if the Drilling thereof is required by a final order of the BLM. Such an order shall be deemed final upon expiration of the time allowed for appeal therefrom without the commencement of appropriate appeal proceedings or, if such proceedings are commenced within said time, upon the final disposition of the appeal. Whenever Unit Operator receives any such order, it shall promptly mail a copy thereof to each Party. If any such order is appealed, the Party appealing shall give prompt notice thereof to Unit Operator and to each of the other Parties, and, upon final disposition of the appeal, Unit Operator shall give each Party prompt notice of the result thereof.

**10.2 Election to Drill.** Any Party desiring to Drill, or to participate in the Drilling of, a Required Well shall give to Unit Operator notice thereof within thirty (30) days after the order requiring such well becomes final or within such lesser time as may be required to insure compliance with such order. If such notice is given within said period, Unit Operator shall Drill the Required Well for the account of the Party or Parties giving such notice; provided, however, if the Required Well is a Development Well, it shall not be Drilled unless it receives the Approval of the Parties within the participating area involved. All rights and obligations 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 under Article 8, if the same is a Development Well, or under Article 9, if the same is an Exploratory Well or a Subsequent Test Well.

**10.3 Alternatives to Drilling.** 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 the well and if payment thereof receives, within said period, the Approval of the Parties who would be chargeable with the Costs incurred in Drilling the well if the well were Drilled as provided in Section 10.4, Unit Operator shall pay such compensatory royalties for the account of said Parties; or

**B. Contraction.** If the Drilling of the well may be avoided, without other penalty, by contraction of the Unit Area, Unit Operator shall make a reasonable effort to effect such contraction; or

**C. Termination.** If the Required Well is a Subsequent Test Well, the Parties shall join in termination of the Unit Agreement in accordance with its provisions.

**10.4 Required Drilling.** If none of the foregoing alternatives is available, Unit Operator shall Drill the Required Well under whichever of the following provisions is applicable:

**A. Development Well.** If the Required Well is a Development Well, it shall be Drilled by Unit Operator for the account of all Parties within the participating area in which the well is Drilled; or

**B. Exploratory Well.** If the Required Well is an Exploratory Well, the Drilling Block for such well shall consist of all forty (40) acre subdivisions and lots of the Public Land Survey of which more than one-half of the surface area is within a distance of 2,640 feet from the proposed bottom hole location of such well, but excluding therefrom all lands within any participating area theretofore

established for the pool or zone to which the well is to be Drilled. Unit Operator shall Drill such well for the account of all the Parties owning Committed Working Interests within the Drilling Block, on an Acreage Basis among themselves; and no such Party shall have the right to elect not to participate in the Drilling of said well.

## **ARTICLE 11**

### **DEEPENING, PLUGGING BACK, AND ABANDONMENT**

**11.1 Attempted Deepening or Plugging Back.** The attempted Deepening or Plugging Back of wells not completed as producers of unitized substances at their original projected depths shall be governed by the following provisions of this Section 11.1 and by the provisions of Section 11.2, unless every Party entitled to the notice provided for in Subdivision A of this Section 11.1 has consented to the plugging and abandonment of such well:

**A. Notice by Unit Operator.** Before abandoning any well which has been Drilled to its original projected depth but not completed as a producer of unitized substances, Unit Operator shall give notice of its intention to plug and abandon such well to each Drilling Party and Non-Drilling Party.

**B. Right to Initiate Proposal.** Each Party who participated in the Drilling of a well concerning which notice is given in accordance with Subdivision A of this Section 11.1 and any other Party owning a Committed Working Interest in the tract of land on which the well is located may initiate a proposal to attempt to Deepen or Plug Back such well; provided, however, if the well was Drilled as a Development Well, a proposal to Deepen or Plug Back may be initiated only by a Party owning a Committed Working Interest in the tract of land on which the well is located.

**C. Right to Participate.** In order to be entitled to participate in a Deepening or Plugging Back operation, a Party must have the right to initiate the same or must own a Committed Working Interest in the Drilling Block theretofore established for Drilling the well involved; if no Drilling Block was theretofore established for Drilling such well, the Drilling Block for such Deepening or Plugging Back operation shall be established automatically in accordance with the provisions of Subdivision B of Section 10.4, which shall be applicable hereto.

**D. Time and Manner of Initiating Proposal.** A period of twenty-four (24) hours (exclusive of Saturdays, Sundays, and holidays) from and after receipt of the notice given pursuant to Subdivision A of this Section 11.1 shall be allowed within which a Party entitled to do so may initiate a proposal to Deepen or Plug Back. Any such proposal shall be initiated by giving notice thereof to Unit Operator and to each Party entitled to participate in the proposed operation. If no such proposal is initiated within said period, Unit Operator shall plug and abandon the well for the account of the Completing Party if a Completion attempt was made or, if not, then for the account of the Drilling Party.

**E. Election.** If a proposal to Deepen or Plug Back a well is initiated, each Party entitled to participate in the operation proposed shall have a period of forty-eight (48) hours (exclusive of Saturdays, Sundays, and holidays) from and after receipt of such proposal within which to notify Unit Operator whether or not it elects to participate in the proposed operation. The failure of a Party to signify its election within said 48-hour period shall be deemed an election not to participate in the proposed operation.

**F. Effect of Election.** The Party or Parties electing to participate in an operation to Deepen or Plug Back a well as above provided shall constitute the Participating Party for such operation. Each Party who was entitled to make such election but failed to do so as above provided shall be a Non-Participating Party with respect to such operation. Such operation shall be conducted by Unit Operator for the account of the Party or Parties constituting the Participating Party, on an Acreage Basis among themselves, subject, however, to the provisions of Section 11.2 and Section 11.3. If the Party or Parties making such election do not proceed with the operation, the Costs incurred in plugging and abandoning the well shall be charged and borne as part of the Costs incurred in Drilling the well.

**G. Rights and Obligations of Participating Party and Non-Participating Party.** Upon the commencement of a Deepening or Plugging Back operation otherwise than for the account of all Parties entitled to participate therein, the provisions of Article 12 shall be applicable to such operation.

**11.2 Deepening or Plugging Back to Participating Area.** If a well within the surface boundaries of a participating area is to be Deepened or Plugged Back to the pool or zone for which such participating area was established, such operation, including the Completion of such well, may be conducted only if it receives the Approval of the Parties within such participating area, and only upon such terms and conditions as may be specified in such Approval, and upon such further terms and conditions as may be agreed to by the Parties owning interests in the well immediately prior to the commencement of any such Deepening or Plugging Back operation.

**11.3 Conflicts.** If conflicting elections to attempt to Deepen or Plug Back are made in accordance with the provisions of this Article 11, preference shall be given first to Deepening. However, if a Deepening attempt does not result in completion of the well as a producer of unitized substances, Unit Operator shall again give notice in accordance with Subdivision A of Section 11.1 before plugging and abandoning the well.

**11.4 Attempted Completion.** The attempted Completion of wells Deepened or Plugged Back to their projected depths, except wells Deepened or Plugged Back to a participating area, shall be governed by the provisions of Section 9.3, unless every Participating Party has consented to the plugging and

abandonment of such well, in which event Unit Operator shall plug and abandon the well for the account of the Participating Party.

**11.5 Abandonment of Producing Wells.** A well completed as a producer of unitized substances within a participating area shall be abandoned for plugging if and when abandonment thereof receives the Approval of the Parties within such participating area, subject, however, to the provisions of Section 11.6. The abandonment of a well completed as a producer but not included in a participating area shall be governed by the following provisions:

**A. Consent Required.** Such well shall not be abandoned for production from the pool or zone in which it is Completed, except with the consent of all Parties then owning the well.

**B. Abandonment Procedure.** If the abandonment of such well receives the Approval of the Parties who own the well but is not consented to by all such Parties, Unit Operator shall give notice thereof to each Party, if any, then having an interest in the well who did not join in such Approval. Any such non-joining Party who objects to abandonment of the well (herein called Non-Abandoning Party) may give notice thereof to all other Parties (herein called Abandoning Parties) then having interests in the well, provided such notice is given within thirty (30) days after receipt of the notice given by Unit Operator. If such objection is so made, the Non-Abandoning Party or Parties shall forthwith pay to the Abandoning Parties their respective shares of the Salvage Value of the well. Upon the making of such payment, the Abandoning Parties shall be deemed to have relinquished to the Non-Abandoning Party or Parties all their operating rights and working interest in the well, but only with respect to the pool or zone in which it is then Completed, and all their interest in the materials and equipment in or pertaining to the well. If there is more than one Non-Abandoning Party, the interests so relinquished shall be owned by the Non-Abandoning Parties in the proportions which their respective interests in the well bear to the total of their interests therein immediately prior to such relinquishment.

**C. Rights and Obligations of Non-Abandoning Party.** After the relinquishment above provided for, such well shall be operated by Unit Operator for the account of the Non-Abandoning Party or Parties, who shall own all Production therefrom and shall bear all Costs, Lease Burdens, and other burdens thereafter incurred in operating the well and plugging it when abandoned (unless the well is taken over for Deepening or Plugging Back as hereinafter provided) and also the Costs of any additional tankage, flow lines, or other facilities needed to measure separately the unitized substances produced from the well. Costs shall include an overhead charge computed at the highest per well rate applicable to the operation of a single producing well in accordance with Exhibit 1, if such rate is provided.

**D. Option to Repurchase Materials.** If a well taken over by the Non-Abandoning Party or Parties as above provided is abandoned for plugging within six (6) months after relinquishment by the Abandoning Parties of their interests therein, each Abandoning Party shall have the right at its option to repurchase that portion of the materials and equipment salvaged from the well which is equal to the interest relinquished by it to the Non-Abandoning Party or Parties, at the value previously fixed therefor. Said option may be exercised only by notice given to Unit Operator and to the Non-Abandoning Party or Parties within fifteen (15) days after receipt of the notice given by Unit Operator pursuant to Section 11.6.

**11.6 Deepening or Plugging Back Abandoned Producing Wells.** Before plugging any well authorized for abandonment pursuant to Section 11.5, Unit Operator shall give notice to the Party or Parties owning Committed Working Interests in the tract of land upon which the well is located, which Parties, for the further purposes of this Section 11.6, shall constitute the Parties entitled to initiate and participate in a proposed Deepening or Plugging Back operation. Within ten (10) days after receipt of said notice, any such Party desiring the Deepening or Plugging Back of such well shall give notice thereof to Unit Operator and to each Party entitled to participate in the proposed operation; and all the provisions of Subdivisions E, F, and G of Section 11.1 shall apply in the same manner as if the proposed Deepening or Plugging Back were a proposal for the Drilling of an Exploratory Well, subject, however, to the provisions of Section 11.2 and Section 11.3. If no Party gives notice of desire to Deepen or Plug Back such well within said period of ten (10) days, or if such notice is given but no party elects to proceed with the Deepening or Plugging Back of the well within the time specified therefor, Unit Operator shall plug and abandon the well for the account of the Party or Parties owning the well.

## ARTICLE 12 RIGHTS AND OBLIGATIONS OF DRILLING PARTY AND NON-DRILLING PARTY

**12.1 Use of Terms.** As used in this Article, the terms "Drilling Party" and "Non-Drilling Party" are to be understood as including "Completing Party" and "Non-Completing Party" and "Participating Party" and "Non-Participating Party", respectively, as such terms are used in Articles 8, 9, and 11.

**12.2 Scope of Article.** The rights and obligations of the Drilling Party and Non-Drilling Party with respect to a well which is Drilled, Deepened, Plugged Back, or Completed otherwise than for the account of all Parties entitled to participate therein shall be governed by the succeeding provisions of this Article 12.

**12.3 Relinquishment of Interest by Non-Drilling Party.** When a well is Drilled, Deepened, Plugged Back, or Completed otherwise than for the account of all Parties entitled to participate therein, each Non-Drilling Party, upon the commencement of such operation, shall be deemed to have relinquished to the Drilling Party, and the Drilling Party shall own, all such Non-Drilling Party's operating rights and



working interest in and to such well. In the case of a Deepening or Plugging Back, if a Non-Drilling Party owned an interest in the well immediately prior to the Deepening or Plugging Back, the Drilling Party shall pay to such Non-Drilling Party its share of the Salvage Value of the well, such payment to be made at the time the well is taken over by the Drilling Party for Deepening or Plugging Back.

**12.4 Reversion of Relinquished Interest.** If the well is completed as a producer of unitized substances and is a Development Well or results in the establishment or enlargement of a participating area to include such well and if, by reason thereof, there is included in such participating area any land within the Drilling Block in which a Non-Drilling Party owns a Committed Working Interest, then the operating rights and working interest relinquished by such Non-Drilling Party shall revert to it at such time as the proceeds ~~market value~~ of that portion of the Production obtained from the well after such relinquishment which is allocated to all the acreage of such Non-Drilling Party in the participating area involved (after deducting from such proceeds ~~market value~~ all Lease Burdens and <sup>excise taxes</sup> all taxes upon or measured by Production that are payable up to such time on said portion of the Production from such well) shall equal the total of the following:

A. 100% of that portion of the Costs incurred in Equipping the well and in operating the well after such relinquishment, and up to such time, that would have been charged to such Non-Drilling Party had the well been Drilled, Deepened, Plugged Back, or Completed and Equipped for the account of all Parties entitled to participate therein.

