

Northeast Blanco Area  
Townships 30 and 31 North  
Ranges 6, 7 and 8 West  
San Juan and Rio Arriba  
Counties, New Mexico

### GEOLOGICAL MEMORANDUM

Stanolind geophysical (magnetometer) work in western Rio Arriba and eastern San Juan Counties, New Mexico has delineated a large anomalous area in Townships 30 and 31 North, Ranges 6, 7 and 8 West. This area, which is approximately six miles wide and twelve miles long, is located in the northern part of the San Juan Basin Province about twelve miles northeast of the town of Blanco.

As shown on the attached plat, approximately 75 per cent of the land in the anomalous area is Federal, hence, we believe it would be in the public interest to join all lands located thereon in a Unit Agreement. By so doing, any accumulation of oil or gas which might be discovered underlying the area could be more properly developed and produced in the interest of conservation. The proposed Unit Agreement outline is shown on the attached plat in red and is based on the magnetometer information attached hereto.

In order to properly test the oil and gas possibilities of the subject area, we believe the Unit Agreement should provide for the drilling of a test well to a depth sufficient to test all potentially productive horizons down to and including the Dakota (basal Cretaceous) Sandstone. The following tabulation of expected formations and the thickness of each is based on data from the Stanolind #1 Rosa Unit Well located in Section 11, Township 31 North, Range 6 West, four miles east of the subject area.

<u>PERIOD</u>	<u>FORMATION</u>	<u>THICKNESS</u>
Tertiary	Wasatch	0' - 850'
	Animas	850' - 2400'
Cretaceous	Ojo Alamo	2400' - 2500'
	Kirkland-Fruitland	2500' - 3175'
	Pictured Cliffs	3175' - 3450'
	Lewis Shale	3450' - 5300'
	Cliff House	5300' - 5450'
	Menefee	5450' - 5650'
	Point Lookout	5650' - 5800'
	Mancos	5800' - 7700'
	Greenhorn Limestone	7700' - 7750'
	Graneros	7750' - 7850'
Dakota Sand	7850' - 8100'	

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In addition to testing the Dakota Sandstone, such a well would also determine the possibilities for production from the Pictured Cliffs Sand and from the Cliff House and Point Lookout formations of the Mesa Verde Group, all of which are known to carry oil or gas in the San Juan Basin.

According to our magnetic information the most favorable location for the above test well is the southwest quarter of Section 23, Township 31 North, Range 7 West, and this location is recommended subject to possible slight changes in order to locate on more favorable terrain.

It is requested that the Geophysical map attached hereto be kept in confidence.

s/ Russell Farmer  
Russell Farmer  
Division Geologist  
Stanolind Oil and Gas Company  
Fort Worth, Texas

UNIT OPERATING AGREEMENT UNDER  
UNIT AGREEMENT FOR THE DEVELOPMENT AND OPERATION  
OF THE NORTHEAST BLANCO UNIT AREA, COUNTY OF SAN JUAN  
STATE OF NEW MEXICO

THIS AGREEMENT, made and entered into, as of the \_\_\_\_\_ day of \_\_\_\_\_, 19\_\_\_\_, by and between BLACKWOOD & NICHOLS COMPANY, a partnership composed of F. G. Blackwood, Dola Blackwood, W. J. Hilseweck, Helen Hilseweck, John W. Nichols, Mary D. Nichols and John W. Fisher, hereinafter designated as "Unit Operator" and the undersigned as owners of working interests in the unitized substances within the Unit Area subject to the Unit Agreement herein below described, as may subscribe this agreement and become parties hereto, which owners are hereinafter sometimes referred to individually as "Working Interest Owner" and collectively as "Working Interest Owners";

WITNESSETH: THAT,

WHEREAS, the parties hereto have executed, as of the date hereof, a certain Unit Agreement for the Development and Operation of the Northeast Blanco Unit Area, County of San Juan, State of New Mexico, hereinafter sometimes referred to as "Unit Agreement"; and

WHEREAS, the term "working interest owner" as used herein relating to the subject lands shall mean and refer only to such an interest committed hereto as may be obligated to bear or share, either in cash or out of production a portion or all of the costs or expenses of developing, equipping or operating any land within the Unit Area subject to this agreement. If the working interest in any tract is or shall hereafter be owned by more than one party, the term "working interest owner," when used with respect to such tract, shall refer to all such parties owning the working interest therein; and

WHEREAS, Section 7 of the Unit Agreement provides for a separate Unit Operating Agreement to be executed by the parties hereto, wherein and whereby such parties shall agree among themselves with respect to certain matters and things relating to the development and operation of the said area.

NOW, THEREFORE, in consideration of the premises and the covenants and agreements herein contained, it is mutually agreed by and between the parties as follows:

1. UNIT PLAN CONFIRMED: The Unit Agreement for the Development and Operation of the Northeast Blanco Unit Area and all exhibits attached thereto are hereby confirmed and made a part of this agreement and, in the event of any conflict between the provisions of the Unit Agreement and the provisions of this agreement, the provisions of the Unit Agreement shall prevail.

2. UNIT OPERATOR: Blackwood & Nichols Company, the party hereto named as Unit Operator of the Unit Area under the provisions of the Unit Agreement, or its duly appointed successor Unit Operator, shall have the exclusive right to develop and operate the Unit Area subject to the provisions of this agreement and of the Unit Agreement. The Unit Operator shall not sustain any liability to the Working Interest Owners for any acts done or omitted, in good faith performance of any of the provisions of this agreement, and in the exercise of its judgment and discretion.

The number of employees used by Unit Operator in conducting unit operations, the selection of such employees, the hours of labor and the compensation for services to be paid any and all such employees shall be determined by Unit Operator. Such employees shall be the employees of Unit Operator.

3. TITLES: Each Working Interest Owner hereto represents that it is now the owner of an interest in one or more of the tracts of land in the Unit Area. Within ten (10) days after the effective date of this agreement, each Working Interest Owner at his own expense shall furnish the Unit Operator with up-to-date abstracts of title covering and affecting its interest together with such original and supplemental title opinions as may be available, and in addition for lands of the United States, acceptable up-to-date reports as to the status of the lands as appears from the records of the Bureau of Land Management of the Department of Interior. The Unit Operator shall thereupon examine all title opinions, abstracts and status reports. All expenses incurred in connection with such examination of titles shall be borne by each Working Interest Owner proportionate to its respective interest in the Unit Area. Each Working Interest Owner shall severally pay the cost of curative work on its own titles. The Unit Operator shall pass upon all titles and shall determine the curative work required in connection with each title. All tracts of land or parts thereof, unless and until eliminated from the Unit Agreement under Section 28 thereof, shall form and comprise the Unit Area hereunder. Any tract of land or interest therein eliminated from the Unit Agreement shall, as of the date of its elimination therefrom, be eliminated herefrom without prejudice to any obligations theretofore accrued hereunder in respect of such tract or interest.

Notwithstanding the foregoing, each party hereto shall sustain the entire loss occasioned by any defect in or failure of its titles, and Unit Operator in his capacity of Unit Operator is hereby relieved from any and all liability in connection therewith; and upon any loss of title to any land or interest therein committed to this agreement and the Unit Agreement there shall be an appropriate adjustment of the percentages of participation of the parties hereto.

