

MERRION OIL & GAS CORPORATION

P. O. Box 840
FARMINGTON NEW MEXICO 87499

April 8, 1986

El Paso Natural Gas Company
Post Office Box 1492
El Paso, Texas 79978

Attn: Mr. Richard Jordan

Re: Casinghead Gas Contracts

Dear Mr. Jordan,

Enclosed please find two executed copies of the Casinghead Gas contract covering the Canada Mesa #3E well, Gallup side. As per our telephone conversation, we would like for you to consider similar contracts covering the following wells:

- 1) Rocky Mountain #1, located in the SW/4, Section 24, T24N, R2W, Rio Arriba County, New Mexico, which is producing from the Undesignated Gallup formation at an approximate rate of 50 MCF/day.
- 2) Oso Canyon Gas Com C #1, in the NW/4, Section 13, T24N, R2W, Rio Arriba County, New Mexico, producing from the Gavilan Mancos at 25 MCF/day approximately.
- 3) Krystina Com #1, located in the SW/4, Section 14, T24N, R2W, Rio Arriba County, New Mexico, also producing from the Gavilan Mancos at a rate of about 90 MCF/day.

We appreciate your consideration and early response on these contracts.

Yours very truly,

MERRION OIL & GAS CORPORATION


Gregory Merrion
President

JGM/clm

Enclosures

ILLEGIBLE

COPY

TOMMY ROBERTS

ATTORNEY-AT-LAW

(505) 326-3359

P. O. BOX 129
FARMINGTON, NEW MEXICO 87499OFFICE
3005 NORTHBRIDGE DR. • SUITE GCERTIFIED MAIL P 638 547 488
RETURN RECEIPT REQUESTED

July 28, 1986

El Paso Natural Gas Company
P. O. Box 1492
El Paso, Texas 79978

Re: Request for Casinghead Gas Contract

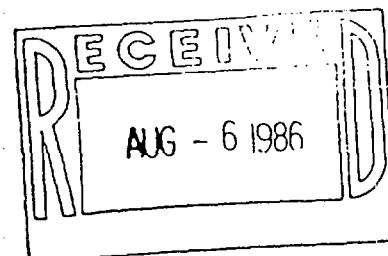
- 1) Rocky Mountain No. 1 Well
- 2) Oso Canyon Gas Com C No. 1 Well
- 3) Krystina Com No. 1 Well

Gentlemen:

By letter dated April 8, 1986, addressed to the attention of Mr. Richard Jordan, J. Gregory Merrion, President of Merrion Oil & Gas Corporation, notified you of the execution and return of two (2) copies of a Casinghead Gas Contract covering the Merrion Oil & Gas Corporation Canada Mesa No. 3E (Gallup) Well and requested that you provide similar contract coverage for casinghead gas produced from the above referenced wells. Subsequently, Mr. Jordan verbally notified Mr. Merrion that El Paso Natural Gas Company would not issue contracts covering production from the above referenced wells. No explanation was given for the refusal of El Paso Natural Gas Company to issue contracts.

The purpose of this letter is to once again request that El Paso Natural Gas Company provide contract coverage for casinghead gas produced from these wells. Merrion Oil & Gas Corporation proposes to pay all costs associated with laying a gathering line to a meter which would be provided and set at your expense. In addition, Merrion Oil & Gas Corporation is willing to sell casinghead gas from these wells pursuant to the terms of your spot market release program and under a month-to-month contract similar in nature to the short term gas purchase agreement currently offered by El Paso Natural Gas Company for spot market sales.