B. 400 % of that portion of the Costs incurred in Drilling, Deepening, Plugging Back, or Completing the well that would have been charged to such Non-Drilling Party had the well been Drilled, Deepened, Plugged Back, or Completed and Equipped for the account of all Parties entitled to participate therein.

However, if such well is subsequently Deepened or Plugged Back, then (1) any payment made to such Non-Drilling Party as its share of the Salvage Value of the well in accordance with Section 12.3 shall be added to and deemed part of the Costs incurred in operating the well, for the purposes of Subdivision A above, and (2) if such Non-Drilling Party did not participate in the initial Drilling of the well, but the Drilling Party did participate therein, and if the interest relinquished by such Non-Drilling Party upon the initial Drilling of the well had not reverted to it before such Deepening or Plugging Back, then, for the purposes of Subdivision B above, there shall be added to and deemed part of the Costs incurred in the Deepening or Plugging Back the then unrecovered portion of the Costs incurred in the initial Drilling of the well down to the pool or zone in which such well is completed as a producer of unitized substances as a result of such Deepening or Plugging Back.

**12.5 Effect of Reversion.** From and after reversion to a Non-Drilling Party of its relinquished interest in a well, such Non-Drilling Party shall share, on an Acreage Basis, in the ownership of the well, the operating rights and working interest therein, the materials and equipment in or pertaining to the well, the Production therefrom, and the Costs of operating the well.

**12.6 Rights and Obligations of Drilling Party.** The Drilling Party for whom a well is Drilled, Deepened, Plugged Back, or Completed shall pay and bear all Costs incurred therein and shall own the well, the materials and equipment in the well or pertaining thereto, and the Production therefrom, subject to reversion to each Non-Drilling Party of its relinquished interest in the well. If the well is a Development Well or results in the establishment or enlargement of a participating area to include the well, then, until reversion to a Non-Drilling Party of its relinquished interest, the Drilling Party shall pay and bear (a) that portion of the Costs incurred in operating the well that otherwise would be chargeable to such Non-Drilling Party, and (b) all Lease Burdens that are payable with respect to that portion of the Production from such well which is allocated to the acreage of such Non-Drilling Party. If the Drilling Party includes two or more Parties, the burdens imposed upon and the benefits accruing to the Drilling Party shall be shared by such Parties on an Acreage Basis among themselves.

**12.7 Accounting Due Non-Drilling Party.** In the event a relinquishment of interest by a Non-Drilling Party occurs pursuant to any provision of this Agreement with respect to any well and Production is had from such well, Unit Operator shall furnish each Non-Drilling Party, upon its request, all information referred to in Subdivision F of Section 16.1 and, in addition, the following:

A. an itemized statement of the Costs of the operation in which the Non-Drilling Party did not participate; and

B. until reversion occurs, a monthly itemized statement of the Costs incurred in operating said well, the quantity of Production obtained therefrom, the proceeds received from the sale of such Production, and the Lease Burdens paid with respect thereto.

**12.8 Stand-By Rig Time.** Stand-by time for the rig on a well for the period of time allowed for the initiation of a proposal and for the response thereto shall be charged and borne as part of the Costs incurred in the operation just completed. Stand-by time subsequent to said period of time shall be charged to and borne as Costs incurred in the proposed operation, unless no Party elected to participate therein.

**12.9 Subsequently Created Lease Burdens.** Anything herein to the contrary notwithstanding, if, subsequent to the date of this Agreement, any Party shall create an overriding royalty, production payment, net proceeds interest, carried interest, or any other interest out of its Committed Working Interest and at any time become a Non-Drilling Party with respect to any operation conducted under this Agreement, then the Drilling Party entitled to receive the share of Production to which the Non-Drilling Party would otherwise be entitled shall receive the same free and clear of any such burden, and the Non-Drilling Party who created such burden shall hold the Drilling Party harmless with respect thereto.

**ARTICLE 13**  
**ADJUSTMENT ON ESTABLISHMENT OR CHANGE OF**  
**PARTICIPATING AREA**

**13.1 When Adjustment Made.** Whenever, in accordance with the Unit Agreement, a participating area is established, or revised by contraction or enlargement, and whenever two or more participating areas are combined (the participating area resulting from such establishment, revision, or combination being hereinafter referred to as a "resulting area"), an adjustment shall be made in accordance with the succeeding provisions of this Article 13, as of the date on which the establishment, revision, or combination that creates such resulting area becomes effective, such date being hereinafter referred to as the "effective date" of such resulting area. For the purposes of this Article 13, all Costs of a usable well shall be deemed to have been incurred on the date the well was Completed.

**13.2 Definitions.** As used in this Article 13:

A. "Usable well" within a resulting area means a well which is either (1) completed in and capable of producing unitized substances from a pool or zone for which the resulting area was created or (2) used as a disposal well, injection well, or otherwise in connection with the production of unitized substances from such resulting area.

B. "Intangible value" of a usable well within a resulting area means the amount of those Costs incurred in Drilling, Completing, and Equipping such well, down to the deepest pool or zone for which such resulting area was created, which contribute to the production of unitized substances therefrom and which are properly classified as intangible costs in conformity with accounting practices generally accepted in the industry, reduced at the following rates for each month during any part of which such well was operated prior to the effective date of such resulting area:

- (1) 0.5 % per month for a cumulative total of 60 months, and
- (2) 0 % per month for each month in excess of said cumulative total.

C. "Tangible property" serving a resulting area means any kind of tangible property (whether or not in or pertaining to a well) which has been acquired for use in or in connection with the production of unitized substances from such resulting area or any portion thereof, and the cost of which has been charged as Costs pursuant to this Agreement.

D. "Value" of tangible property means the amount of Costs incurred in the construction or installation thereof (except installation costs properly classified as part of the intangible costs incurred in connection with a well), reduced, in the case of tangible property which is generally regarded as depreciable, at the rate of 0.5 % per month for each month during any part of which such well has been operated prior to the effective date of such resulting area.

**13.3 Method of Adjustment on Establishment or Enlargement.** As promptly as reasonably possible after the effective date of a resulting area created by the establishment or enlargement of a participating area, and as of such effective date, an adjustment shall be made in accordance with the following provisions, except to the extent otherwise specified in Section 13.6 :

A. The intangible value of each usable well within such resulting area on the effective date thereof shall be credited to the Party or Parties owning such well immediately prior to such effective date, in proportion to their respective interests in such well immediately prior to such effective date. The total amount so credited as the intangible value of usable wells shall be charged to all Parties within the resulting area on an Acreage Basis.

B. The value of each item of tangible property serving the resulting area on the effective date thereof shall be credited to the Party or Parties owning such item immediately prior to such effective date, in proportion to their respective interests in such item immediately prior to such effective date. The total amount so credited as the value of the tangible property shall be charged to all Parties within the resulting area on an Acreage Basis.

C. If a resulting area, on the effective date thereof, is served by any tangible property or usable well which also serves another participating area or other participating areas, the value of such tangible property and usable well (including the intangible value thereof) shall be determined in accordance with Subdivision D of Section 13.2, and such value shall be fairly apportioned between such resulting area and such other participating area or areas, provided that such apportionment receives the Approval of the Parties in each participating area concerned. That portion of the value of such tangible property and usable well (including the intangible value thereof) which is so apportioned to the resulting area shall be included in the adjustment made as of the effective date of such resulting area in the same manner as is the value of tangible property serving only the resulting area.

D. The credits and charges above provided for shall be made by Unit Operator in such manner that an adjustment shall be made for the intangible value of usable wells separate and apart from an adjustment for the value of tangible property. On each such adjustment, each Party who is charged an amount in excess of the amount credited to it shall pay to Unit Operator the amount of such excess, which shall be considered as Costs chargeable to such Party for all purposes of this Agreement; and such amount, when received by Unit Operator, shall be distributed or credited to the Parties who, in such adjustment, are credited with amounts in excess of the amounts charged to them respectively.

**13.4 Method of Adjustment on Contraction.** As promptly as reasonably possible after the effective date of a contraction of a participating area, an adjustment shall be made with each Party owning a



Committed Working Interest in land excluded from the participating area by such contraction (such Committed Working Interest being hereinafter in this Section referred to as "excluded interest") in accordance with the following provisions:

A. An adjustment for intangibles shall be made in accordance with Subdivision B of this Section 13.4, and a separate adjustment for tangibles shall be made in accordance with Subdivision C of this Section 13.4.

B. Such Party shall be credited with the sum of (1) the total amount theretofore charged against such Party with respect to its excluded interest, pursuant to the provisions of Exhibit 1, as intangible Costs incurred in the development and operation of the participating area prior to the effective date of such contraction, plus (2) the total amount charged against such Party with respect to such excluded interest as intangible value of usable wells in any previous adjustment or adjustments made upon the establishment or revision of such participating area. Such Party shall be charged with the sum of (1) the market value of that portion of the Production from such participating area which, prior to the effective date of such contraction, was delivered to such Party with respect to such excluded interest, less the amount of Lease Burdens and taxes paid or payable on said portion, plus (2) the total amount credited to such Party with respect to such excluded interest as intangible value of usable wells in any previous adjustment or adjustments made upon the establishment or revision of such participating area. Any difference between the amount of said credit and the amount of said charge shall be adjusted as hereinafter provided.

C. Such Party shall be credited with the sum of (1) the total amount theretofore charged against such Party with respect to its excluded interest, pursuant to the provisions of Exhibit 1, as Costs other than intangible Costs incurred in the development and operation of the participating area prior to the effective date of such contraction, plus (2) the total amount charged against such Party with respect to its excluded interest as value of tangible property in any previous adjustment or adjustments made upon the establishment or revision of such participating area, plus (3) the excess, if any, of the credit provided for in Subdivision B of this Section 13.4 over the charge provided for in said Subdivision B. Such Party shall be charged with the sum of (1) the excess, if any, of the charge provided for in said Subdivision B over the credit therein provided for, plus (2) the total amount credited to such Party with respect to its excluded interest as value of tangible property in any previous adjustment or adjustments made upon the establishment or revision of such participating area.

D. If the charge provided for in Subdivision C of this Section 13.4 is equal to or greater than the credit therein provided for, no adjustment shall be made with such Party. However, if the credit provided for in said Subdivision C is in excess of the charge therein provided for, such excess shall be charged on an Acreage Basis against Parties who remain in the participating area after such contraction and shall be paid by said Parties to Unit Operator upon receipt of invoices therefor. Such payments, when received by Unit Operator, shall be paid by it to the Party owning such excluded interest.

**13.5 Ownership of Wells and Tangible Property.** From and after the effective date of a resulting area, all usable wells within such resulting area and all tangible property serving such resulting area shall be owned by the Parties within such area on an Acreage Basis, except that (a) in the case of tangible property serving a participating area or participating areas in addition to the resulting area, only that undivided interest therein which is proportionate to that portion of the value thereof which is included in the adjustment provided for shall be owned by the Parties within the resulting area on an Acreage Basis, and (b) if a Party within the resulting area was a Non-Drilling Party for a well which is a usable well within such resulting area on the effective date thereof, and if the relinquished interest of such Non-Drilling Party in such well has not reverted to it prior to such effective date, the Drilling Party for such well shall own the interest therein that would otherwise be owned by such Non-Drilling Party until reversion to such Non-Drilling Party of its relinquished interest in such well.

**13.6 Relinquished Interest of Non-Drilling Parties.** If the interest relinquished by a Non-Drilling Party in a well which is a usable well within a resulting area on the effective date thereof has not reverted to it prior to such effective date, then insofar, but only insofar, as they relate to such well, the adjustments provided for in Section 13.3 shall be subject to the following provisions, wherein the sum of the intangible value of such well, plus the value of the tangible property in or pertaining thereto, is referred to as the "value" of such well:

A. The Drilling Party for such well shall be charged with that part of the value of the well that would otherwise be chargeable to such Non-Drilling Party with respect to (1) such Non-Drilling Party's Committed Working Interest or Interests in the participating area in which the well was Drilled, as such participating area existed when the Drilling of the well was commenced, if the well was Drilled as a Development Well, or (2) the Committed Working Interest or Interests of such Non-Drilling Party which entitled it to participate in the Drilling, Deepening, Plugging Back, or Completion of the well, if it was Drilled, Deepened, Plugged Back, or Completed otherwise than as a Development Well. However, such Non-Drilling Party shall be charged with such part, if any, of the value of such well as is chargeable to it, in accordance with Subdivisions A and B of Section 13.3, with respect to its Committed Working Interests other than those referred to in (1) and (2) above.

B. If that part of the value of such well which would have been credited to such Non-Drilling Party if the well had been Drilled, Deepened, Plugged Back, or Completed for the account of all Parties entitled to participate therein exceeds the amount provided in Subdivision A of this Section 13.6 to be charged against the Drilling Party, such excess shall be applied against the reimburse-

ment to which the Drilling Party is entitled out of Production that would otherwise accrue to such Non-Drilling Party. Any balance of such excess over the amount necessary to complete such reimbursement shall be credited to such Non-Drilling Party.