If the true owner of such title fails or refuses to commit its interest to the said agreements, the interest so affected shall be eliminated from this agreement and the Unit Agreement, and as required by the Unit Agreement, no portion of Unit production nor Unit expense shall be allocated to such interest per force of said agreements nor shall any production attributable by law to such interest be deemed Unit production.

The Unit Operator in its capacity of Unit Operator shall sustain no liability to any part hereto for and on account of loss occasioned by reason of any erroneous payment caused by failure or defect of title, but such loss shall be the loss of all the parties hereto owning working interests in the affected participating area proportionate to their actual interests in such area, without prejudice to pursue any rights in law or in equity against the party whose title failed or against any person paid in error for recovery of such loss. Any future recovery of any sums so erroneously paid shall be paid or credited to the parties to whom such payments were charged in like proportion.

4. DUTIES OF UNIT OPERATOR: Unit Operator shall in the conduct of operations hereunder:

(a) conduct the same in a good and workmanlike manner, and have the right and duty to conduct such operations in accordance with its best judgment of what a prudent Operator would do under the same or similar circumstances;

(b) consult freely with Working Interest Owners concerning unit operations, and keep Working Interest Owners advised of all matters arising during the operation of the Unit Area which Unit Operator, in the exercise of its best judgment, considers important;

(c) keep true and correct books, accounts and records of its operations hereunder, and permit at all reasonable times the inspection, examination and auditing of same by any party hereto;

(d) permit any party hereto to have access to the lands and premises hereunder for inspection at all reasonable times;

(e) upon written request, furnish each Working Interest Owner with copies of all run tickets, and likewise upon request furnish each party hereto, on or before the 20th day of each calendar month, with a statement of the production, and the kinds thereof taken from the premises during the preceding calendar month; provided, that settlement for production, unless made by the purchaser direct, shall be made by Unit Operator by the 25th day of the month following the month in which production is sold, except gas, for which payment shall be made by the 25th day of the second month following the month of sale.

(f) on request furnish any Working Interest Owner a copy of the log of any

well and other engineering data pertaining to unit operations and samples from the cores and cuttings encountered in drilling wells, provided that such Working Interest Owner gives Unit Operator written notice of its desire to have such samples prior to the commencement of the well;

(g) comply with all valid applicable Federal and State laws and regulations; and

(h) keep the land in the unit area free from liens and encumbrances occasioned by its operations, save only the lien granted the Unit Operator under this agreement.

5. ADVISORY COMMITTEE CREATED: An "Advisory Committee" is hereby created consisting of one representative of each Working Interest Owner signatory hereto, and its assigns, to be designated in writing by each party. The representative of the Unit Operator shall be chairman of the Committee. Each member shall have a vote equal to the proportionate or fractional acreage interest in the working interest owned by his principal in the participating area involved in any determination to be made by the Committee, or in the Unit Area where the determination concerns any matter affecting the Unit Area as a whole. Except as otherwise specified herein or in the Unit Agreement, an affirmative vote of 65% of the voting power of the Committee, taken in the manner to be determined by the Committee, referred to hereinafter, upon any matters upon which such Committee is authorized to act shall constitute the decision of the Committee and be binding on the Committee and upon each of the parties hereto; provided, however, that should any party own as much as 65% voting interest in the Unit Area or in a participating area, as the case may be, its vote must be supported by the affirmative vote of at least one additional party to bind all the parties hereto; and provided further that if one party owns 30% or more voting interest, the vote of such party shall not serve to defeat or disapprove any matter approved by the majority (over 50%) unless supported by at least one additional voting interest but in case the foregoing provisions would either carry or defeat both the affirmative and negative vote on any issue, such issue shall be determined by the larger vote. The Committee is authorized to adopt a rule providing that where any action is agreed to in writing by all members of the Committee, it shall be part of the Committee's records and shall have the same force and effect as if adopted at a regular meeting at which a quorum was present.

6. POWERS AND DUTIES OF ADVISORY COMMITTEE: The Advisory Committee shall be charged, subject to the provisions of this agreement, with compliance with the terms and conditions of the Unit Agreement and the leases and necessary contracts affecting

the development and operation of the lands covered hereby as long as the same shall be owned and held by the parties hereto, and shall have, among other powers, the power and authority:

(a) to exercise the powers of the Working Interest Owners set forth in the Unit Agreement and this agreement;

(b) to adopt such rules and regulations as it may deem advisable for its proper functioning including the selection of the time and place for holding regular meetings, calling of special meetings, and the manner of taking votes on any question.

(c) to approve or disapprove the location, drilling, and letting of contracts for drilling or recompletion of any and all wells. The approval of the drilling or recompletion of any well shall be construed to mean and include the approval of any necessary expenditures for the drilling, completing and equipping of such well, including the necessary lines, separators, and necessary tankage if a producer, and if a dry hole the plugging and abandonment thereof, except as otherwise provided in Section 9 and 17 hereof.

(d) to approve or disapprove any single expenditure in excess of \$5,000.00 other than normal operating expenses.

(e) to approve or disapprove the use of facilities owned by one participating area for purposes of operation and development outside of said area, and to determine the amount of any charges therefor, unless otherwise provided for in this agreement or in the Unit Agreement.

(f) to approve or disapprove any expenditure for expert technical advice including any extra services rendered by Unit Operator's technical staff not contemplated by the provisions of the Accounting Procedure, hereto attached, marked "Exhibit 1," and not covered by the overhead, district, and camp expenses therein authorized, which overhead in said Accounting Procedure is intended to only cover normal development and operations.

(g) to approve or disapprove any partial relinquishment of the rights of the Unit Operator.

(h) to approve or disapprove the abandonment of any well or wells or the disposal of any major items of surplus material or equipment other than junk, having an original cost of \$1,000.00 or more (any such item or items of less cost may be disposed of without such approval), except as otherwise provided in Section 17 hereof.

(i) to approve or disapprove any proposed plan for development of the Unit Area or any participating area or amendment thereof, or any proposed expansion or contraction of the Unit Area or any designation or enlargement of a participating

area, unless otherwise required by Public Authority.

(j) to determine the basis of investment adjustment and the adjusted basis of prorated future development and operating costs and to readjust percentages of participation upon enlargement or reduction of the Unit Area or enlargement of any participating area or upon elimination of acreage for failure of title.

(k) to approve or disapprove any arrangements for repressuring or cycling and to approve or disapprove any change in the existing method of operation.

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

Subject to the provisions hereof, Unit Operator shall have full control of the premises subjected hereto and shall conduct and manage the development and operation of unitized lands for the production of unitized substances therefrom for the account of the parties hereto.

It is specifically understood, that if the Working Interest in the initial participating area or any subsequent participating area or areas is owned by one party, such party shall alone control the action of the Unit Operator in all matters referred to above in respect thereto until such area or areas may be enlarged to include an additional Working Interest Owner or Owners therein.

7. INSURANCE: Unit Operator agrees that Contractors or Subcontractors will carry insurance as follows, to cover drilling and development operations on all lands subject to this agreement:

(a) Workmen's Compensation Insurance as required by the laws of the State of New Mexico.

(b) Contractor's Public Liability Insurance in amounts of \$100,000 for injuries for one person and \$300,000 for injuries in one accident.

(c) Automobile Public Liability and Property Damage Insurance in amounts of \$100,000 for injuries to one person, \$200,000 for injuries in one accident and \$10,000 for property damage.