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El Paso Natural Gas Company

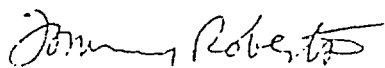
July 28, 1986

Page Two

In making this request for contract coverage, Merrion Oil & Gas Corporation notes that the above referenced wells are located in or near the Gavilan Mancos Oil Pool. It has also been noted that El Paso Natural Gas Company is an affiliate of Burlington Northern, the successor to the interests of Southland Royalty Corporation in the area of the Gavilan Mancos Oil Pool, and Merrion Oil & Gas Corporation assumes those interests include the benefits of gas purchase agreements applicable to production from existing wells in that area. With the benefit of gas purchase agreements, your affiliate company is in a position to sell the casinghead gas production from its wells; but, more importantly, it is able to continue to produce and sell oil. Without the benefit of gas purchase agreements, Merrion Oil & Gas Corporation must shut in its wells, thereby losing the ability to produce and sell oil which is capable of being produced from the wells. Under these circumstances, your affiliate company is given a significant competitive advantage in conducting its operations in the area of the Gavilan Mancos Oil Pool.

Merrion Oil & Gas Corporation looks forward to receiving an early response to this request for gas purchase contract coverage for the above referenced wells.

Sincerely,



TOMMY ROBERTS, Attorney for
Merrion Oil & Gas Corporation

TR:nk

xc: Merrion Oil & Gas Corporation ✓

SEP 23 1986

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Exhibit #, page 4

COPY

El Paso
Natural Gas Company

P. O. BOX 1492
EL PASO, TEXAS 79978
PHONE 915-541-2600

September 16, 1986

Mr. Tommy Roberts
3005 Northridge Drive, Suite G
Farmington, New Mexico 87499

Re: J. Gregory Merrion
Request for Gas Purchase Agreement

Dear Mr. Roberts:

We have received your letter dated July 28, 1986 regarding a contract for three undedicated wells owned by your client, J. Gregory Merrion. At the present, we are unable to comply with your request. In order to clear-up some apparent misunderstandings, we would offer the following information:

1. El Paso's released gas spot market program is offered to those of our producer-suppliers who have gas wells under contract to El Paso which are shut-in as a method of providing to them an outlet for such gas and the attendant cash flow. Only existing facilities are utilized, and El Paso receives a credit to its contractual minimum purchase obligation (if any) for all gas sold thereby. Mr. Merrion's wells, which are the subject of the referenced request, are not under any form of contract dedication to El Paso. Consequently, they do not meet the qualifications for this particular program.
2. You are correct in your statement that El Paso purchases casinghead gas production from the Gallup formation in this general area, including purchases from a corporate affiliate. However, we note that such affiliated purchases in this pool consist of a minority interest in only one well which is located some three miles distant from the nearest of your client's three new wells. We also note that Northwest Pipeline Corporation is a purchaser of gas production in this same area. In fact, they would appear to be the primary purchaser in the area of Mr. Merrion's three wells. We certainly do not concur that any El Paso affiliate is afforded an advantage over your client in selling Gavilan Mancos oil and gas production.

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As we have advised your client previously, at least three options exist for the disposal of gas production from these wells:

1. Sale to Northwest Pipeline Company

As you are aware, we have a jurisdictional gathering and exchange agreement with Northwest which stems from the 1974 divestiture. Thereunder, we would be happy to gather and redeliver the gas in the event Northwest tenders a contract. We are presently seeking FERC approval to extend that jurisdictional agreement to non-tradition (i.e., spot market) purchases.

2. Sale to El Paso Gas Marketing Company

Separate and apart from gas attributable to El Paso Natural Gas Company's released gas spot market program, El Paso Gas Marketing Company (EPGM) functions in a broker/middleman role as a purchaser and marketer of otherwise undedicated supplies. Their purchase of this gas would likely require that it be delivered to EPGM to the tailgate of a processing plant (such as Blanco) at the seller's sole cost and expense (i.e., any new facilities required plus appropriate tariff rates for the services provided). If you wish to pursue this avenue, we suggest that you contact Mr. Harold W. Adams of EPGM at (915) 541-5304.

3. Sale to Other Purchasers

El Paso remains ready and willing to transport this gas under the terms and provisions of its Order No. 436 tariff for "open access" transportation. Any such arrangements would, of course, be subject to the FERC regulations governing such activities. Based upon our discussions with your client, he appears to have significant direct marketing efforts underway at this time which would fall under this same sort of arrangement.