#### ARTICLE 14 SUPERVISION OF OPERATIONS BY PARTIES

**14.1 Right of Supervision.** Each operation conducted by Unit Operator under this Agreement or the Unit Agreement shall be subject to supervision and control in accordance with the succeeding provisions of this Article 14 by the Parties who are chargeable with the Costs thereof.

**14.2 Voting Control.** In the supervision of an operation conducted by Unit Operator, the Parties chargeable with the Costs of such operation shall have the right to vote in proportion to their respective obligations for such Costs. The Parties having the right to vote on any other matter shall vote thereon on an Acreage Basis. Except as provided for in the Unit Agreement and except as otherwise specified in this Agreement (particular reference being made to Section 25.1, Section 27.1, and that portion of Section 11.5 relating to abandonment of producing wells outside of a participating area), the affirmative vote of Parties having 65 % or more of the voting power on any matter which is proper for action by them shall be binding upon all Parties entitled to vote thereon; provided, however, if one Party voting in the affirmative has 65 % or more but less than 75 % of the voting power, the affirmative vote of such Party shall not be binding upon the Parties entitled to vote thereon unless its vote is supported by the affirmative vote of at least one additional Party; and provided further, that if one Party voting in the negative or failing to vote has more than 35 % but less than 50% of the voting power, the affirmative vote of the Parties having a majority of the voting power shall be binding upon all Parties entitled to vote unless there is a negative vote of at least one additional Party. In the event only two Parties are entitled to vote, the vote of the one with the greater interest shall prevail. If only one Party is entitled to vote, such Party's vote shall control. A Party failing to vote shall not be deemed to have voted either in the affirmative or in the negative. Any Approval or Direction provided for in this Agreement which receives the affirmative vote above specified shall be deemed given by and shall be binding upon all Parties entitled to vote thereon, except where the vote of a larger percentage is specifically required.

**14.3 Meetings.** Any matter which is proper for consideration by the Parties, or any of them, may be considered at a meeting held for that purpose. A meeting may be called by Unit Operator at any time, and a meeting shall be called by Unit Operator upon written request of any Party having voting power on any matter to be considered at the meeting. At least ten (10) days in advance of each meeting, Unit Operator shall give each Party entitled to vote thereat notice of the time, place, and purpose of the meeting. Unit Operator's representative shall be the Chairman of such meeting.

**14.4 Action Without Meeting.** In lieu of calling a meeting, Unit Operator may submit any matter which is proper for consideration by the Parties, or any of them, by giving to each such Party notice, describing in adequate detail the matter so submitted. Each Party entitled to vote on any matter so submitted shall communicate its vote thereon to Unit Operator within such period as may be designated in the notice given by Unit Operator (which period shall be not less than ten (10) nor more than thirty (30) days); provided, however, if, within ten (10) days after submission of such matter, request is made for a meeting in accordance with Section 14.3, such matter shall be considered only at a meeting called for that purpose. If a meeting is not required, then, at the expiration of the period designated in the notice given by it, Unit Operator shall give to each Party entitled to vote thereon notice, stating the tabulation and result of the vote.

**14.5 Representatives.** Promptly after execution of this Agreement, each Party, by notice to all other Parties, shall designate a representative authorized to vote for such Party and may designate an alternate authorized to vote for such Party in the absence of its representative. Any such designation of a representative or alternate representative may be revoked at any time by notice given to all other Parties, provided such notice designates a new representative or alternate representative, as the case may be.

**14.6 Audits.** Audits may be made of Unit Operator's records and books of account pertaining to operations hereunder, as provided in Exhibit 1.

**14.7 Extraneous Projects.** Nothing contained in this Agreement shall be deemed to authorize the Parties, by vote or otherwise, to act upon any matter or to authorize any expenditure unless such matter or expenditure relates to the conduct of operations authorized by the Unit Agreement or this Agreement.

#### ARTICLE 15 UNIT OPERATOR'S POWERS AND RIGHTS

**15.1 In General.** Subject to the limitations set forth in this Agreement, all operations authorized by the Unit Agreement and this Agreement shall be managed and conducted by Unit Operator. Unit Operator shall have exclusive custody of all materials, equipment, and any other property used in connection with any operation within the Unit Area.

**15.2 Employees.** 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.

**15.3 Non-Liability.** Unit Operator shall not be liable to any Party for anything done or omitted to be done by it in the conduct of operations hereunder, except in case of bad faith.

**15.4 Force Majeure.** The obligations of Unit Operator hereunder shall be suspended to the extent

that, and only so long as, performance thereof is prevented by fire, action of the elements, strikes or other differences with workmen, acts of civil or military authorities, acts of the public enemy, restrictions or restraints imposed by law or by regulation or order of governmental authority, whether Federal, State, or local, inability to obtain necessary rights of access, or any other cause reasonably beyond the control of Unit Operator, whether or not similar to any cause above enumerated. Whenever performance of its obligations is prevented by any such cause, Unit Operator shall give notice thereof to the Parties as promptly as is reasonably practicable.

**15.5 Lien.** Each of the Parties hereby grants to Unit Operator a lien upon its Committed Working Interests, its interest in all jointly owned materials, equipment, and other property, and its interest in all Production, as security for payment of Costs chargeable to it, together with any interest payable thereon. In addition to Unit Operator's rights under the foregoing lien, and as a secured party, Unit Operator shall be entitled to the benefit of any statutory operator's lien provided for in the jurisdiction in which the Unit Area is located. Unit Operator may, but need not, bring an action at law or in equity to enforce collection of such indebtedness, with or without foreclosure of such lien, and, in addition, shall have all rights provided under the terms of the Uniform Commercial Code or of any other law. In addition to the foregoing, and not in limitation thereof, upon default by any Party in the payment of Costs chargeable to it, Unit Operator shall have the right to collect and receive proceeds from the purchaser of such Party's share of Production, up to the amount owing by such Party, plus interest at the rate of 12 % per annum until paid. Each such purchaser shall be entitled to rely upon Unit Operator's statement concerning the existence and amount of any such default. None of the remedies or rights specified above shall be deemed exclusive, and the exercise of any such remedy or right shall not be deemed an election of remedies and shall not affect enforceability of the foregoing lien or security interest.

**15.6 Advances.** Unit Operator, at its election, shall have the right from time to time to demand and receive from the Parties chargeable therewith payment in advance of their respective shares of the estimated amount of Costs to be incurred during any month, which right may be exercised only by submission to each such Party of a properly 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 for any month shall be submitted on or about the twentieth (20th) day of the next preceding month. The amount of each such invoice shall be payable within fifteen (15) days after receipt thereof and thereafter shall bear interest at the rate of 12 % per annum until paid. Proper adjustment shall be made monthly between such advances and Costs, to the end that each Party shall bear and pay its proportionate share of Costs incurred and no more. Unit Operator may request advance payment or security for the total estimated Costs to be incurred in a particular Drilling, Deepening, Plugging Back, or Completing operation and, notwithstanding any other provisions of this Agreement, shall not be obligated to commence such operation unless and until such advance payment is made or Unit Operator is furnished security acceptable to it for such payment by the Party or Parties chargeable therewith.

**15.7 Use of Unit Operator's Drilling Equipment.** Any Drilling, Deepening, or Plugging Back operation conducted hereunder may be conducted by Unit Operator with its own tools and equipment, provided that the rates to be charged and the applicable terms and conditions are set forth in a form of drilling contract which receives the Approval of the Party or Parties chargeable with the Costs of such operation, except that in any case where Unit Operator alone constitutes the Drilling Party, such form shall receive the Approval of the Parties within the participating area or other designated area for such well prior to the commencement of such operation.

**15.8 Rights as Party.** As an owner of a Committed Working Interest, the Party acting as Unit Operator shall have the same rights and obligations hereunder as if it were not Unit Operator. In each instance where this Agreement requires or permits a Party to give notice, consent, or approval to Unit Operator, such notice, consent, or approval shall be deemed properly given by the Party acting as Unit Operator if and when given to all other Parties entitled to give or receive such notice, consent, or approval.

## ARTICLE 16 UNIT OPERATOR'S DUTIES

**16.1 Specific Duties.** In the conduct of operations hereunder, Unit Operator shall:

**A. Drilling of Wells.** Drill, Deepen, Plug Back, or Complete a well or wells only in accordance with the provisions of this Agreement.

**B. Compliance with Laws and Agreements.** Comply with the provisions of the Unit Agreement, all applicable laws and governmental regulations (whether Federal, State, or local), and Directions of the Parties pursuant to this Agreement. In case of conflict between such Directions and the provisions of the Unit Agreement or such laws or regulations, the provisions of the Unit Agreement or such laws or regulations shall govern.

**C. Consultation with Parties.** Consult freely with the Parties within the area affected by any operation hereunder and keep them advised of all matters arising in operations hereunder which Unit Operator deems important, in the exercise of its best judgment.

**D. Payment of Costs.** Pay all costs incurred in operations hereunder promptly as and when due and payable and keep the Committed Working Interests and all property used in connection with operations under this Agreement free from liens which may be claimed for the payment of such Costs, except any such lien which it disputes, in which event Unit Operator may contest the disputed lien upon giving notice thereof to the Parties affected thereby.

**E. Records.** Keep full and accurate records of all Costs incurred and of all controllable materials and equipment, which records, and receipts and vouchers in support thereof, shall be available for inspection by authorized employees or agents of the Parties at reasonable intervals during usual business hours at the office of Unit Operator.

**F. Information.** Furnish promptly to each Party chargeable with Costs of the operation involved ~~and to each additional Party who makes timely written request therefor~~ (1) copies of Unit Operator's authorizations for expenditures or itemizations of estimated expenditures in excess of Fifty Thousand Dollars (\$50,000.00), (2) copies of all drilling reports, well logs, and State and Federal reports, (3) samples of cores and cuttings taken from wells Drilled hereunder, to be delivered at the well in containers furnished by the Party requesting same, and (4) such other and additional information or reports as may be required by Direction of the Parties within the area affected. If multiple copies of any such materials are requested by any Party, Unit Operator may charge the cost thereof directly to the requesting Party.

**G. Access to Unit Area.** Permit each Party, <sup>chargeable with the costs of the operation in-</sup> through its authorized employees or agents, but at <sup>volved</sup> such Party's 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 materials, equipment, or other property used in connection with operations under this Agreement and to have access at reasonable times to information and data in the possession of Unit Operator concerning Unit operations.

#### 16.2 Insurance.

**A. Unit Operator's.** Unit Operator shall comply with the Workmen's Compensation Law of the State in which the Unit Area is located. Unit Operator shall also maintain in force at all times with respect to operations hereunder such other insurance, if any, as may be required by law. In addition, Unit Operator shall maintain such other insurance, if any, as is described in Exhibit 3 or as receives the Approval of the Parties from time to time. Unit Operator shall carry no other insurance for the benefit of the Parties, except as above specified. Upon request of any Party, Unit Operator shall furnish evidence of insurance carried by it with respect to operations hereunder.

**B. Contractors'.** Unit Operator shall require all contractors engaged in operations under this Agreement to comply with the Workmen's Compensation Law of the State in which the Unit Area is located and to maintain such other insurance as may be required by Direction of the Parties.

**C. Automotive Equipment.** In the event Automobile Public Liability insurance is specified in Exhibit 3 or subsequently receives the Approval of the Parties, no direct charge shall be made by Unit Operator for premiums paid for such insurance for Unit Operator's fully owned automotive equipment.

**16.3 Non-Discrimination.** In connection with the performance of work under this Agreement, Unit Operator agrees to comply with the provisions of Exhibit 4.

Unit Operator agrees to insert non-discrimination provisions in all subcontracts hereunder, as required by law or regulation.

**16.4 Drilling Contracts.** Each Drilling, Deepening, Plugging Back, or Completing operation conducted hereunder, and not performed by Unit Operator with its own tools and equipment in accordance with Section 15.7, shall be performed by a reputable drilling contractor having suitable equipment and personnel, under written contract between Unit Operator and the contractor, at the most favorable rates and on the most favorable terms and conditions bid, if bids were obtained, but otherwise at rates and on terms and conditions receiving the Approval of the Parties.

**16.5 Uninsured Losses.** Any and all payments made by Unit Operator in the settlement or discharge of any liability to third persons (whether or not reduced to judgment) arising out of an operation conducted hereunder and not covered by insurance herein provided for shall be charged as Costs and borne by the Party or Parties for whose account such operation was conducted.

### ARTICLE 17 LIMITATIONS ON UNIT OPERATOR

**17.1 Specific Limitations.** In the conduct of operations hereunder, Unit Operator shall not, without first obtaining the Approval of the Parties:

**A. Change in Operations.** Make any substantial change in the basic method of operation of any well, except in the case of an emergency.

**B. Limit on Expenditures.** Undertake any project reasonably estimated to require an expenditure in excess of Fifty Thousand Dollars (\$50,000.00) provided, however, that (1) Unit Operator is authorized to make all usual and customary operating expenditures that are required in the normal course of producing operations, (2) whenever Unit Operator is authorized to conduct a Drilling, Completing, or Deepening or Plugging Back operation, or to undertake any other project, in accordance with this Agreement, Unit Operator shall be authorized to make all reasonable and necessary expenditures in connection therewith, and (3) in case of emergency, Unit Operator may make such immediate expenditures as may be necessary for the protection of life or property, but notice of such emergency shall be given to all Parties as promptly as reasonably possible.