With respect to production operations on all lands subject to this agreement, Unit Operator shall carry with a reputable insurance carrier, Workmen's Compensation Insurance, Contractor's Public Liability Insurance with limits of \$50,000 for one person and \$100,000 for one accident, and Automobile Public Liability Insurance with limits of \$100,000 for one person, \$200,000 for one accident and \$10,000 for property damage.

Unit Operator shall carry insurance required under this agreement at the expense of the parties hereto and for the benefit of Working Interest Owners hereunder; however, premiums for Automobile Public Liability and Property Damage Insurance on Unit Operator's fully-owned equipment shall not be charged directly to the joint account, but will be covered by the flat rate charges assessed for use of such equipment. Unit Operator will not carry at the expense of the joint account fire, wind-storm, explosion or underground damage insurance covering operations hereunder.

8. COST OF OPERATIONS: The actual cost to the Unit Operator of performing its obligations as Unit Operator hereunder shall be kept separately for each participating area, and in each area such cost shall be apportioned to each tract in the same ratio as that defined in the Unit Agreement for the allocation of production in that area, and among the Working Interest Owners in each tract in proportion to their comparative interests therein, and as so allocated shall be paid as hereinafter provided by the several Working Interest Owners, and as nearly as may be done all costs shall be charged directly to each participating area and the operations served. All such costs, expenses, credits, and related matters and the method of handling the accounting with respect thereto shall be in accordance with the provisions of the Accounting Procedure attached hereto, made a part hereof, and marked for identification as Exhibit "1", except that:

(a) Unit Operator shall not apportion any part of the salaries and expenses of its District Superintendent, other general district employees, or district office expenses to the joint account as provided in Paragraph 11 of Section II of said Exhibit "1", and the monthly per well overhead rates set forth under Paragraph 12 of Section II of said Exhibit "1" shall be in lieu of any charges for any part of the compensation or salaries paid to Unit Operator's District Superintendent and to other general district employees and shall be in lieu of any charges for district office expenses as well as Unit Operator's division office and principal business office expenses, but said overhead rates shall not be in lieu of any charges for any part of the compensation or salaries paid to Unit Operator's Field Superintendent and general field employees and shall not be in lieu of any charges for field office and camp expenses;

(b) For wells of a depth either under 4,000 feet or over 8,000 feet, the following overhead rates shall apply in lieu of the rates set forth in Paragraph 12 of Section II of Exhibit "1":

<u>Well Depth</u>	<u>Drilling Wells</u>	<u>Producing Wells</u>		
		<u>First Five</u>	<u>Next Five</u>	<u>All Wells Over 10</u>
Under 4,000'	\$100.00	\$25.00	\$15.00	\$10.00
Over 8,000'	300.00	60.00	50.00	40.00

(c) At the time material is needed for operations hereunder, the Unit Operator may be compelled to furnish from its warehouse or other properties material procured or purchased at prices in excess of those determined in accordance with the provisions of Paragraph 2 of Section III of said Exhibit "1". In such event, the Unit Operator shall notify the Working Interest Owner of such material, and the Working Interest Owner, within a period of ten (10) days after receipt of said notice, shall advise the Unit Operator whether the Working Interest Owner elects to furnish in kind at the location, or at the railway receiving point nearest thereto, its proportionate share of any such material which is capable of being separately furnished in kind; provided, that the Unit Operator shall not be obligated to accept any such material from the Working Interest Owner unless, in the opinion of the Unit Operator, it is of a type, size and capacity, and in a condition, acceptable for use by the Unit Operator in the joint account operation. In the event that the Working Interest Owner does not so furnish in kind its said proportionate share of such material, the Unit Operator shall transfer to the joint account operation all such material not so furnished and, notwithstanding any provisions of said Paragraph 2 of Section III to the contrary, shall charge the non-furnishing Working Interest Owner for its proportionate share thereof on the basis of the Unit Operator's direct costs and expenses (not including any salaries or expenses of its personnel which are included in the overhead charges hereunder) incurred in procuring or purchasing and shipping such material so transferred and in moving it to the property.

(d) In the event of any conflict between the provisions contained in the body of this instrument or in the Unit Agreement and those contained in said Accounting Procedure, the provisions of the former shall govern to the extent of such conflict. The term "Operator" as used in Exhibit "1" shall be deemed to refer to the Unit Operator, and the term "Non-Operators" as used in Exhibit "1" shall be deemed to refer to the Working Interest Owners herein.

Unit Operator is hereby granted a prior lien upon the rights and interest of each Working Interest Owner in the Unit Area and the unitized substances allocated to each such Working Interest Owner, and the material and equipment thereon, to secure the payment of its proportionate part of the said costs and expenses. Should any Working Interest Owner fail to pay its proportionate part of said costs and expenses within thirty (30) days after being billed therefor as provided for in the referred to Accounting Procedure, Exhibit "1", Unit Operator shall have the right at its option at any time thereafter, such default continuing, to foreclose said lien upon the respective interests of such Working Interest Owner.

Unit Operator, at its election, may request each Working Interest Owner here-  
to to advance its respective proportion of the development and operating costs here-  
under in accordance with an estimate by Unit Operator to be made not less than ten  
days in advance of the month in which the costs and expenses are to be incurred. The  
costs and expenses actually incurred in such month shall be billed to each party as  
herein otherwise provided, and the advances made by each party under the provisions  
of this Section, less any delinquencies of such party in the payment of his operating  
expenses, shall constitute a credit against estimates thereafter made by Unit Operator  
under the provisions of this Section. Each month adjustments shall be made between  
Unit Operator and each party in order that the advances to the credit of each party  
shall equal his share of the estimated expenses to be incurred in the succeeding  
month.

9. TEST WELLS: The cost of drilling, equipping and completing the Dakota test  
well provided for in Section 9 of the Unit Agreement, and the cost of plugging and  
abandoning same if a dry hole shall be paid (and advanced if required by Unit Opera-  
tor) by all the Working Interest Owners hereto in the proportion that the ownership  
of working interests on an acreage basis within the Unit Area of each party hereto  
bears to the total working interests on an acreage basis in the Unit Area owned by  
all parties hereto, except that the obligations of Stanolind Oil and Gas Company with  
respect to said test well shall be only as contained in that 'Farmout Contract' dated  
March 8, 1951, between said company, and Blackwood & Nichols, et al, reference to  
which is made for greater particularity.

In the event it is decided to drill any additional Dakota test wells prior  
to establishing a Dakota participating area, or prior to the establishment of an ad-  
ditional participating area, or any additional test wells to test heretofore untested  
formations, such wells shall be drilled by the Unit Operator except as otherwise may  
be provided by this agreement. The basis of contribution to the cost of such wells  
and the final adjustment of disposition of such costs shall be made the subject of a  
special agreement between the Unit Operator and the Working Interest Owners.