You may rest assured that it is not El Paso Natural Gas Company's intent to inhibit or forestall in any way your client's efforts to sell oil and gas production from these three new wells. On

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Mr. Tommy Roberts
Farmington, New Mexico 87499

Exhibit A, page 6

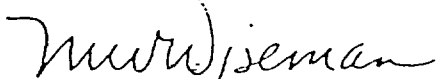
September 16, 1986

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the other hand, we remain unable to extend a purchase contract to him in light of our continuing oversupply situation. We will extend any reasonable assistance we can--whether or not it may fall under one of the three categories described above--in order to facilitate Mr. Merrion's marketing of his gas.

Very truly yours,

GAS PURCHASES DEPARTMENT



Michael W. Wiseman
Manager, Gas Contracts

MWW:ac

c: Mr. H. W. Adams

MERRION OIL & GAS CORPORATION

610 REILLY AVE. • P O BOX 840
FARMINGTON NEW MEXICO 87499

September 29, 1986

El Paso Natural Gas Company
Post Office Box 1492
El Paso, Texas 79978

Attn: Mr. Michael W. Wiseman
Manager, Gas Contracts

Re: Cavilan Field Casinghead Gas
Sales

Dear Mr. Wiseman,

We are delighted to learn, as stated in your letter of September 16th to our attorney Mr. Tommy Roberts, that El Paso has no intention to inhibit or forestall in any way our efforts for gas production from our Gavilan Field wells. We further are delighted to know that the reason you are unable to buy our gas is mainly a case of an oversupply situation.

We have talked with your Mr. Adams regarding sale to El Paso Gas Marketing Company, and he offered us very little hope for marketing this small quantity of gas (approximately 150 mcf/day). The other alternatives you mention are similarly not immediately possible.

In view of the foregoing, I would like to make a proposal which would eliminate all of the objections you might have to taking our gas.

We will lay lines to your low-pressure gathering system in the area, and sell you gas at your market-out price on a contract cancellable by us on 30 days' notice. In order to relieve your oversupply situation, we will cancel your contractual take-or-pay obligations in an amount of gas equal in heating value to the gas you take from our Gavilan Field wells. In choosing which contracts the canceled take-or-pay obligations will come from, we will attempt to cancel those requirements which will, on the average, be as nearly as possible equal in value to the gas you have taken from these wells. A calculation of this cancelled obligation will take place annually on or about the first day of April of each year for the prior calendar year.

Please advise even so that we may commence selling gas.

Yours very truly,

MERRION OIL & GAS CORPORATION

J. Gregory Merrion
J. Gregory Merrion
President

JGM/clm

Nov. 4 / 1986
response to Merrion

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November 4, 1986

Merrion Oil & Gas Corporation
610 Reilly Ave.
Farmington, New Mexico 87499

Attention: Mr. J. Gregory Merrion

Re: Gavilan Field Casinghead Gas Sales

Gentlemen:

We have received your letter dated September 29, 1986 sent in response to my earlier letter regarding the above-referenced gas. While your proposed solution is most creative, it does not appear workable from our viewpoint.

You suggest that we would receive relief from our take-or-pay obligations covering an equivalent volume of gas produced from your other Gavilan Field wells. However, as you may know, El Paso's production scheduling methodology does not consider the take-or-pay obligation for a specific well in determining whether or not that well is to be produced but rather considers only the weighted average cost of gas in the well's pool as part of our least-cost loading. Clearly, the addition of more deliverability to our system--especially casinghead gas with its non-swing characteristics--would serve to aggravate our current position.

As stated earlier, El Paso Natural Gas Company remains ready to assist, in any way it can, (short of offering a contract for your gas) to add you in the marketing of this non-swing production.

Very truly yours,

GAS PURCHASES DEPARTMENT

Michael W. Wiseman
Manager, Gas Contracts

MWW:ac

c: Mr. H. W. Adams