**C. Partial Relinquishment.** Make any partial relinquishment of its rights as Unit Operator, appoint any sub-operator, or execute any Designation of Agent.

D. **Settlement of Claims.** Pay in excess of Five Thousand Dollars (\$5,000.00) in settlement of any claim (other than Workmen's Compensation claims) for injury to or death of persons or for loss of or damage to property.

E. **Determinations.** Make any of the determinations provided in the Unit Agreement to be made by Unit Operator, except as otherwise specified in this Agreement.

## ARTICLE 18 TITLES

18.1 **Representation of Ownership.** Each Party represents to all other Parties that, to the best of its knowledge and belief, its ownership of Committed Working Interests in the Unit Area is that set out in Exhibit B to the Unit Agreement. If it develops that any such ownership is incorrectly stated, the rights and responsibilities of the Parties shall be governed by the provisions of this Article 18, but such erroneous statement shall not be a cause for canceling or terminating this Agreement.

### 18.2 Title Papers to be Furnished.

A. **Lease Papers.** Each Party, after executing this Agreement, shall upon request promptly furnish Unit Operator with copies of all leases, assignments, options, and other contracts which it has in its possession relating to its Committed Working Interests.

B. **Title Papers for Initial Test Well.** Promptly after the effective date of this Agreement each Party within the area described as the Title Examination Area in Exhibit 2 shall, at its own expense but without responsibility for the accuracy thereof, furnish Unit Operator with the following title materials relating to all lands within such area in which it owns Committed Working Interests:

- (1) Abstracts of title based upon the County records, certified to the current date;
- (2) All lease papers, or copies thereof, mentioned in Subdivision A of this Section 18.2 which the Party has in its possession and which have not been previously furnished to Unit Operator;
- (3) Copies of any title opinions which the Party has in its possession;
- (4) If Federal lands are involved, status reports of current date, setting forth the entries found in the District Land Office for such lands, and also certified copies of the Serial Registers for the Federal leases involved;
- (5) If State lands are involved, status reports of current date, setting forth the entries found in the State records for such lands; and
- (6) If Indian lands are involved, status reports of current date, setting forth the entries found in the office of the Superintendent of the Indian Agency and in the Area Office for such lands.

C. **Title Papers for Subsequent Wells.** Any Party who proposes the Drilling of a Subsequent Test Well or Exploratory Well shall, at the time of giving notice for such proposed well, designate a title examination area not exceeding 2,560 acres and not including any lands within a participating area. When the Drilling of a Development Well receives the Approval of the Parties within the participating area in which it is to be Drilled, a title examination area covering lands outside any participating area may be designated by the Approval of such Parties. Each Party within any such title examination area shall, at its own expense and upon request, furnish Unit Operator with the title materials listed in Subdivision B of this Section 18.2 not previously furnished, relating to all lands within such area in which it owns Committed Working Interests.

D. **Title Papers on Establishment or Enlargement of a Participating Area.** Upon the establishment or the enlargement of a participating area, each Party shall promptly furnish Unit Operator all the title materials listed in Subdivision B of this Section 18.2 not previously furnished, relating to all its Committed Working Interests in the lands lying within such participating area as established or enlarged.

18.3 **Title Examination.** Promptly after all title materials delivered pursuant to Section 18.2 have been received, Unit Operator shall deliver the same to an attorney or attorneys approved by the Parties within the title examination area. Unit Operator shall arrange to have said materials examined promptly by such attorney or attorneys and shall distribute copies of title opinions to all Parties within the title examination area as soon as they are received. Each Party shall be responsible, at its expense, for curing its own titles. After a reasonable time, not exceeding thirty (30) days, has been allowed for any necessary curative work, Unit Operator shall submit to each Party written recommendations for approval or disapproval of the title to each Committed Working Interest involved, and thereafter the Parties shall advise Unit Operator in writing, within fifteen (15) days after receipt of such recommendations, of approval or disapproval of titles. Unless otherwise agreed, the cost of all title examinations made under this Section 18.3 shall be charged as part of the Costs of Drilling the well for which such title examination was made.

18.4 **Option for Additional Title Examination.** Any Party who furnishes materials for title examination pursuant to Section 18.2 shall have the right to examine all materials furnished Unit Operator. If such additional, independent title examination is elected, it shall be at the sole cost and expense of the Party electing to perform the same; and such Party shall bear any expense which may be necessary to reproduce title materials for its use, if required. Whether or not such additional title examination is elected, each Party shall have the right to approve or disapprove titles according to the provisions of this Article 18.

18.5 **Approval of Titles Prior to Drilling.** Where the Committed Working Interests within a title

examination area are owned by more than one Party, no Drilling shall be conducted in such area until titles to the Committed Working Interests therein have received the Approval of the Parties as hereinafter in this Section provided. If a Drilling Block has been designated for the Drilling of a well, such well shall not be Drilled until titles to the Committed Working Interests within the title examination area established for such well have received the Approval of the Parties within the Drilling Block in which such well is to be Drilled. Approval of title to lands within a Drilling Block shall be binding upon all Parties owning Committed Working Interests within such Drilling Block. If lands outside a participating area are included in the title examination area for a Development Well, such well shall not be Drilled until titles to the Committed Working Interests within such title examination area have received the Approval of the Parties therein. In the event Approval of the Parties is not obtained as in this Section 18.5 provided, the Drilling Party (whether one or more) may proceed with the Drilling of the well; but said Drilling Party (a) shall, by so proceeding, assume all risk attending the failure to obtain such approval to the same extent as if approval of titles to all lands within the Drilling Block (if one has been established) or within the title examination area (in all other instances) had been obtained, and (b) shall also be deemed to have given its approval to the titles to all lands within the Drilling Block (if one has been established) or within the title examination area (in all other instances).

**18.6 Approval of Titles Prior to Inclusion of Land in a Participating Area.** Where the Committed Working Interests within a participating area are owned by more than one Party, no Committed Working Interest shall be included within said participating area or be entitled to participate in the Production of unitized substances from said participating area until title to such Committed Working Interest has received the Approval of the Parties within said participating area. Approval of titles to lands within a participating area shall be binding upon all Parties within such participating area and all Parties coming within such participating area upon any enlargement thereof.

**18.7 Failure of Title to Committed Working Interest Before Approval.** If title to a Committed Working Interest shall fail in whole or in part prior to receiving the Approval of the Parties, the Parties who improperly claimed said interest shall sustain the entire loss occasioned by such failure of title and do hereby expressly relieve and indemnify Unit Operator and all other Parties from and against any and all liability on account thereof.

**18.8 Failure of Title to Committed Working Interest After Approval.** If title to a Committed Working Interest which has received the Approval of the Parties under Section 18.5 fails in whole or in part at a time when the tract affected thereby is within an active Drilling Block or within a Drilling Block upon which a well has been completed otherwise than as a producer of unitized substances in paying quantities, or if title to a Committed Working Interest which has received the Approval of the Parties under Section 18.6 fails in whole or in part at a time when the tract affected thereby is within a participating area, then:

A. the loss, the cost of litigation, and any ensuing liability shall be borne by the Parties having interests in the affected participating area or Drilling Block (including the Party whose Committed Working Interest has been lost and including the acreage of such Committed Working Interest);

B. there shall be relinquished to the Party whose Committed Working Interest has been lost such proportionate part of each of the other Committed Working Interests in the lands within such affected participating area or Drilling Block, subject to a like proportion of their respective Lease Burdens, as may be necessary to make the loss of such Committed Working Interest a joint loss of the Parties within such participating area or Drilling Block; and

C. the relinquished portions of said Committed Working Interests (subject to their proportionate part of the Lease Burdens attributable thereto) shall be deemed owned by the Party receiving same.

**18.9 Joinder by True Owner.** If title to a Committed Working Interest fails in whole or in part, such Committed Working Interest shall no longer be subject to this Agreement or the Unit Agreement. The true owner of a Committed Working Interest, title to which has failed, may join in this Agreement or enter into a separate Operating Agreement with the Parties to this Agreement upon such terms and conditions as receive the Approval of the Parties within the Unit Area and subject to any valid claims by the true owner.

**18.10 Title Challenge.** In the event of any suit or action challenging the title of any Party to any of the oil and gas rights committed by said Party to this Agreement and to the Unit Agreement, the Party served will immediately notify the other Parties, and the Party whose title has been challenged shall forthwith take over and be in charge of the conduct of the litigation and shall bear the entire cost of such litigation, unless the title has previously received the Approval of the Parties, in which event the provisions of Section 18.8 shall apply.

## ARTICLE 19 UNLEASED INTERESTS

**19.1 Treated as Leased.** If a Party owns in fee all or any part of the oil and gas rights in any tract within the Unit Area which is not subject to any oil and gas lease or other contract in the nature thereof, such Party shall be deemed to own a Committed Working Interest in such tract and also a royalty interest therein in the same manner as if such Party's oil and gas rights in such tract were covered by the form of oil and gas lease attached as Exhibit 5.

**19.2 Execution of Lease.** In any provision of this Agreement where reference is made to an assignment or conveyance by any Party of its Committed Working Interest to any other Party, each such reference as to any Party owning an unleased interest shall be interpreted to mean that such Party shall



execute an oil and gas lease to such other Party in the form of Exhibit 5, which shall satisfy the requirement for an assignment or conveyance of a Committed Working Interest.

## ARTICLE 20 RENTALS AND LEASE BURDENS

20.1 **Rentals.** Each Party shall be obligated to pay any and all rentals and other sums (other than Lease Burdens) payable upon or with respect to its Committed Working Interests, subject, however, to the right of each Party to surrender any of its Committed Working Interests in accordance with Article 27. Upon request, each Party shall furnish to Unit Operator satisfactory evidence of the making of such payments. However, no Party shall be liable to any other Party for unintentional failure to make any such payment, provided it has acted in good faith.

20.2 **Lease Burdens.** Each Party entitled to receive a share of Production shall be obligated for any and all payments, whether in cash or in kind, accruing to any and all Lease Burdens, net profits interests, carried interests, and any similar interest payable with respect to such share or the proceeds thereof; provided, however, at any time any such Party entitled to receive Production is not taking in kind or separately disposing of its share, that portion of such Production or the proceeds thereof (at the option of such Party) accruing to such Lease Burdens shall, upon request, be distributed to such Party.

20.3 **Loss of Committed Working Interest.** If a Committed Working Interest is lost through failure to make any payment above provided to be made by the Party owning the same, such loss shall be borne entirely by such Party; provided, however, if the Committed Working Interest so lost covers land within a participating area, the provisions of Section 18.8 shall apply.

## ARTICLE 21 TAXES

21.1 **Payment.** Any and all ad valorem and severance taxes payable upon Committed Working Interests (and upon Lease Burdens which are not payable by the owners thereof) or upon materials, equipment, or other property acquired and held by Unit Operator hereunder, and any and all taxes (other than income taxes) upon or measured by unitized substances produced from the Unit Area which are not payable by the purchaser or purchasers thereof or by the owner of Lease Burdens shall be paid by Unit Operator as and when due and payable.

21.2 **Apportionment.** Taxes upon materials, equipment, and other property acquired and held by Unit Operator hereunder shall be charged to and borne by the Parties owning the same in proportion to their respective interests therein. All taxes paid by Unit Operator upon or measured by the value of Production shall be charged to and borne by the Parties owning the same in the same proportions as the assessed values of their respective portions of such Production bear to the whole thereof. All other taxes paid by Unit Operator shall be charged to and borne by the Parties in proportion to their ownership in the Committed Working Interests or unitized substances (as the case may be) upon which or with respect to which such taxes are paid. All reimbursements from owners of Lease Burdens, whether obtained in cash or by deduction from Lease Burdens, on account of any taxes paid for such owners shall be paid or credited to the Parties in the same proportions as such taxes were charged to such Parties.

21.3 **Transfer of Interests.** In the event of a transfer by one Party to another under the provisions of this Agreement of any Committed Working Interest or of any other interest in any well or in the materials and equipment in any well, or in the event of the reversion of any relinquished interest as in this Agreement provided, the taxes above mentioned assessed against the transferred or reverted interest for the taxable period in which such transfer or reversion occurs shall be apportioned among said Parties so that each shall bear the percentage of such taxes which is proportionate to that portion of the taxable period during which it owned such interest.

21.4 **Notices and Returns.** Each Party shall promptly furnish Unit Operator with copies of notices, assessments, levies, or tax statements received by it pertaining to the taxes to be paid by Unit Operator. Unit Operator shall make such returns, reports, and statements as may be required by law in connection with any taxes above provided to be paid by it and shall furnish copies to the Parties upon request. It shall notify the Parties of any tax which it does not propose to pay before such tax becomes delinquent.

## ARTICLE 22 WITHDRAWAL OF TRACTS AND UNCOMMITTED INTERESTS

22.1 **Right of Withdrawal.** If the owner of any substantial interest in a tract within the Unit Area fails or refuses to join in the Unit Agreement, then such tract may be withdrawn from the Unit Agreement, as provided in the Unit Agreement.

22.2 **Non-Withdrawal.** Should the Party or Parties having the right under the Unit Agreement to withdraw a tract from the Unit Agreement fail to exercise such right, then all payments and liabilities accruing to the owners of uncommitted interests in such tract shall be paid and borne by such Party or Parties.