10. ESTABLISHMENT OF NEW PARTICIPATING AREAS OR ENLARGEMENT OF EXISTING PARTICI-  
PATING AREAS: In the event any test well drilled shall encounter the unitized sub-  
stances in quantity sufficient to justify the establishment of a new and separate  
participating area or the enlargement of an existing participating area for the forma-  
tion encountered, such participating area or enlargement shall be formed as provided  
in Section 11 of the said Unit Agreement. Upon the establishment of any participat-  
ing area, there shall be a retroactive adjustment of the cost of drilling, completing,  
equipping for production and operating the said test well from the commencement of

operations on said well until the effective date of the establishment to the end that the owners of working interests in the participating area newly established shall reimburse without interest the party or parties who paid for the cost and expense of drilling, completing, equipping for production, and operating the well, less any income derived by the last named party or parties up to the date of settlement, and thereafter the costs incurred and benefits derived from the operation of the well shall be borne by and inure to the benefit of the Working Interest Owners in the participating area or areas, and the working interests attributable to the non-participating portion of the Unit Area shall thereafter be liable for no part of the costs and entitled to no part of the benefits derived therefrom.

11. FUTURE WELLS DRILLED BY UNIT OPERATOR: All wells drilled in the Unit Area by Unit Operator after the effective date of this agreement shall be drilled on a competitive contract basis at the usual rates prevailing in the region of the Unit Area. Unit Operator, if it so desires, may employ its own tools and equipment in the drilling of such wells, but in such event the charge therefor shall not exceed the competitive prevailing rate charged by independent contractors doing work of a similar nature. Before the commencement of the drilling of any well by the Unit Operator, the Unit Operator and the other affected Working Interest Owners shall agree upon the then competitive prevailing rate and upon the contract under which Unit Operator will drill such well.

12. WELLS DRILLED OUTSIDE PARTICIPATING AREA: The Unit Operator, upon obtaining the approval, where necessary of Federal or State authority, may drill any test well within the Unit Area but outside the boundaries of any established participating area, for the account, and at the sole cost, risk and expense of the Working Interest Owners within any participating area, but such participating area shall be committed to the drilling of such a well only by the consent of the parties owning an interest in the same as provided in Section 5 and 6 hereof. In the alternative such wells may be drilled as provided in Section 13 of the Unit Agreement.

13. CHANGE OF PARTICIPATING AREA - INVESTMENT ADJUSTMENT: Separate participating areas for different formations may be established and any participating area may be diminished on account of failure of title or may be enlarged, all as provided by the said Unit Agreement and this agreement. On the enlargement of any participating area there shall be an investment adjustment between the owners of working interest in the enlarged participating area who are parties hereto and the Working Interest Owners in the former participating area who are parties hereto, to the end that the investment in wells, well equipment, facilities, and all other property within the enlarged participating area shall be paid for by the affected Working Interest Owners in the en-

larged participating area proportionate to the interest of each in the cost of operation and revenue derived from the enlarged participating area, and also to the end that the parties who have previously paid said costs shall be reimbursed on the basis hereinafter set forth. The affected Working Interest Owners in the participating area before its enlargement shall receive credit for the intangible cost of drilling, completing, and equipping for production all wells capable of producing unitized substances situated within said participating area. The costs to be so credited shall be measured by the average cost of drilling, completing and equipping for production wells of like character and depth in that region in a good and workmanlike manner at the time when said wells were drilled. Credit shall also be given for the casing and other tangible property and facilities installed in the wells and for any structures, facilities or other property at a percentage of original cost, such percentage to be separately agreed upon by the Working Interest Owners in the enlarged participating area. The affected Working Interest Owners on any tract outside of the participating area that is to be admitted to the enlarged participating area shall likewise receive credit for the intangible cost of drilling, completing, and equipping any wells on their respective leases, together with the value of the tangible equipment, facilities, and structures located thereon and used in connection therewith on the basis as last hereinabove set out. The sum total of all credit shall be the investment cost apportionable to the enlarged participating area. The investment adjustment shall be made by cash settlement among the Working Interest Owners through the Unit Operator. No credit shall be given for the previous cost of operating any wells or repairing or maintaining other property, nor shall there be any debit for and on account of production taken from wells prior to the effective date of the enlargement of the participating area.

14. MARGINAL WELL - SEPARATE OPERATION: In the event that any well drilled under the provisions of Section 16 hereof shall encounter the unitized substances in producible but not in paying quantities, so that the well is not admitted to any participating area, it may be separately operated by the parties who financed the drilling thereof for their own account as provided by Section 13 of the Unit Agreement. If the drilling of the well was financed by parties other than the Working Interest Owners on the well tract, such Working Interest Owners may at any time take over the well by reimbursing the parties financing the same for the unrecovered portion of the drilling and operating costs thereof; but if the parties who financed any such well desire to abandon the same, the Working Interest Owners on the well tract may then take over and operate the well by payment of the fair salvage value of the casing and other necessary equipment left in the well, provided also that if the Working Interest

Owners on the well tract do not elect to take over and operate such well, the same shall be plugged and abandoned at the cost of the parties who financed such well.

15. TAXES: All ad valorem taxes assessed on privately owned land within the Unit Area shall be paid by the owner of the land unless otherwise provided in any contract or agreement between such owner and a Working Interest Owner hereunder. Each Working Interest Owner, however, shall ascertain that the land contributed by it to the Unit Area shall not be sold for nonpayment of any ad valorem taxes constituting a lien thereon and in the event of such sale, such Working Interest Owner shall, at its own expense, effect the redemption of such land or take any other measures permitted by law or the terms of its lease to prevent the loss of the land as a result of the tax sale.

Unit Operator, subject to the provisions of the Unit Agreement, shall render and pay all taxes on tangible personal property owned by the Working Interest Owners in all participating areas and all other taxes of any nature or kind whatever (except the Federal and State income taxes in any state, licenses, franchises, or other similar tax necessary to be paid by the parties hereto to maintain their corporate existence) and shall charge to and collect such taxes from the respective Working Interest Owners in the respective participating areas in the proportion that each of such parties participates in the unitized substances produced therefrom as set out in the percentage participation schedules applicable to such areas.

In the event any taxable valuation is assessed on or against said property or any portion thereof, which the Unit Operator deems to be unreasonable, it shall be the duty of Unit Operator to protest said taxable valuation within the time and manner as prescribed by law, and prosecute such protest to final determination. When any such protested valuation of such property shall have been determined, Unit Operator shall pay, for the joint account, the taxes thereon, together with any interest or penalty accrued by reason of such protest, and bill each party for its proportionate share of such payments in accordance with the Accounting Procedure, "Exhibit 1," hereto attached.

16. DRILLING OF ADDITIONAL WELLS: Except for the Dakota test well to be drilled under this agreement in the Unit Area as provided in Section 9 hereof, any Working Interest Owner who desires to be relieved of the obligation to contribute to the cost and the obligation to share in the risk of drilling any well at a location outside the boundaries of an existing participating area, or to test any untested formation, may be so relieved by notifying the Unit Operator in writing prior to the commencement of operations for said well.

Certain further provisions are made in Section 13 of the Unit Agreement as to the drilling of such outside well by the party or parties owning or controlling a majority of the working interests under such well location. The basis of contribution to the cost of such well and the final adjustment or disposition of such costs shall be made the subject of a special agreement between the parties financing said well. Said cost in either event shall include, if a producer, the cost of completing and equipping the well for production, and, if a nonproducer, the cost of plugging and abandoning the well.

In either case, if the well produces unitized substances in producible but not in paying quantities, the said well shall be handled as provided in the third paragraph in Section 13 of the Unit Agreement and, if operated by the Unit Operator, shall be operated for the account of the Working Interest Owners who participated in the cost and risk of drilling the well.

Likewise in either case, if said well is completed as a producer of unitized substances in paying quantities, the well shall be operated by the Unit Operator in the appropriate participating area as enlarged or to be established as a result of the drilling of this well as the case may be, and there shall be an investment adjustment among the Working Interest Owners as provided in Section 10 or Section 13 hereof as the case may be. Separate accounts shall be maintained as to costs and production of said well and the entire Working Interest portion of the production from the well after deducting 100% of the operating costs attributable to the well to the date of reimbursement hereinafter provided for, shall be first allocated to the Working Interest Owners who participated in the cost and expense of drilling said well in proportion to their contribution to the cost of such well, until said Working Interest Owners have received from the proceeds thereof, in addition to the 100% credit for the cost of the well allowed above in the investment adjustment, an additional 50% of the cost of drilling, testing, completing and equipping such well. After the parties who participated in the cost of drilling said well have been fully reimbursed to the extent above described, then and thereafter said well shall be operated by the Unit Operator for the joint account of all Working Interest Owners herein, and the subsequent costs and expenses of operation and the production derived therefrom shall be apportioned in the same manner and in the same proportion as if all Working Interest Owners hereto had originally participated in the drilling of said well.

If any well be drilled hereunder to test any formation other than the formation then producing in any participating area and said well is not completed as a paying producer from the objective formation but the well can be plugged back or deepened, as

the case may be, and made into a paying producer in a formation for which a participating area has been established, the Working Interest Owners in the affected participating area shall have the right to take over said well and cause the Unit Operator to plug back or deepen as the case may be and to complete and operate it all for the account of such participating area upon effecting an investment adjustment for the cost of said well from the surface to such producing formation on the same basis provided in Section 13 hereof.

Notwithstanding the foregoing, in the event Unit Operator is required to drill an extension well outside the boundaries of any participating area or any development well within a participating area by governmental order, or demand, whether such order or demand is initiated by the government independent of its consideration of any plan of development, or is issued as a required alteration of a plan of development, the cost of drilling and completing said well if a producer, and of plugging and abandoning the well if a dry hole, shall be borne by all of the Working Interest Owners in said participating area in proportion to their interest therein. The consent of a Working Interest Owner to a plan of development calling for the drilling of a well or wells shall be deemed consent to participate in the cost of drilling such well or wells. Should Unit Operator be required by governmental order to drill a well to test any previously untested formation in the Unit Area, the costs of drilling and equipping such well if a producer, and plugging and abandoning the well if a dry hole, shall be initially borne by all of the parties hereto in the manner provided for a test well in Section 9 hereof; provided, further, that in the event such well is completed as a paying producer resulting in the establishment of a participating area, the parties advancing said costs shall be reimbursed for all the costs of drilling, equipping and operating the well by cash adjustment by the Working Interest Owners in the Participating Area, after which, the well shall be owned by and operated for the account of the Working Interest Owners of the participating area so established.

In the event any well is multiply completed as a paying producer in more than one formation, the Working Interest Owners of the respective participating areas established for such formations shall arrange for an appropriate allocation of investment and operating costs of such well by separate agreement.

17. OPTION AS TO ABANDONMENT OF WELLS: If the affected Working Interest Owners hereto are unable to agree as to the proposed abandonment of any well or wells, then such party or parties not desiring to abandon the same shall tender to the other affected Working Interest Owner or Owners a sum equal to the last named parties' proportionate share in the salvage of the material and equipment in said well or wells

determined in accordance with the Accounting Procedure 'Exhibit 1', hereto attached and upon receipt of said sum, the said parties wishing to abandon said well shall assign to the other Working Interest Owners their rights in the well and well property down to and including the producing formation in the land on which said well is situated, said well may thereafter be operated by the Unit Operator for the separate account of the remaining Working Interest Owners. Proper bills of sale and division orders shall be executed by the assigning parties to accomplish the purposes hereof, and no further wells shall be drilled to the producing formation within the drainage area of said well as established by the well spacing system then in use in said field, but there shall be no conveyance of any rights in and to any land or leasehold rights in the acreage surrounding said well, and the percentage of participation of the parties under the Unit Agreement and this Agreement as to all other wells then or thereafter drilled and as to the land and leasehold rights under this Agreement and the Unit Agreement shall be unaffected by this transfer.

18. ASSIGNMENTS: Any Working Interest Owner may, at any time, transfer or assign all of his working interest to any other Working Interest Owner who is then a party to the Unit Agreement and to this agreement, or to any other person, association or corporation, when such assignment is made expressly subject to the terms of the Unit Agreement and the terms of this agreement, and wherein the assignee shall accept and agree to perform all duties, obligations, and liabilities thereof. In such assignment, it shall be competent for the assignor to reserve a royalty interest. Upon the making of such assignment, irrespective of whether a royalty interest is reserved, the assignor shall thereupon be relieved of all future duties, obligations and liabilities of a Working Interest Owner under this agreement and under the Unit Agreement. A partial assignment of working interest shall be effective as above described to the extent of the interest so assigned.

19. WITHDRAWAL OF PARTY: If any party hereto so desires, it may withdraw from this agreement by conveying, assigning, and transferring, without warranty, either express or implied to the other parties hereto who do not desire to withdraw all of its right, title and interest in and under the leases included in the Unit Area, together with the withdrawing party's interest in all wells, casing, material, equipment, fixtures, and other personal property belonging to the joint account, but such conveyance or assignment shall not relieve said party from any obligation or liability accruing or incurred prior to the date thereof. The interest so conveyed and assigned shall be held and owned by the assignees in the proportion set out in applicable percentage participation schedules and; thereupon the withdrawing party shall be relieved from all obligations and liabilities thereafter to accrue under this contract, and

the right of such party to any benefits subsequently accruing hereunder shall cease; but assignees shall pay assignor for its interest in all casings, material, equipment, fixtures, and other personal property owned by the joint account at the salvage value thereof, computed in accordance with the Accounting Procedure, "Exhibit 1," hereto attached.

20. LIABILITY: The liability of the parties hereunder shall be several and not joint or collective. Each party shall be individually responsible only for its own obligations as set out in this agreement and shall be liable only for its proportionate share of the costs and expenses as provided by this contract, and nothing herein contained or implied shall be deemed to create a partnership between or among the parties hereto. Whenever in this agreement reference is made to operations for the account of any of the parties hereto or to charges or credit to the account of the parties hereto, or whenever similar language is used, the parties use such language merely as a convenient method of referring to the accounting necessary between them, and it is agreed that no such phraseology shall ever be construed as creating any joint liability upon the part of the parties hereto for any obligation incurred under this agreement, or as setting apart or creating any fund or jointly owned property for the satisfaction of any such obligation; or as creating a common fund for any other purpose. No funds received by Unit Operator under this agreement, whether received as proceeds from the sale of unitized substances, or as advances or as payments on account of costs or expenses, or otherwise, need be segregated by Unit Operator or maintained by it as a joint fund, but may be commingled with its own funds and distributed by Unit Operator as provided for in this agreement.

Unit Operator shall not be liable or responsible for any damage to the Unit Area or the property, equipment or facilities used in the development and operation thereof, or for the loss of any production arising out of its operation of the Unit Area, except only for bad faith or gross negligence in connection therewith.