## ARTICLE 23 COMPENSATORY ROYALTIES

23.1 **Notice.** Whenever demand is made in accordance with the Unit Agreement for the payment of compensatory royalties, Unit Operator shall give notice thereof to each Party affected by the demand.

23.2 **Demand for Failure to Drill a Development Well.** If the demand for compensatory royalties results from the failure to have Drilled a Development Well and such well is not Drilled, then Unit

Operator shall pay such compensatory royalties. Such payment shall be charged as Costs incurred in operations within the participating area involved.

**23.3 Demand for Failure to Drill a Well Other Than a Development Well.** If the demand for compensatory royalties results from the failure to have Drilled a well other than a Development Well and such well is not Drilled, then Unit Operator shall pay such compensatory royalties. Such payment shall be chargeable to and borne by the Parties who would be obligated to bear the Costs of such well if the well were Drilled as a Required Well under Subdivision B of Section 10.4.

#### **ARTICLE 24 SEPARATE MEASUREMENT AND SALVAGE**

**24.1 Separate Measurement.** If a well completed as a producer of unitized substances is in or becomes included in a participating area but is not owned on an Acreage Basis by all the Parties within such participating area and if, within thirty (30) days after request therefor by any interested Party, a method of measuring the Production from such well without the necessity of additional facilities does not receive the Approval of the Parties, then Unit Operator shall install such additional tankage, flow lines, or other facilities for separate measurement of the unitized substances produced from such well as Unit Operator may deem suitable. The Costs of such facilities for separate measurement shall be charged to and borne by the Drilling Party for such well and treated as Costs incurred in operating such well, notwithstanding any other provisions of this Agreement.

**24.2 Salvaged Materials.** If any materials or equipment are salvaged from a well completed as a producer after being Drilled, Deepened, Plugged Back, or Completed otherwise than for the account of all the Parties entitled to participate therein before reversion to the Non-Drilling Party of its relinquished interest in the well, the proceeds derived from the sale thereof or, if not sold, the Salvage Value thereof, shall be treated in the same manner as proceeds of Production from such well for the purpose of determining reversion to the Non-Drilling Party of its relinquished interest in such well.

#### **ARTICLE 25 ENHANCED RECOVERY AND PRESSURE MAINTENANCE**

**25.1 Consent Required.** Unit Operator shall not undertake any program of enhanced recovery or pressure maintenance involving injection of gas, water, or other substance by any method, whether now known or hereafter devised, without first obtaining the consent of Parties owning, on an Acreage Basis, not less than 90 % of the Committed Working Interests in the participating area affected by any such program. After the Parties have voted to undertake a program of enhanced recovery or pressure maintenance in accordance with this Section 25.1, the conduct of such program shall be subject to supervision by the Parties as set forth in Article 14.

**25.2 Above-Ground Facilities.** This Agreement shall not be deemed to require any Party to participate in the construction or operation of any gasoline plant, sulphur recovery plant, dewaxing plant, or other above-ground facilities to process or otherwise treat Production, other than such facilities as may be required for treating Production in ordinary lease operations and such facilities as may be required in the conduct of operations authorized under Section 25.1.

#### **ARTICLE 26 TRANSFERS OF INTEREST**

**26.1 Sale by Unit Operator.** If Unit Operator sells all its Committed Working Interests, it shall resign and a new Unit Operator shall be selected as provided in the Unit Agreement.

**26.2 Assumption of Obligations.** No transfer of any Committed Working Interest shall be effective unless the same is made expressly subject to the Unit Agreement and this Agreement and the transferee agrees in writing to assume and perform all obligations of the transferor under the Unit Agreement and this Agreement insofar as they relate to the interest assigned, except that such assumption of obligations shall not be required in case of a transfer by mortgage or deed of trust as security for indebtedness.

**26.3 Effective Date.** A transfer of Committed Working Interests shall not be effective as among the Parties until the first day of the month next following the delivery to Unit Operator of the original or a certified copy of the instrument of transfer conforming to the requirements of Section 26.2. In no event shall a transfer of Committed Working Interests relieve the transferring Party of any obligations accrued under this Agreement prior to said effective date, for which purpose any obligation assumed by the transferor to participate in the Drilling, Deepening, Plugging Back, or Completing of a well prior to such effective date shall be deemed an accrued obligation.

#### **ARTICLE 27 RELEASE FROM OBLIGATIONS AND SURRENDER**

**27.1 Surrender or Release Within Participating Area.** A Committed Working Interest in land within a participating area shall not be surrendered except with the consent of all Parties within such participating area. However, a Party who owns a Committed Working Interest in land within a participating area and who is not at the time committed to participate in the Drilling, Deepening, Plugging Back, or Completing of a well within such participating area may be relieved of further obligations with respect to such participating area, as then constituted, by executing and delivering to Unit Operator an assignment conveying to all other Parties within such participating area all Committed Working Interests owned by such Party in lands within the participating area, together with the



entire interest of such Party in any and all wells, materials, equipment, and other property within or pertaining to such participating area.

**27.2 Procedure on Surrender or Release Outside Participating Area.** Whenever a Party or Parties owning 100% of the Committed Working Interest in any tract which is not within any participating area desire to surrender said 100% interest, such Party or Parties shall give to all other Parties notice thereof, describing such Committed Working Interest. The Parties receiving such notice, or any of them, shall have the right at their option to take from the Party or Parties desiring to surrender an assignment of such Committed Working Interest by giving the Party or Parties desiring to surrender notice of election so to do within thirty (30) days after receipt of notice of the desire to surrender. If such election is made as above provided, the Party or Parties taking the assignment (which shall be taken by them in proportion to the acreage of their respective Committed Working Interests among themselves in the Unit Area) shall pay the assigning Party or Parties for its or their share of the Salvage Value of all wells, if any, in which the assigning Party or Parties own an interest and which are located on the land covered by such Committed Working Interest, which payment shall be made upon receipt of the assignment. If no Party elects to take such assignment within said thirty (30) day period, then the Party or Parties owning such Committed Working Interest may surrender the same, if surrender thereof can be made in accordance with the Unit Agreement. Whenever a Party owning less than 100% of the Committed Working Interest in any tract desires to surrender its interest therein, such interest may be acquired by the other Party or Parties owning Committed Working Interests in said tract without notice being given to any other Parties owning interests within the Unit Area. In the event the other Party or Parties owning Committed Working Interests in the tract to be surrendered do not desire to acquire such interest, the interest shall be treated as a 100% interest.

**27.3 Accrued Obligations.** A Party making an assignment or surrender in accordance with Section 27.1 or Section 27.2 shall not be relieved of its liability for any obligation accrued under this Agreement at the time the assignment or surrender is made or of the obligation to bear its share of the Costs incurred in any Drilling, Deepening, Plugging Back, or Completing operation in which such Party had elected to participate prior to the making of such assignment or surrender, except to the extent that the Party or Parties receiving such assignment shall assume, with the Approval of the Parties, any and all obligations of the assigning Party under this Agreement and under the Unit Agreement.

## ARTICLE 28 LIABILITY

**28.1 Liability.** The liability of the Parties hereunder shall be several and not joint or collective. Each Party shall be responsible only for its obligations as herein set out.

**28.2 No Partnership Created.** It is not the intention of the Parties to create, nor shall this Agreement or the Unit Agreement be construed as creating, a mining or other partnership or association between the Parties or as rendering them liable as partners or associates.

**\* 28.3 Election.** Each of the Parties hereby elects, under the authority of Section 761(a) of the Internal Revenue Code of 1954, to be excluded from the application of all the provisions of Subchapter K of Chapter 1 of Subtitle A of the Internal Revenue Code of 1954. In making this election, each Party states that income derived by it from operations under this Agreement can be adequately determined without computation of partnership taxable income. If the income tax laws of the State or States in which the Unit Area is located contain, or hereafter contain, provisions similar to those contained in the Subchapter of the Internal Revenue Code of 1954 above referred to under which a similar election is permitted, each of the Parties agrees that such election shall be exercised; and should the income tax laws of such State or States require evidence of such election, Unit Operator is authorized and directed to execute the same on behalf of each Party. Beginning with the first taxable year of operation under this Agreement, each Party agrees that the deemed election provided by Federal Regulations Section 1.761-2(b)(2)(ii) will apply, and no Party will file an application under Federal Regulations Section 1.761-2(b)(3)(i) to revoke said election. \*See page 22.

## ARTICLE 29 NOTICES

**29.1 Giving and Receipt.** Whenever a rig is on location, every notice and every response shall be by telephone, to be confirmed promptly in writing. In all other instances, any notice, response, consent, advice, or statement herein provided or permitted to be given shall be in writing and shall be deemed given only when received by the Party to whom the same is directed.

**29.2 Addresses.** For the foregoing purposes, each Party's address and telephone number shall be deemed to be the address and telephone number set forth under or opposite its signature hereto, unless and until such Party specifies another address or telephone number by not less than ten (10) days' prior notice to all other Parties.

## ARTICLE 30 EXECUTION

**30.1 Counterparts.** This Agreement may be executed in counterparts, and all such counterparts taken together shall be deemed to constitute one and the same instrument.

**30.2 Ratification.** This Agreement may be executed by the execution and delivery of a good and sufficient instrument of ratification, adopting and entering into this Agreement. Such ratification shall have the same effect as if the Party executing it had executed this Agreement or a counterpart hereof.

**30.3 Effect of Signature.** When this Agreement is executed by two Parties, execution by each shall be deemed consideration for execution by the other, and each Party theretofore or thereafter executing this Agreement shall thereupon become and remain bound hereby until the termination of this Agreement. However, if the Unit Agreement does not become effective within twelve (12) months from and after the date of this Agreement, then, at the expiration of said period, this Agreement shall terminate.

**ARTICLE 31  
SUCCESSORS AND ASSIGNS**

**31.1 Covenants.** This Agreement shall be binding upon and shall inure to the benefit of all Parties signing the same, their heirs, devisees, personal representatives, successors and assigns, and their successors in interest, whether or not it is signed by all the Parties listed below. The terms hereof shall constitute covenants running with the lands and the Committed Working Interests of the Parties.

**ARTICLE 32  
HEADINGS FOR CONVENIENCE**

**32.1 Headings.** The Table of Contents and the headings used in this Agreement are inserted for convenience only and shall be disregarded in construing this Agreement.

**ARTICLE 33  
RIGHT OF APPEAL**

**33.1 Not Waived.** Nothing contained in this Agreement shall be deemed to constitute a waiver by any Party of any right it would otherwise have to contest the validity of any law or any order or regulation of governmental authority (whether Federal, State, or local) relating to or affecting the conduct of operations within the Unit Area or to appeal from any such order.

**ARTICLE 34  
SUBSEQUENT JOINDER**

**34.1 Prior to the Commencement of Operations.** Prior to the commencement of operations under the Unit Agreement, all owners of working interests in the Unit Area who have joined the Unit Agreement shall be privileged to execute or ratify this Agreement.

**34.2 After Commencement of Operations.** After commencement of operations under the Unit Agreement, any working interest in land within the Unit Area which is not then committed hereto may be committed to this Agreement and to the Unit Agreement upon such reasonable terms and conditions as may receive the Approval of the Parties.

**ARTICLE 35  
CARRIED INTERESTS**

**35.1 Treatment of.** If any working interest shown on Exhibit B to the Unit Agreement and committed thereto is a carried working interest, such interest shall, if the carrying Party executes this Agreement, be deemed to be, for the purpose of this Agreement, a Committed Working Interest owned by the carrying Party.

**ARTICLE 36  
EFFECTIVE DATE AND TERM**

**36.1 Effective Date and Term.** This Agreement shall become effective upon the effective date of the Unit Agreement, shall continue in effect during the term of the Unit Agreement, and shall terminate concurrently therewith.

**36.2 Effect of Termination.** Termination of this Agreement shall not relieve any Party of its obligations then accrued hereunder. Notwithstanding termination of this Agreement, the provisions hereof relating to the charging and payment of Costs and the disposition of materials and equipment shall continue in force until all materials and equipment owned by the Parties have been disposed of and until final accounting between Unit Operator and the Parties has been made. Termination of this Agreement shall automatically terminate all rights and interests acquired by virtue of this Agreement in lands within the Unit Area, except such transfers of Committed Working Interests as have been evidenced by formal written instruments of transfer.

**ARTICLE 37**  
**OTHER PROVISIONS**

28.3 TAX ELECTION. (Continued) This election by the Parties to be excluded from the application of all of the provisions of Subchapter K does not apply in any way to any subsequent agreements between the Parties or with third parties concerning the sharing of costs for the drilling of any wells in the unit area. The Parties reserve the right to decide with each such subsequent agreement whether they elect to be excluded from the application of Subchapter K.

IN WITNESS WHEREOF, this Agreement has been executed by the Parties as of the day and year first above written.

As Unit Operator and Working Interest Owner

LEONARD MINERALS COMPANY

By \_\_\_\_\_  
Managing Partner

Address: 1400 Electric Service Bldg.  
115 West Seventh Street  
Fort Worth, Texas 76102

Date of Execution:  
\_\_\_\_\_

Telephone: (817) 335-4261

STATE OF Texas )  
 ) ss.  
COUNTY OF Tarrant )

The foregoing instrument was acknowledged before me by Obie P. Leonard, Jr., as Managing Partner of Leonard Minerals Company.