If, and in the event, notwithstanding the foregoing provisions of this section, the Unit, the Unit Operator or any member of the Unit is held liable by a court of competent jurisdiction for any matter or thing for which it is herein provided the Unit or person so named shall not be liable, the amount of such liability as finally determined shall thereupon be treated, regarded and paid as an item of unit expense.

21. NOTICES: All notices required or permitted to be given hereunder shall be in writing and shall be deemed to have been properly served and addressed when sent by mail or telegram to the parties executing this agreement at the addresses set opposite their respective names.

22. SUBSEQUENT JOINDER: Any Working Interest Owner having interests in the Unit Area who for any reason does not subscribe to this agreement at the time of its

inception may subsequently become a party thereto by signing an instrument with the Unit Operator expressly ratifying this agreement; however, the Unit Operator may in its discretion refuse to admit a Working Interest Owner to participation in this agreement unless all the Working Interest Owners having interests in the tract or tracts of land in which the applicant Working Interest Owner has an interest likewise elect to join. The Unit Operator shall promptly furnish to the remaining Working Interest Owners who are then parties hereto, with copies of all such instruments.

This agreement may be executed in any number of counterparts with the same force and effect as if all the parties had signed the same document.

23. DISPOSAL OF PRODUCTION: Each of the parties hereto shall own and, at its own expense, shall take in kind and separately dispose of its proportionate part of all the oil, gas, casinghead gas and other hydrocarbon substances produced and saved from the lease acreage covered hereby, exclusive of the production which the Unit Operator may use in developing and producing operations and in preparing and treating oil for market purposes and of production unavoidably lost; provided that each of the parties shall pay, or secure the payment of the royalty interest in its proportionate part of the production.

24. UNAVOIDABLE DELAY: All obligations under this agreement requiring the Unit Operator to commence or continue drilling or to operate on or produce unitized substances from any of the lands covered by this agreement shall be suspended while, but only so long as, the Unit Operator despite the exercise of due care and diligence is prevented from complying with such obligations, in whole or in part, by strikes, lockouts, acts of God, Federal, State, or municipal laws or agencies, unavoidable accidents, uncontrollable delays in transportation, inability to obtain necessary materials in open market, or other matters beyond the reasonable control of the Unit Operator whether similar to matters herein enumerated or not.

25. EFFECTIVE DATE AND TERM: This agreement shall become effective as to all parties executing the same upon the effective date of the Unit Agreement, and the term hereof shall be the same as that of the Unit Agreement. This agreement may be terminated in any manner by which the said Unit Agreement may be terminated.

IN WITNESS WHEREOF, the parties have executed this contract the day and year first above written.

DATE:

UNIT OPERATOR AND WORKING INTEREST OWNER

BLACKWOOD & NICHOLS COMPANY

By

  
General Partner

WORKING INTEREST OWNERS

STANOLIND OIL AND GAS COMPANY

ATTEST:

DATE:

*[Signature]*  
Ass't Secretary

By

*[Signature]* 4/83  
Vice President

APPROVED  
*[Signature]*  
2/14

Address: \_\_\_\_\_

ATTEST:

DATE:

\_\_\_\_\_  
Secretary

By

\_\_\_\_\_  
President

Address: \_\_\_\_\_

ATTEST:

DATE:

\_\_\_\_\_  
Secretary

By

\_\_\_\_\_  
President

Address: \_\_\_\_\_

ATTEST:

DATE:

\_\_\_\_\_  
Secretary

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President

Address: \_\_\_\_\_

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President

Address: \_\_\_\_\_

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DATE:

\_\_\_\_\_  
Secretary

By

\_\_\_\_\_  
President

Address: \_\_\_\_\_

ATTEST:

DATE:

\_\_\_\_\_  
Secretary

By

\_\_\_\_\_  
President

Address: \_\_\_\_\_



STATE OF Oklahoma)  
COUNTY OF  Tulsa )

On this 13 day of August, 1951, before me appeared \_\_\_\_\_  
J. J. Rouse, to me personally known, who, being by me duly  
sworn, did say that he is the Vice President of \_\_\_\_\_  
Shenandoah Oil and Gas Company  
and that the seal affixed to said instrument is the corporate seal of said corporation,  
and that said instrument was signed and sealed in behalf of said corporation by  
authority of its Board of Directors, and said J. J. Rouse  
acknowledged said instrument to be the free act and deed of said corporation.

Given under my hand and notarial seal this 13 day of August, 1951.

My Commission expires:  
My Commission Expires May 11, 1955

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

STATE OF \_\_\_\_\_)  
COUNTY OF \_\_\_\_\_)

On this \_\_\_ day of \_\_\_\_\_, 19\_\_\_, before me appeared \_\_\_\_\_  
\_\_\_\_\_, to me personally known, who, being by me duly  
sworn, did say that he is the \_\_\_\_\_ President of \_\_\_\_\_  
and that the seal affixed to said instrument is the corporate seal of said corporation,  
and that said instrument was signed and sealed in behalf of said corporation by  
authority of its Board of Directors, and said \_\_\_\_\_  
acknowledged said instrument to be the free act and deed of said corporation.

Given under my hand and notarial seal this \_\_\_ day of \_\_\_\_\_, 19\_\_\_,

My Commission expires:  
\_\_\_\_\_

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

STATE OF \_\_\_\_\_)  
COUNTY OF \_\_\_\_\_)

On this \_\_\_ day of \_\_\_\_\_, 19\_\_\_, before me appeared \_\_\_\_\_  
\_\_\_\_\_, to me personally known, who, being by me duly  
sworn, did say that he is the \_\_\_\_\_ President of \_\_\_\_\_  
and that the seal affixed to said instrument is the corporate seal of said corporation,  
and that said instrument was signed and sealed in behalf of said corporation by  
authority of its Board of Directors, and said \_\_\_\_\_  
acknowledged said instrument to be the free act and deed of said corporation.

Given under my hand and notarial seal this \_\_\_ day of \_\_\_\_\_, 19\_\_\_

My Commission expires:  
\_\_\_\_\_

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

STATE OF \_\_\_\_\_)  
COUNTY OF \_\_\_\_\_)

On this \_\_\_ day of \_\_\_\_\_, 19\_\_\_, before me appeared \_\_\_\_\_  
\_\_\_\_\_, to me personally known, who, being by me duly  
sworn, did say that he is the \_\_\_\_\_ President of \_\_\_\_\_  
and that the seal affixed to said instrument is the corporate seal of said corporation,  
and that said instrument was signed and sealed in behalf of said corporation by  
authority of its Board of Directors, and said \_\_\_\_\_  
acknowledged said instrument to be the free act and deed of said corporation.

Given under my hand and notarial seal this \_\_\_ day of \_\_\_\_\_, 19\_\_\_

My Commission expires:  
\_\_\_\_\_

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

STATE OF \_\_\_\_\_ )  
COUNTY OF \_\_\_\_\_ )

On this \_\_\_\_\_ day of \_\_\_\_\_, 19\_\_\_\_, before me personally appeared

to me known to be the person \_\_\_\_\_ described in and who executed and delivered the foregoing instrument, and acknowledged to me that \_\_\_\_\_ executed the same as \_\_\_\_\_ free act and deed.

GIVEN UNDER MY HAND AND SEAL OF OFFICE, this \_\_\_\_\_ day of \_\_\_\_\_, 19\_\_\_\_.