This      day of December, 1985.  
WITNESS my hand and official seal.

My Commission Expires:  
\_\_\_\_\_

\_\_\_\_\_  
Notary Public

EXHIBIT " 1 "

Attached to and made a part of the Unit Operating Agreement for the Taos Trough Unit,  
Colfax, Mora and Taos Counties, New Mexico

ACCOUNTING PROCEDURE  
JOINT OPERATIONS

I. GENERAL PROVISIONS

1. Definitions

"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.  
"Joint Account" shall mean the account showing the charges paid and credits received in the conduct of the Joint Operations and which are to be shared by the Parties.  
"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.  
"First Level Supervisors" shall mean those employees whose primary function in Joint Operations is the direct supervision of other employees and/or contract labor directly employed on the Joint Property in a field operating capacity.  
"Technical Employees" shall mean those employees having special and specific engineering, geological or other professional skills, and whose primary function in Joint Operations is the handling of specific operating conditions and problems for the benefit of the Joint Property.  
"Personal Expenses" shall mean travel and other reasonable reimbursable expenses of Operator's employees.  
"Material" shall mean personal property, equipment or supplies acquired or held for use on the Joint Property.  
"Controllable Material" shall mean Material which at the time is so classified in the Material Classification Manual as most recently recommended by the Council of Petroleum Accountants Societies.

2. Statement and Billings

Operator shall bill Non-Operators on or before the last day of each month for their proportionate share of the Joint Account for the preceding month. Such bills will be accompanied by statements which identify the authority for expenditure, lease or facility, and all charges and credits summarized by appropriate classifications of investment and expense except that items of Controllable Material and unusual charges and credits shall be separately identified and fully described in detail.

3. Advances and Payments by Non-Operators

- A. 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 within fifteen (15) days after receipt of the billing or by the first day of the month for which the advance is required, whichever is later. Operator shall adjust each monthly billing to reflect advances received from the Non-Operators.
- B. 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 prime rate in effect at Chase  
Manhattan Bank, N.A. on the first day of the month in which delinquency occurs plus 1% 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, plus attorney's fees, court costs, and other costs in connection with the collection of unpaid amounts.

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 Controllable Material as provided for in Section V.

## 5. Audits

- A. 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 Joint Account 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 a joint audit 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. The audits shall not be conducted more than once each year without prior approval of Operator, except upon the resignation or removal of the Operator, and shall be made at the expense of those Non-Operators approving such audit.
- B. The Operator shall reply in writing to an audit report within 180 days after receipt of such report.

## 6. Approval By Non-Operators

Where an approval or other agreement of the Parties or Non-Operators is expressly required under other sections of this Accounting Procedure and if the agreement to which this Accounting Procedure is attached contains no contrary provisions in regard thereto, Operator shall notify all Non-Operators of the Operator's proposal, 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. Ecological and Environmental

Costs incurred for the benefit of the Joint Property as a result of governmental or regulatory requirements to satisfy environmental considerations applicable to the Joint Operations. Such costs may include surveys of an ecological or archaeological nature and pollution control procedures as required by applicable laws and regulations.

### 2. Rentals and Royalties

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

### 3. Labor

- A. (1) Salaries and wages of Operator's field employees directly employed on the Joint Property in the conduct of Joint Operations.
- (2) Salaries of ~~First Level~~ Supervisors in the field below District Manager.
- (3) Salaries and wages of Technical Employees directly employed on the Joint Property if such charges are excluded from the overhead rates.
- (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 the overhead rates.
- B. Operator's cost of holiday, vacation, sickness and disability benefits and other customary allowances paid to employees whose salaries and wages are chargeable to the Joint Account under Paragraph 3A of this Section II. Such costs under this Paragraph 3B 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 3A of this Section II. 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 costs chargeable to the Joint Account under Paragraphs 3A and 3B of this Section II.
- D. Personal Expenses of those employees whose salaries and wages are chargeable to the Joint Account under Paragraph 3A of this Section II.

### 4. Employee Benefits

Operator's current costs 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 3A and 3B of this Section II shall be Operator's actual cost not to exceed the percent most recently recommended by the Council of Petroleum Accountants Societies.

### 5. Material

Material purchased or furnished by Operator for use on the Joint Property as provided under Section IV. Only such Material shall be purchased for or transferred to the Joint Property as may be required for immediate use and is reasonably practical and consistent with efficient and economical operations. The accumulation of surplus stocks shall be avoided.

### 6. 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 where like material is normally available or railway receiving point nearest the Joint Property unless agreed to by the Parties.

- 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 where like material is normally available, or railway receiving point nearest the Joint Property unless agreed to by the Parties. No charge shall be made to the Joint Account for moving Material to other properties belonging to Operator, unless agreed to by the Parties.
- C. In the application of subparagraphs A and B above, the option to equalize or charge actual trucking cost is available when the actual charge is \$400 or less excluding accessorial charges. The \$400 will be adjusted to the amount most recently recommended by the Council of Petroleum Accountants Societies.

## 7. Services

The cost of contract services, equipment and utilities provided by outside sources, except services excluded by Paragraph 10 of Section II and Paragraph i, ii, and iii, of Section III. The cost of professional consultant services and contract services of technical personnel directly engaged on the Joint Property if such charges are excluded from the overhead rates. The cost of professional consultant services or contract services of technical personnel not directly engaged on the Joint Property shall not be charged to the Joint Account unless previously agreed to by the Parties.

## 8. Equipment and Facilities Furnished By Operator

- A. Operator shall charge the Joint Account for use of Operator owned equipment and facilities at rates commensurate with costs of ownership and operation. Such rates shall include costs of maintenance, repairs, other operating expense, insurance, taxes, depreciation, and interest on gross investment less accumulated depreciation not to exceed twelve percent (12 %) per annum. Such rates shall not exceed average commercial rates currently prevailing in the immediate area of the Joint Property.
- B. In lieu of charges in paragraph 8A above, Operator may elect to use average commercial rates prevailing in the immediate area of the Joint Property less 20%. For automotive equipment, Operator may elect to use rates published by the Petroleum Motor Transport Association.

## 9. 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 those resulting from Operator's gross negligence or willful misconduct. Operator shall furnish Non-Operator written notice of damages or losses incurred as soon as practicable after a report thereof has been received by Operator.

## 10. Legal Expense

Expense of handling, investigating and settling litigation or claims, discharging of liens, payment of judgements and amounts paid for settlement of claims incurred in or resulting from operations under the agreement or necessary to protect or recover the Joint Property, except that no charge for services of Operator's legal staff or fees or expense of outside attorneys shall be made unless previously agreed to by the Parties. All other legal expense is considered to be covered by the overhead provisions of Section III unless otherwise agreed to by the Parties, except as provided in Section I, Paragraph 3.

## 11. 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. If the ad valorem taxes are 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 tax value generated by each party's working interest.

## 12. Insurance

Net premiums paid for insurance required to be carried for the Joint Operations 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 Worker'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 at Operator's cost not to exceed manual rates.

## 13. Abandonment and Reclamation

Costs incurred for abandonment of the Joint Property, including costs required by governmental or other regulatory authority.

## 14. Communications

Cost of acquiring, leasing, installing, operating, repairing and maintaining communication systems, including radio and microwave facilities directly serving the Joint Property. In the event communication facilities/systems serving the Joint Property are Operator owned, charges to the Joint Account shall be made as provided in Paragraph 8 of this Section II.

## 15. 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 of direct benefit to the Joint Property and is incurred by the Operator in the necessary and proper conduct of the Joint Operations.

### III. OVERHEAD

#### 1. Overhead - Drilling and Producing Operations

- i. As compensation for administrative, supervision, office services and warehousing costs, Operator shall charge drilling and producing operations on either:

(☒) Fixed Rate Basis, Paragraph 1A, or  
 ( ) Percentage Basis, Paragraph 1B

Unless otherwise agreed to by the Parties, such charge shall be in lieu of costs and expenses of all offices and salaries or wages plus applicable burdens and expenses of all personnel, except those directly chargeable under Paragraph 3A, Section II. 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 the Parties as a direct charge to the Joint Account.

- ii. The salaries, wages and Personal Expenses of Technical Employees and/or the cost of professional consultant services and contract services of technical personnel directly employed on the Joint Property:

( ) shall be covered by the overhead rates, or  
 (☒) shall not be covered by the overhead rates.

- iii. The salaries, wages and Personal Expenses of Technical Employees and/or costs of professional consultant services and contract services of technical personnel either temporarily or permanently assigned to and directly employed in the operation of the Joint Property:

(☒) shall be covered by the overhead rates, or  
 ( ) shall not be covered by the overhead rates.

#### A. Overhead - Fixed Rate Basis

- (1) Operator shall charge the Joint Account at the following rates per well per month:

Drilling Well Rate \$ 7,165.00  
 (Prorated for less than a full month)  
 Producing Well Rate \$ 548.00

- (2) Application of Overhead - Fixed Rate Basis shall be as follows:

##### (a) Drilling Well Rate

- (1) Charges for drilling wells shall begin on the date the well is spudded and terminate on the date the drilling rig, completion rig, or other units used in completion of the well is released, whichever is later, except that no charge shall be made during suspension of drilling or completion operations for fifteen (15) or more consecutive calendar days.
- (2) Charges for wells undergoing any type of workover or recompletion for a period of five (5) consecutive work days or more shall be made at the drilling well rate. Such charges shall be applied for the period from date workover operations, with rig or other units used in workover, commence through date of rig or other unit release, except that no charge shall be made during suspension of operations for fifteen (15) or more consecutive calendar days.

##### (b) Producing Well Rates

- (1) An active well either produced or injected into for any portion of the month shall be considered as a one-well charge for the entire month.
  - (2) Each active completion in a multi-completed well in which production is not commingled down hole shall be considered as a one-well charge providing each completion is considered a separate well by the governing regulatory authority.
  - (3) An inactive gas well shut in because of overproduction or failure of purchaser to take the production shall be considered as a one-well charge providing the gas well is directly connected to a permanent sales outlet.
  - (4) A one-well charge shall be made for the month in which plugging and abandonment operations are completed on any well. This one-well charge shall be made whether or not the well has produced except when drilling well rate applies.
  - (5) All other inactive wells (including but not limited to inactive wells covered by unit allowable, lease allowable, transferred allowable, etc.) shall not qualify for an overhead charge.
- (3) 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 calendar year preceding 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 Statistics Canada, as applicable. The adjusted rates shall be the rates currently in use, plus or minus the computed adjustment.

#### B. Overhead - Percentage Basis

- (1) Operator shall charge the Joint Account at the following rates:



## (a) Development

\_\_\_\_\_ Percent ( \_\_\_\_\_ %) of the cost of development of the Joint Property exclusive of costs provided under Paragraph 10 of Section II and all salvage credits.

## (b) Operating

\_\_\_\_\_ Percent ( \_\_\_\_\_ %) of the cost of operating the Joint Property exclusive of costs provided under Paragraphs 2 and 10 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.

## (2) Application of Overhead - Percentage Basis shall be as follows:

For the purpose of determining charges on a percentage basis under Paragraph 1B 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 rig and crew capable of drilling to the producing interval on the Joint Property; also, preliminary expenditures necessary in preparation for drilling and expenditures incurred in abandoning when the 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 2 of this Section III. All other costs shall be considered as operating.

**2. Overhead - Major Construction**

To compensate Operator for overhead costs incurred in the construction and installation of fixed assets, the expansion of fixed assets, and any other project clearly discernible as a fixed asset required for the development and operation of the Joint Property, Operator shall either negotiate a rate prior to the beginning of construction, or shall charge the Joint Account for overhead based on the following rates for any Major Construction project in excess of \$ 25,000.00 :

- A. 5 % of first \$100,000 or total cost if less, plus  
 B. 3 % of costs in excess of \$100,000 but less than \$1,000,000, plus  
 C. 2 % of costs in excess of \$1,000,000.

Total cost shall mean the 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 and workover wells and artificial lift equipment shall be excluded.

**3. Catastrophe Overhead**

To compensate Operator for overhead costs incurred in the event of expenditures resulting from a single occurrence due to oil spill, blowout, explosion, fire, storm, hurricane, or other catastrophes as agreed to by the Parties, which are necessary to restore the Joint Property to the equivalent condition that existed prior to the event causing the expenditures, Operator shall either negotiate a rate prior to charging the Joint Account or shall charge the Joint Account for overhead based on the following rates:

- A. 5 % of total costs through \$100,000; plus  
 B. 3 % of total costs in excess of \$100,000 but less than \$1,000,000; plus  
 C. 2 % of total costs in excess of \$1,000,000.

Expenditures subject to the overheads above will not be reduced by insurance recoveries, and no other overhead provisions of this Section III shall apply.