My Commission expires:

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

STATE OF \_\_\_\_\_ )  
COUNTY OF \_\_\_\_\_ )

On this \_\_\_\_\_ day of \_\_\_\_\_, 19\_\_\_\_, before me personally appeared

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GIVEN UNDER MY HAND AND SEAL OF OFFICE, this \_\_\_\_\_ day of \_\_\_\_\_, 19\_\_\_\_.

My Commission expires:

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

STATE OF \_\_\_\_\_ )  
COUNTY OF \_\_\_\_\_ )

On this \_\_\_\_\_ day of \_\_\_\_\_, 19\_\_\_\_, before me personally appeared

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GIVEN UNDER MY HAND AND SEAL OF OFFICE, this \_\_\_\_\_ day of \_\_\_\_\_, 19\_\_\_\_.

My Commission expires:

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

STATE OF \_\_\_\_\_ )  
COUNTY OF \_\_\_\_\_ )

On this \_\_\_\_\_ day of \_\_\_\_\_, 19\_\_\_\_, before me personally appeared

to me known to be the person \_\_\_\_\_ described in and who executed and delivered the foregoing instrument, and acknowledged to me that \_\_\_\_\_ executed the same as \_\_\_\_\_ free act and deed.

GIVEN UNDER MY HAND AND SEAL OF OFFICE, this \_\_\_\_\_ day of \_\_\_\_\_, 19\_\_\_\_.

My Commission expires:

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

STATE OF \_\_\_\_\_ )  
COUNTY OF \_\_\_\_\_ )

On this \_\_\_\_\_ day of \_\_\_\_\_, 19\_\_\_\_, before me personally appeared

to me known to be the person \_\_\_\_\_ described in and who executed and delivered the foregoing instrument, and acknowledged to me that \_\_\_\_\_ executed the same as \_\_\_\_\_ free act and deed.

GIVEN UNDER MY HAND AND SEAL OF OFFICE, this \_\_\_\_\_ day of \_\_\_\_\_, 19\_\_\_\_.

My Commission expires:

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

R E C A P I T U L A T I O N

<u>Land</u>	<u>Acres in Unit</u>	<u>Percentage of Unit Area</u>
Federal	26,076.90	79.00
State	3,750.47	11.36
Patented	<u>3,181.39</u>	<u>9.64</u>
Total of Unit Area	33,008.76	100.00%

1984 JUN 24 AM 8:24  
MAIN OFFICE OCC

Attached to and made a part of Unit Operating Agreement under unit agreement for the development and operation of the Northeast Blanco Unit Area, County of San Juan, State of New Mexico

## ACCOUNTING PROCEDURE (UNIT AND JOINT LEASE OPERATIONS)

### I. GENERAL PROVISIONS

#### 1. Definitions

The term "joint property" as herein used shall be construed to mean the subject area covered by the agreement to which this "Accounting Procedure" is attached.

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

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

#### 2. Statements and Billings

Operator shall bill Non-Operator on or before the last day of each month for its proportionate share of costs and expenditures during the preceding month. Such bills will be accompanied by statements, reflecting the total costs and charges as set forth under Sub-Paragraph B below:

A. Statement in detail of all charges and credits to the joint account.

B. Statement of all charges and credits to the joint account, summarized by appropriate classifications indicative of the nature thereof.

C. Statements, as follows:

- (1) Detailed statement of material ordinarily considered controllable by Operators of oil and gas properties;
- (2) Statement of all other charges and credits to the joint account summarized by appropriate classifications indicative of the nature thereof; and
- (3) Statement of any other receipts and credits.

#### 3. Payments by Non-Operator

Each party shall pay its proportion of all such bills within fifteen (15) days after receipt thereof. If payment is not made within such time, the unpaid balance shall bear interest at the rate of six per cent (6%) per annum until paid.

#### 4. Audits

Payment of any such bills shall not prejudice the right of Non-Operator to protest or question the correctness thereof. All statements rendered to Non-Operator by Operator during any calendar year shall be conclusively presumed to be true and correct after eighteen months following the close of any such calendar year, unless within said eighteen months period Non-Operator takes written exception thereto and makes claim on Operator for adjustment. Failure on the part of Non-Operator to make claim on Operator for adjustment within such period shall establish the correctness thereof and preclude the filing of exceptions thereto or the making of claims for adjustment thereon. A Non-Operator, upon notice in writing to Operator and all other Non-Operators, shall have the right to audit Operator's accounts and records relating to the accounting hereunder, within eighteen months next following the close of any calendar year. Non-Operator shall have six months next following the examination of the Operator's records within which to take written exception to and make any and all claims on Operator. The provisions of this paragraph shall not prevent adjustments resulting from the physical inventory of property as provided for in Section VI, Inventories, hereof.

### II. DEVELOPMENT AND OPERATING CHARGES

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

#### 1. Rentals and Royalties

Delay or other rentals, when such rentals are paid by Operator for the joint account; royalties, when not paid direct to royalty owners by the purchaser of the oil, gas, casinghead gas, or other products.

#### 2. Labor, Transportation, and Services

Labor, transportation, and other services necessary for the development, maintenance, and operation of the joint property. Labor shall include (A) Operator's cost of vacation, sickness and disability benefits of employees, and expenditures or contributions imposed or assessed by governmental authority applicable to such labor, and (B) Operator's current cost of established plans for employees' group life insurance, hospitalization, pension, retirement, stock purchase, thrift, bonus, and other benefit plans of like nature, applicable to Operator's field payroll; provided that the charges under Part (B) of this paragraph shall not exceed five per cent (5%) of the total of such labor charged to the joint account.

#### 3. Material

Material, equipment, and supplies purchased or furnished by Operator, for use of the joint property. So far as it is reasonably practical and consistent with efficient and economical operation, only such material shall be purchased for or transferred to the joint property as required for immediate use, and the accumulation of surplus stocks shall be avoided.

#### 4. Moving Material to Joint Property

Moving material to the joint property from Vendor's or from Operator's warehouse in the district or from the other properties of Operator, but in either of the last two events no charge shall be made to the joint account for a distance greater than the distance from the nearest reliable supply store or railway receiving point where such material is available, except by special agreement with Non-Operator.

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

E. In connection with overhead charges, the status of wells shall be as follows:  
 D. \$ 25.00 per well per month for all producing wells over ten (10).  
 C. \$ 30.00 per well per month for the second five (5) producing wells.  
 B. \$ 40.00 per well per month for the first five (5) producing wells.  
 A. \$ 175.00 per month for each drilling well, beginning on the date the well is spudded and terminating when it is on production or is plugged, as the case may be, except that no charge shall be made during the suspension of drilling operations for fifteen (15) or more consecutive days.

joint property covered hereby the following overhead charges:  
 in the development and operation of said properties; and Operator shall have the right to assess against the or field office expenses incurred in operating any such properties, or any other expenses of Operator incurred in the development and operation of the division office located at Midland, Texas, and any portion of the office expense of the principal business office located at Oklahoma City, Okla., but which are not in lieu of district managing officers and employees of Operator, including the division superintendent, the entire staff and ex-overhead charges, which shall be in lieu of any charges for any part of the compensation or salaries paid to

**12. Overhead**

A proportionate share of the salaries and expenses of Operator's District Superintendent and other general district or field employees serving the joint property, whose time is not allocated direct to the joint property, and a proportionate share of maintaining and operating a district office and all necessary camps, including housing facilities for employees if necessary, in conducting the operations on the joint property and other leases owned and operated by Operator in the same locality. The expense of, less any revenue from, these facilities shall include depreciation or a fair monthly rental in lieu of depreciation on the investment. Such charges shall be apportioned to all leases served on some equitable basis consistent with Operator's accounting practice.

**11. District and Camp Expense**

A. Premiums paid for insurance carried for the benefit of the joint account, together with all expenditures incurred and paid in settlement of any and all losses, claims, damages, judgments, and other expenses, including legal services, not recovered from insurance carrier.  
 B. If no insurance is required to be carried, all actual expenditures incurred and paid by Operator in settlement of any and all losses, claims, damages, judgments, and any other expenses, including legal services, shall be charged to the joint account.

**10. Insurance**

All taxes of every kind and nature assessed upon or in connection with the properties which are the subject of this agreement, the production therefrom or the operation thereof, and which taxes have been paid by the Operator for the benefit of the parties hereto.

**9. Taxes**

A. If a majority of the interests hereunder shall so agree, actions or claims affecting the joint interests hereunder may be handled by the legal staff of one or more of the parties hereto, and a charge commensurate with the services rendered may be made against the joint account, but no such charge shall be made until approved by the legal department of or attorneys for the respective parties hereto.  
 B. Fees and expenses of outside attorneys shall not be charged to the joint account unless authorized by the majority of the interests hereunder.

**8. Litigation, Judgments, and Claims**

All costs and expenses of litigation, or legal services otherwise necessary or expedient for the protection of the joint interests, including attorney's fees and expenses as hereinafter provided, together with all judgments obtained against the joint account or the subject matter of this agreement; actual expenses incurred by any party or parties hereto in securing evidence for the purpose of defending against any action or claim prosecuted or urged against the joint account or the subject matter of this agreement.  
 A. If a majority of the interests hereunder shall so agree, actions or claims affecting the joint interests hereunder may be handled by the legal staff of one or more of the parties hereto, and a charge commensurate with the services rendered may be made against the joint account, but no such charge shall be made until approved by the legal department of or attorneys for the respective parties hereto.  
 B. Fees and expenses of outside attorneys shall not be charged to the joint account unless authorized by the majority of the interests hereunder.

**7. Damages and Losses**

Damages or losses incurred by fire, flood, storm, or any other cause not controllable by Operator through the exercise of reasonable diligence. Operator shall furnish Non-Operator written notice of damage or losses incurred by fire, storm, flood, or other natural or accidental causes as soon as practicable after report of the same has been received by Operator.

**6. Use of Operator's Equipment and Facilities**

Use of and service by Operator's exclusively owned equipment and facilities as provided in Paragraph 4, of Section III, "Basis of Charges to Joint Account."  
 Moving surplus material from the joint property to outside vendees, if sold f.o.b. destination, or minor returns to Operator's warehouse or other storage point. No charge shall be made to the joint account for moving major surplus material to Operator's warehouse or other storage point for a distance greater than the distance to the nearest reliable supply store or railway receiving point, except by special agreement with Non-Operator; and no charge shall be made to the joint account for moving material to other properties belonging to Operator, except by special agreement with Non-Operator.

**5. Moving Surplus Material from Joint Property**

- F. The above overhead schedule on producing wells shall be applied to individual leases; provided that, whenever leases covered by this agreement are operated as a unitized project in the interest of economic development, the schedule shall be applied to the total number of wells, irrespective of individual leases.
- G. The above specific overhead rates may be amended from time to time by agreement between Operator and Non-Operator if, in practice, they are found to be insufficient or excessive.

### 13. Warehouse Handling Charges

None

### 14. Other Expenditures

Any other expenditure incurred by Operator for the necessary and proper development, maintenance, and operation of the joint property.

## III. BASIS OF CHARGES TO JOINT ACCOUNT

### 1. Purchases

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

### 2. Material Furnished by Operator

Material required for operations shall be purchased for direct charge to joint account whenever practicable, except that Operator may furnish such material from Operator's stocks under the following conditions:

#### A. New Material (Condition "A")

- (1) New material transferred from Operator's warehouse or other properties shall be priced f. o. b. the nearest reputable supply store or railway receiving point, where such material is available, at current replacement cost of the same kind of material. This will include material such as tanks, rigs, pumps, sucker rods, boilers, and engines. Tubular goods (2" and over), shall be priced on carload basis effective at date of transfer and f. o. b. railway receiving point nearest the joint account operation, regardless of quantity transferred.
- (2) Other material shall be priced on basis of a reputable supply company's Preferential Price List effective at date of transfer and f. o. b. the store or railway receiving point nearest the joint account operation where such material is available.
- (3) Cash discount shall not be allowed.

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

- (1) Material which is in sound and serviceable condition and is suitable for reuse without reconditioning shall be classed as Condition "B" and priced at 75% of new price.
- (2) Material which cannot be classified as Condition "B" but which,
  - (a) After reconditioning will be further serviceable for original function as good second hand material (Condition "B"), or
  - (b) Is serviceable for original function but substantially not suitable for reconditioning, shall be classed as Condition "C" and priced at 50% of new price.
- (3) Material which cannot be classified as Condition "B" or Condition "C" shall be priced at a value commensurate with its use.
- (4) Tanks, derricks, buildings, and other equipment involving erection costs shall be charged at applicable percentage of knocked-down new price.

### 3. Warranty of Material Furnished by Operator

Operator does not warrant the material furnished beyond or back of the dealer's or manufacturer's guaranty; and, in case of defective material, credit shall not be passed until adjustment has been received by Operator from the manufacturers or their agents.

### 4. Operator's Exclusively Owned Facilities

The following rates shall apply to service rendered to the joint account by facilities owned exclusively by Operator:

- A. Water service, fuel gas, power, and compressor service: At rates commensurate with cost of providing and furnishing such service to the joint account but not exceeding rates currently prevailing in the field where the joint property is located.
- B. Automotive Equipment: Rates commensurate with cost of ownership and operation. Such rates should generally be in line with schedule of rates adopted by the Petroleum Motor Transport Association, or some other recognized organization, as recommended uniform charges against joint account operations and revised from time to time. Automotive rates shall include cost of oil, gas, repairs, insurance, and other operating expense and depreciation; and charges shall be based on use in actual service on, or in connection with, the joint account operations. Truck, tractor, and pulling unit rates shall include wages and expenses of driver.
- C. A fair rate shall be charged for the use of drilling and cleaning-out tools and any other items of Operator's fully owned machinery or equipment which shall be ample to cover maintenance, repairs, depreciation, and the service furnished the joint property; provided that such charges shall not exceed those currently prevailing in the field where the joint property is located.
- D. Whenever requested, Operator shall inform Non-Operator in advance of the rates it proposes to charge.
- E. Rates shall be revised and adjusted from time to time when found to be either excessive or insufficient.

## IV. DISPOSAL OF LEASE EQUIPMENT AND MATERIAL

The Operator shall be under no obligation to purchase interest of Non-Operator in surplus new or secondhand material. Derricks, tanks, buildings, and other major items shall not be removed by Operator from the joint property without the approval of Non-Operator. Operator shall not sell major items of material to an outside party without giving Non-Operator an opportunity either to purchase same at the price offered or to take Non-Operator's share in kind.