**4. Amendment of Rates**

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

**IV. PRICING OF JOINT ACCOUNT MATERIAL PURCHASES, TRANSFERS AND DISPOSITIONS**

Operator is responsible for Joint Account Material and shall make proper and timely charges and credits for all Material movements affecting the Joint Property. Operator shall provide all Material for use on the Joint Property; however, at Operator's option, such Material may be supplied by the Non-Operator. Operator shall make timely disposition of idle and/or surplus Material, such disposal being made either through sale to Operator or Non-Operator, division in kind, or sale to outsiders. Operator may purchase, but shall be under no obligation to purchase, interest of Non-Operators in surplus condition A or B Material. The disposal of surplus Controllable Material not purchased by the Operator shall be agreed to by the Parties.

**1. Purchases**

Material purchased shall be charged at the price paid by Operator after deduction of all discounts received. In case of Material found to be defective or returned to vendor for any other reasons, credit shall be passed to the Joint Account when adjustment has been received by the Operator.

**2. Transfers and Dispositions**

Material furnished to the Joint Property and Material transferred from the Joint Property or disposed of by the Operator, unless otherwise agreed to by the Parties, shall be priced on the following basis exclusive of cash discounts:

## A. New Material (Condition A)

### (1) Tubular Goods Other than Line Pipe

- (a) Tubular goods, sized 2½ inches OD and larger, except line pipe, shall be priced at Eastern mill published carload base prices effective as of date of movement plus transportation cost using the 80,000 pound carload weight basis to the railway receiving point nearest the Joint Property for which published rail rates for tubular goods exist. If the 80,000 pound rail rate is not offered, the 70,000 pound or 90,000 pound rail rate may be used. Freight charges for tubing will be calculated from Lorain, Ohio and casing from Youngstown, Ohio.
- (b) For grades which are special to one mill only, prices shall be computed at the mill base of that mill plus transportation cost from that mill to the railway receiving point nearest the Joint Property as provided above in Paragraph 2.A.(1)(a). For transportation cost from points other than Eastern mills, the 30,000 pound Oil Field Haulers Association interstate truck rate shall be used.
- (c) Special end finish tubular goods shall be priced at the lowest published out-of-stock price, f.o.b. Houston, Texas, plus transportation cost, using Oil Field Haulers Association interstate 30,000 pound truck rate, to the railway receiving point nearest the Joint Property.
- (d) Macaroni tubing (size less than 2½ inch OD) shall be priced at the lowest published out-of-stock prices f.o.b. the supplier plus transportation costs, using the Oil Field Haulers Association interstate truck rate per weight of tubing transferred, to the railway receiving point nearest the Joint Property.

### (2) Line Pipe

- (a) Line pipe movements (except size 24 inch OD and larger with walls ¾ inch and over) 30,000 pounds or more shall be priced under provisions of tubular goods pricing in Paragraph A.(1)(a) as provided above. Freight charges shall be calculated from Lorain, Ohio.
  - (b) Line pipe movements (except size 24 inch OD and larger with walls ¾ inch and over) less than 30,000 pounds shall be priced at Eastern mill published carload base prices effective as of date of shipment, plus 20 percent, plus transportation costs based on freight rates as set forth under provisions of tubular goods pricing in Paragraph A.(1)(a) as provided above. Freight charges shall be calculated from Lorain, Ohio.
  - (c) Line pipe 24 inch OD and over and ¾ inch wall and larger shall be priced f.o.b. the point of manufacture at current new published prices plus transportation cost to the railway receiving point nearest the Joint Property.
  - (d) Line pipe, including fabricated line pipe, drive pipe and conduit not listed on published price lists shall be priced at quoted prices plus freight to the railway receiving point nearest the Joint Property or at prices agreed to by the Parties.
- (3) Other Material shall be priced at the current new price, in effect at date of movement, as listed by a reliable supply store nearest the Joint Property, or point of manufacture, plus transportation costs, if applicable, to the railway receiving point nearest the Joint Property.
- (4) Unused new Material, except tubular goods, moved from the Joint Property shall be priced at the current new price, in effect on date of movement, as listed by a reliable supply store nearest the Joint Property, or point of manufacture, plus transportation costs, if applicable, to the railway receiving point nearest the Joint Property. Unused new tubulars will be priced as provided above in Paragraph 2 A (1) and (2).

## B. Good Used Material (Condition B)

Material in sound and serviceable condition and suitable for reuse without reconditioning:

### (1) Material moved to the Joint Property

At seventy-five percent (75%) of current new price, as determined by Paragraph A.

### (2) Material used on and moved from the Joint Property

- (a) At seventy-five percent (75%) of current new price, as determined by Paragraph A, if Material was originally charged to the Joint Account as new Material or
- (b) At sixty-five percent (65%) of current new price, as determined by Paragraph A, if Material was originally charged to the Joint Account as used Material.

### (3) Material not used on and moved from the Joint Property

At seventy-five percent (75%) of current new price as determined by Paragraph A.

The cost of reconditioning, if any, shall be absorbed by the transferring property.

## C. Other Used Material

### (1) Condition C

Material which is not in sound and serviceable condition and not suitable for its original function until after reconditioning shall be priced at fifty percent (50%) of current new price as determined by Paragraph A. The cost of reconditioning shall be charged to the receiving property, provided Condition C value plus cost of reconditioning does not exceed Condition B value.

## (2) Condition D

Material, excluding junk, no longer suitable for its original purpose, but usable for some other purpose shall be priced on a basis commensurate with its use. Operator may dispose of Condition D Material under procedures normally used by Operator without prior approval of Non-Operators.

- (a) Casing, tubing, or drill pipe used as line pipe shall be priced as Grade A and B seamless line pipe of comparable size and weight. Used casing, tubing or drill pipe utilized as line pipe shall be priced at used line pipe prices.
- (b) Casing, tubing or drill pipe used as higher pressure service lines than standard line pipe, e.g. power oil lines, shall be priced under normal pricing procedures for casing, tubing, or drill pipe. Upset tubular goods shall be priced on a non upset basis.

## (3) Condition E

Junk shall be priced at prevailing prices. Operator may dispose of Condition E Material under procedures normally utilized by Operator without prior approval of Non-Operators.

## D. Obsolete Material

Material which is serviceable and usable for its original function but condition and/or value of such Material is not equivalent to that which would justify a price as provided above may be specially priced as agreed to by the Parties. Such price should result in the Joint Account being charged with the value of the service rendered by such Material.

## E. Pricing Conditions

- (1) Loading or unloading costs may be charged to the Joint Account at the rate of twenty-five cents (25¢) per hundred weight on all tubular goods movements, in lieu of actual loading or unloading costs sustained at the stocking point. The above rate shall be adjusted as of the first day of April each year following January 1, 1985 by the same percentage increase or decrease used to adjust overhead rates in Section III, Paragraph 1.A(3). Each year, the rate calculated shall be rounded to the nearest cent and shall be the rate in effect until the first day of April next year. Such rate shall be published each year by the Council of Petroleum Accountants Societies.
- (2) 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 published or listed prices 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 providing such Material, in making it suitable for use, and in moving it to the Joint Property; provided 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 ten 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.

## V. 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

Adjustments to the Joint Account resulting from the reconciliation of a physical inventory shall be made within six months following the taking of the inventory. Inventory adjustments shall be made by Operator to the Joint Account for overages and shortages, but, Operator shall be held accountable only for shortages due to lack of reasonable diligence.

## 3. Special Inventories

Special inventories may be taken whenever there is any sale, change of interest, or change of Operator 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. In cases involving a change of Operator, all Parties shall be governed by such inventory.

## 4. Expense of Conducting Inventories

- A. The expense of conducting periodic inventories shall not be charged to the Joint Account unless agreed to by the Parties.
- B. The expense of conducting special inventories shall be charged to the Parties requesting such inventories, except inventories required due to change of Operator shall be charged to the Joint Account.

EXHIBIT "2"

Initial Test Well

Attached to and made a part of the Unit  
Operating Agreement for the Taos Trough  
Unit Area, Colfax, Mora and Taos Counties,  
New Mexico.

1. LOCATION: The initial test well shall be drilled at a location selected by Unit Operator and approved by the Authorized Officer of the Bureau of Land Management.
2. DEPTH: The initial test well shall be drilled conformably with the terms of Article 9 of the Taos Trough Unit Agreement.
3. COSTS: All costs and expenses incurred in connection with the initial test well, including drilling, testing and completing into the tanks, if an oil well, or through gas separator, if a gas producer, and plugging and abandoning, if a dry hole, shall be borne and paid for by Leonard Minerals Company and such other parties hereto as agreed to bear such costs in accordance with separate agreement among themselves and where applicable subject to the investment adjustment provisions of Article 13 of this Agreement. Any cash contributions received toward the drilling of the initial test well shall belong to the parties sustaining the risk of drilling the initial test well.
4. TITLE EXAMINATION AREA: The title examination area for the initial test well shall be an area surrounding the location of such well as may be designated by the Unit Operator.
5. COST OF TITLE EXAMINATION: The cost of title examination shall be charged as a cost of drilling the initial test well.
6. DEEPENING, PLUGGING BACK: In the absence of any agreement to the contrary, the attempted completion, deepening or plugging back, and abandonment of the Initial Test Well shall be governed by the provisions of Section 9.3 to this agreement.

EXHIBIT "3"

Insurance

Attached to and made a part of the Unit  
Operating Agreement for the Taos Trough  
Unit Area, Colfax, Mora and Taos Counties  
New Mexico.

As to all operations hereunder, the Operator shall carry for the benefit and protection of the parties hereto Workmen's Compensation insurance in accordance with laws of governmental bodies having jurisdiction, including United States Longshoremen's and Harbor Workers' Compensation Act and as extended to Outer Continental Shelf Operations, as applicable, and Employers' Liability insurance. Workmen's Compensation insurance shall be for statutory limits; Employers' Liability insurance shall provide coverage of \$100,000 each accident with respect to bodily injury and in the aggregate with respect to occupational diseases, except that coverage applicable to exposures under maritime jurisdiction shall be \$100,000 each employee and \$500,000 each accident with respect to bodily injury and in the aggregate with respect to occupational diseases. Operator may elect to be a self-insurer provided Operator complies with applicable laws and in such event Operator shall charge to the joint account in lieu of any premiums for such insurance, a premium equivalent limited to amounts determined by applying manual insurance rates to the payroll.

The Operator shall not be required to carry any other insurance for the joint account. The liability, if any, of the parties hereto in damages for claims growing out of personal injury to or death of third persons or injury or destruction of property of third parties resulting from the operations and development of the premises covered hereby shall be borne by the parties hereto in the proportions of their respective interests in the production therefrom; and each party individually may acquire such insurance as it deems proper to protect itself against such claims. Operator shall require all third party contractors performing work in or on the premises covered hereby to carry such insurance and in such amounts as Operator shall deem necessary.

EXHIBIT "4"

Attached to and made a part of Unit Operating Agreement for the Taos Trough Unit Area, Colfax, Mora and Taos Counties, New Mexico.

EXECUTIVE ORDER 11246 AND EXECUTIVE ORDER 1158  
PROVISIONS OF SECTION 202 OF EXECUTIVE ORDER 11246

(1) The contractor will not discriminate against any employee or applicant for employment because of race, color, religion, sex or national origin. The contractor will take affirmative action to ensure the applicants are employed and that employees are treated during employment, without regard to their race, color, religion, sex or national origin. Such action shall include but not be limited to the following: Employment, upgrading, demotion, or transfer; recruitment or recruitment advertising; layoff or termination; rates of pay or other forms of compensation; and selection for training, including apprenticeship. The contractor agrees to post in conspicuous places available to employees and applicants for employment, notices to be provided by the contracting officer setting forth the provisions of this non-discrimination clause.

(2) The contractor will, in all solicitations or advertisements for employees placed by or on behalf of the contractor, state that all qualified applicants will receive consideration for employment without regard to race, color, religion, sex or national origin.

(3) The contractor will send to each labor union or representative of workers with which he has a collective bargaining agreement or other contract or understanding, a notice, to be provided by the agency contracting officer, advertising the labor union or workers' representative of the contractors' commitments under Section 202 of Executive Order No. 11246 of September 24, 1965, and shall post copies of the notice in conspicuous places available to employees and applicants for employment.

(4) The contractor will comply with all provisions of Executive Order No. 11246 of September 24, 1965, and of the rules, regulations, and relevant orders of the Secretary of Labor.

(5) The contractor will furnish all information and reports required by Executive Order No. 11246 of September 24, 1965, and by the rules, regulations and orders of the Secretary of Labor, or pursuant thereto, and will permit access to his books, records, and accounts, by the contracting agency and the Secretary of Labor for purposes of investigation to ascertain compliance with such rules, regulations, and orders.

(6) In the event of the contractor's non-compliance with the non-discrimination clauses of this contract or with any of such rules, regulations, or orders, this contract may be cancelled, terminated or suspended in whole or in part and the contractor may be declared ineligible for further Government contracts in accordance with procedures authorized in Executive Order No. 11246 of September 24, 1965, and such other sanctions may be imposed and remedies invoked as provided in Executive Order No. 11246 of September 24, 1965, or by rule, regulation or order of the Secretary of Labor, or as otherwise provided by law.

(7) The contractor will include the provisions of Paragraphs (1) through (7) in every subcontract or purchase order unless exempted by rules, regulations or orders of the Secretary of Labor issued pursuant to Section 204 of Executive Order No. 11246 of September 24, 1965, so that such provision will be binding upon each subcontractor or vendor. The contractor will take such action with respect to any subcontract or purchase order as the contracting agency may direct as a means of enforcing such provisions including sanctions for non-compliance; provided, however, that in the event the contractor becomes involved in, or is threatened with, litigation with a subcontractor or vendor as a result of such direction by the contracting agency, the contractor may request the United States to enter into such litigation to protect the interests of the United States.

# OIL & GAS LEASE

THIS AGREEMENT made this \_\_\_\_\_ day of \_\_\_\_\_, 19\_\_\_\_, between \_\_\_\_\_

of \_\_\_\_\_  
(Post Office Address)

herein called lessor (whether one or more) and \_\_\_\_\_, lessee:

1. Lessor, in consideration of TEN AND OTHER DOLLARS in hand paid, receipt of which is here acknowledged, and of the royalties herein provided and of the agreements of the lessee herein contained, hereby grants, leases and lets exclusively unto lessee for the purpose of investigating, exploring, prospecting, drilling, and operating for and producing oil and gas, injecting gas, water, other fluids, and air into subsurface strata, laying pipe lines, storing oil, building tanks, roadways, telephone lines, and other structures and things thereon to produce, save, take care of, treat, process, store and transport said minerals, the

following described land in \_\_\_\_\_ County, New Mexico, to-wit:

## EXHIBIT "5"

Attached to and made a part of the Unit Operating Agreement for the Taos Trough Unit Area, Colfax, Mora and Taos Counties, New Mexico

For the purpose of calculating the rental payments hereinafter provided for, said land is estimated to comprise \_\_\_\_\_ acres, whether it actually comprises more or less.

2. Subject to the other provisions herein contained, this lease shall remain in force for a term of \_\_\_\_\_ years from this date (called "primary term"), and as long thereafter as oil or gas, is produced from said land or land with which said land is pooled.

3. The royalties to be paid by lessee are: (a) on oil, and on other liquid hydrocarbons saved at the well, \_\_\_\_\_ of that produced and saved from said land, same to be delivered at the wells or to the credit of lessor in the pipe line to which the wells may be connected; (b) on gas, including casinghead gas and all gaseous substances, produced from said land and sold or used off the premises or in the manufacture of gasoline or other product therefrom, the market value at the mouth of the well of \_\_\_\_\_ of the gas so sold or used, provided that on gas sold at the wells the royalty shall be \_\_\_\_\_ of the amount realized from such sale; (c) and at any time when this lease is not validated by other provisions hereof and there is a gas and/or condensate well on said land, or land pooled therewith, but gas and/or condensate is not being so sold or used and such well is shut in, either before or after production therefrom, then on or before 90 days after said well is shut in, and thereafter at annual intervals, lessee may pay or tender an advance annual shut-in royalty equal to the amount of delay rentals provided for in this lease for the acreage then held under this lease by the party making such payment or tender, and so long as said shut-in royalty is paid or tendered this lease shall not terminate and it will be considered under all clauses hereof that gas is being produced from the leased premises in paying quantities. Each such payment shall be paid or tendered to the party or parties who at the time of such payment would be entitled to receive the royalties which would be paid under this lease if the well were in fact producing, or be paid or tendered to the credit of such party or parties in the depository bank and in the manner hereinafter provided for the payment of rentals.

4. If operations for drilling are not commenced on said land or on land pooled therewith on or before one (1) year from this date, this lease shall terminate

as to both parties, unless on or before one (1) year from this date lessee shall pay or tender to the lessor a rental of \$ \_\_\_\_\_ which shall cover the privilege of deferring commencement of such operations for a period of twelve (12) months. In like manner and upon like payments or tenders, annually, the commencement of said operations may be further deferred for successive periods of twelve (12) months each during the primary term. Payment

or tender may be made to the lessor or to the credit of the lessor in the \_\_\_\_\_ Bank

at \_\_\_\_\_, which bank, or any successor thereof, shall continue to be the agent for the lessor and lessor's heirs and assigns. If such bank (or any successor bank) shall fail, liquidate, or be succeeded by another bank, or for any reason shall fail or refuse to accept rental, lessee shall not be held in default until thirty (30) days after lessor shall deliver to lessee a recordable instrument making provision for another acceptable method of payment or tender, and any depository charge is a liability of the lessor. The payment or tender of rental may be made by check or draft of lessee, mailed or delivered to said bank or lessor, or any lessor if more than one, on or before the rental paying date. Any timely payment or tender of rental or shut-in royalty which is made in a bona fide attempt to make proper payment, but which is erroneous in whole or in part as to parties, amounts, or depositories shall nevertheless be sufficient to prevent termination of this lease in the same manner as though a proper payment had been made; provided, however, lessee shall correct such error within thirty (30) days after lessee has received written notice thereof by certified mail from lessor together with such instruments as are necessary to enable lessee to make proper payment.

5. Lessee is hereby granted the right and power, from time to time, to pool or combine this lease, the land covered by it or any part or horizon thereof with any other land, lease, leases, mineral estates or parts thereof for the production of oil or gas. Units pooled hereunder shall not exceed the standard pro-rata unit fixed by law or by the New Mexico Oil Conservation Commission or by other lawful authority for the pool or area in which said land is situated, plus a tolerance of 10%. Lessee shall file written unit designations in the county in which the premises are located and such units may be designated from time to time and either before or after the completion of wells. Drilling operations on or production from any part of any such unit shall be considered for all purposes, except the payment of royalty, as operations conducted upon or production from the land described in this lease. There shall be allocated to the land covered by this lease included in any such unit that portion of the total production of pooled minerals from wells in the unit, after deducting any used in lease or unit operations, which the number of surface acres in the land covered by this lease included in the unit bears to the total number of surface acres in the unit. The production so allocated shall be considered for all purposes, including the payment or delivery of royalty, to be the entire production of pooled minerals from the portion of said land covered hereby and included in said unit in the same manner as though produced from said land under the terms of this lease. Any pooled unit designated by lessee, as provided herein, may be dissolved by lessee by recording an appropriate instrument in the County where the land is situated at any time after the completion of a dry hole or the cessation of production on said unit. Lessee is further granted the right and power to commit this lease as to all or any portion of the above described lands or horizons thereof to any unit agreement for the purpose of conserving the natural resources of any oil or gas pool, field or area covered thereby; provided, such unit agreement contains usual and customary provisions for the allocation of oil and gas produced from the unit area and such unit agreement embraces lands of either the United States or State of New Mexico or both, and the form of unit agreement has been approved by either the United States Geological Survey or Commissioner of Public Lands or both and the New Mexico Oil Conservation Commission, and upon such commitment the provisions of this lease shall be conformable to the unit agreement.

6. If prior to the discovery of oil or gas hereunder, lessee should drill and abandon a dry hole or holes hereunder, or if after discovery of oil or gas the production thereof should cease for any cause, this lease shall not terminate if lessee commences reworking or additional drilling operations within 60 days thereafter and diligently prosecutes the same, or (if it be within the primary term) commences or resumes the payment or tender of rentals or commences operations for drilling or reworking on or before the rental paying date next ensuing after the expiration of three months from date of abandonment of said dry hole or holes or the cessation of production. If at the expiration of the primary term oil or gas is not being produced but lessee is then engaged in operations for drilling or reworking of any well, this lease shall remain in force so long as such operations are diligently prosecuted with no cessation of more than 60 consecutive days. If during the drilling or reworking of any well under this paragraph, lessee loses or junks the hole or well and after diligent efforts in good faith is unable to complete said operations then within 30 days after the abandonment of said operations lessee may commence another well and drill the same with due diligence. If any drilling, additional drilling, or reworking operations hereunder result in production, then this lease shall remain in full force so long thereafter as oil or gas is produced hereunder.

7. Lessee shall have free use of oil, gas and water from said land, except water from lessor's wells and tanks, for all operations hereunder, and the royalty shall be computed after deducting any so used. Lessee shall have the right at any time during or after the expiration of this lease to remove all property and fixtures placed by lessee on said land, including the right to draw and remove all casing. When required by lessor, lessee will bury all pipe lines on cultivated lands below ordinary plow depth, and no well shall be drilled within two hundred feet (200 ft.) of any residence or barn now on said land without lessor's consent. Lessor shall have the privilege, at his risk and expense, of using gas from any gas well on said land for stoves and inside lights in the principal dwelling thereon, out of any surplus gas not needed for operations hereunder.

8. The rights of either party hereunder may be assigned in whole or in part and the provisions hereof shall extend to the heirs, executors, administrators, successors and assigns; but no change or division in the ownership of the land, or in the ownership of or right to receive rentals, royalties or payments, however accomplished shall operate to enlarge the obligations or diminish the rights of lessee; and no such change or division shall be binding upon lessee for any purpose until 30 days after lessee has been furnished by certified mail at lessee's principal place of business with acceptable instruments or certified copies thereof constituting the chain of title from the original lessor. If any such change in ownership occurs through the death of the owner, lessee may pay or tender any rentals, royalties or payments to the credit of the deceased or his estate in the depository bank until such time as lessee has been furnished with evidence satisfactory to lessee as to the persons entitled to such sums. In the event of an assignment of this lease as to a segregated portion of said land, the rentals payable hereunder shall be apportioned as between the several leasehold owners ratably according to the surface area of each, and default in rental payment by one shall not affect the rights of other leasehold owners hereunder. An assignment of this lease, in whole or in part, shall, to the extent of such assignment, relieve and discharge lessee of any obligations hereunder, and, if lessee or assignee of part or parts hereof shall fail or make default in the payment of the proportionate part of the rentals due from such lessee or assignee or fail to comply with any other provision of the lease, such default shall not affect this lease in so far as it covers a part of said lands upon which lessee or any assignee thereof shall so comply or make such payments. Rentals as used in this paragraph shall also include shut-in royalty.

9. Should lessee be prevented from complying with any express or implied covenant of this lease, or from conducting drilling or reworking operations hereunder, or from producing oil or gas hereunder by reason of scarcity or inability to obtain or use equipment or material, or by operation of force majeure, or by any Federal or state law or any order, rule or regulation of governmental authority, then while so prevented, lessee's duty shall be suspended, and lessee shall not be liable for failure to comply therewith; and this lease shall be extended while and so long as lessee is prevented by any such cause from conducting drilling or reworking operations on or from producing oil or gas hereunder; and the time while lessee is so prevented shall not be counted against lessee, anything in this lease to the contrary notwithstanding.

10. Lessor hereby warrants and agrees to defend the title to said land, and agrees that lessee, at its option, may discharge any tax, mortgage, or other lien upon said land, and in the event lessee does so, it shall be subrogated to such lien with the right to enforce same and apply rentals and royalties accruing hereunder toward satisfying same. Without impairment of lessee's rights under the warranty, if this lease covers a less interest in the oil or gas in all or any part of said land than the entire and undivided fee simple estate (whether lessor's interest is herein specified or not) then the royalties, shut-in royalty, rental, and other payments, if any, accruing from any part as to which this lease covers less than such full interest, shall be paid only in the proportion which the interest therein, if any, covered by this lease, bears to the whole and undivided fee simple estate therein. Should any one or more of the parties named above as lessors fail to execute this lease, it shall nevertheless be binding upon the party or parties executing the same.

11. Lessee, its/heirs successors, heirs and assigns, shall have the right at any time to surrender this lease, in whole or in part, to lessor or his heirs, successors, and assigns by delivering or mailing a release thereof to the lessor, or by placing a release thereof of record in the county in which said land is situated; thereupon lessee shall be relieved from all obligations, expressed or implied, of this agreement as to acreage so surrendered, and thereafter the rentals and shut-in royalty payable hereunder shall be reduced in the proportion that the acreage covered hereby is reduced by said release or releases.

Executed the day and year first above written.

STATE OF NEW MEXICO,

County of

INDIVIDUAL ACKNOWLEDGMENT (New Mexico Short Form)

The foregoing instrument was acknowledged before me this day of, 19 by

My Commission expires, 19Notary Public

STATE OF NEW MEXICO,

County of

INDIVIDUAL ACKNOWLEDGMENT (New Mexico Short Form)

The foregoing instrument was acknowledged before me this day of, 19 by

My Commission expires, 19Notary Public

STATE OF NEW MEXICO,

County of

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My Commission expires, 19Notary Public

STATE OF

County of

INDIVIDUAL ACKNOWLEDGMENT (New Mexico Short Form)

The foregoing instrument was acknowledged before me this day of, 19 by

My Commission expires, 19Notary Public

No.

OIL AND GAS LEASE  
NEW MEXICO

FROM

TO

Date, 19

Section, Township, Range

No. of Acres

County, New Mexico

Term

STATE OF NEW MEXICO  
COUNTY OF

I hereby certify that this instrument was filed for record on the day of, A. D., 19, at o'clock m, and was duly recorded in Book at Page of the Records of said County.

County Clerk.

By Deputy.

STATE OF NEW MEXICO

County of

CORPORATION ACKNOWLEDGMENT (New Mexico Short Form)

The foregoing instrument was acknowledged before me this day of, 19 by President of corporation on behalf of said corporation.

My Commission Expires:Notary Public

STATE OF

County of

CORPORATION ACKNOWLEDGMENT (New Mexico Short Form)

The foregoing instrument was acknowledged before me this day of, 19 by President of corporation on behalf of said corporation.

My Commission Expires:Notary Public