

BEFORE THE OIL CONSERVATION COMMISSION
OF THE STATE OF NEW MEXICO

IN THE MATTER OF THE APPLICATION OF
H & S OIL COMPANY, UNIT OPERATOR, FOR
APPROVAL OF THE UNIT AGREEMENT FOR THE
WEST ARTESIA GRAYBURG UNIT, COMPRISING
640 ACRES OF STATE AND FEE LANDS IN
SECTIONS 7, 8 AND 17, TOWNSHIP 18 SOUTH,
RANGE 28 EAST, N.M.P.M., EDDY COUNTY,
NEW MEXICO

OFFICE 900
97 Dec 18 AM 9 55

NO. 369.8

APPLICATION

COMES H & S OIL COMPANY, a partnership composed of
Rupert L. Heinsch and Herbert R. Spencer, by its attorney,
A. J. Losee, and states:

1. Applicant proposes to operate and develop as a
unitized area for the secondary recovery of oil from the
Grayburg formation under and by virtue of the terms of the
Unit Agreement, a copy of which is filed herewith and by
reference made a part hereof, the following lands in Eddy
County, New Mexico:

Township 18 South, Range 28 East, N.M.P.M.,

Section 7: SE/4 NE/4, E/2 SE/4
Section 8: S/2 NE/4, NW/4, N/2 SW/4,
SW/4 SW/4, N/2 SE/4
Section 17: N/2 NW/4

containing 640 acres, more or less.

2. The Unit Agreement establishes a participating
area comprising 640 acres of which 520 acres are State lands
and 120 acres are fee lands.

3. Applicant is proposed to be the Operator of the
unitized area.

4. Section 22 of the Unit Agreement, entitled
"Effective Date." provides for the execution or ratification

of the Agreement by working interest owners owning a combined unit participation of at least 85% and by royalty owners owning a combined interest of at least 65% of the royalty interest. When the Unit Agreement has been approved by the State of New Mexico, a sufficient number of working and royalty interest owners will have executed or ratified the instrument so that it will become effective pursuant to said Section 22.

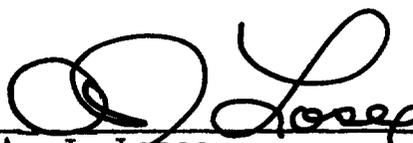
5. The Commissioner of Public Lands of the State of New Mexico has tentatively given his approval to the unit area and to the Unit Agreement.

6. The proposed plan for the development and operation of the Grayburg formation underlying the above described unit area will prevent waste and protect correlative rights and the method of allocating production among the various tracts within the unit area is fair to all of the working and royalty interest owners underlying the same.

WHEREFORE, Applicant prays that an order be entered approving the commingling of the contiguous developed proration units underlying the lands above described into a unit area, under and pursuant to the terms of the attached Unit Agreement.

H & S OIL COMPANY

By



A. J. Losee
P. O. Drawer 239
Artesia, New Mexico

UNIT AGREEMENT
WEST ARTESIA GRAYBURG UNIT
EDDY COUNTY, NEW MEXICO

11/20/57
Case
3698

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UNIT AGREEMENT
FOR THE DEVELOPMENT AND OPERATION OF THE
WEST ARTESIA GRAYBURG UNIT
EDDY COUNTY, NEW MEXICO

THIS AGREEMENT, made and entered into this _____ day of _____, 19____, by and between the parties subscribing, ratifying or consenting hereto, and herein referred to as "parties hereto",

W I T N E S S E T H:

WHEREAS, the parties hereto are the owners of working, royalty or other oil or gas interests in the Unit Area subject to this agreement;

WHEREAS, the Commissioner of Public Lands of the State of New Mexico is authorized by an Act of the Legislature (Sec. 7-11-39, N. M. S. 1953 Anno.) to consent to or approve this agreement on behalf of the State of New Mexico, insofar as it covers and includes lands and mineral interests of the State of New Mexico; and

WHEREAS, the Commissioner of Public Lands of the State of New Mexico is authorized by an Act of the Legislature (Sec. 7-11-41, N.M.S. 1953 Anno.) to amend with the approval of the lessee, any oil and gas lease embracing State lands so that the length of the term of said lease may coincide with the term of such unitized development and operation of State lands; and

WHEREAS, the Oil Conservation Commission of the State of New Mexico is authorized by law (Sec. 65-3-14, N.M.S. 1953 Anno.) to approve this agreement, and the conservation provisions hereof.

WHEREAS, the parties hereto hold sufficient interests in the West Artesia Grayburg Unit covering the land hereinafter described to give reasonably effective control of operation therein; and

WHEREAS, it is the purpose of the parties hereto, to enable institution and consumation of secondary recovery operations, to conserve natural resources, to prevent waste and secure the other benefits obtainable through development and operation of the area subject to this agreement under the terms, conditions and limitations herein set forth.

NOW THEREFORE, in consideration of the premises and the promises hereincontained, the parties hereto commit to this agreement their respective interests in the Unitized Formation as defined underlying the below defined Unit area, and agree severally among themselves as follows:

SECTION 1. UNIT AREA AND DEFINITIONS. For the purpose of this agreement, the following terms and expressions as used herein shall mean:

(a) "Unit Area" as specified on the map attached hereto marked Exhibit "A" is hereby designated and recognized as constituting the Unit Area, containing 720.00 acres, more or less.

(b) "Land Commissioner" is defined as the Commissioner of Public Lands of the State of New Mexico.

(c) "Commission" is defined as the Oil Conservation Commission of the State of New Mexico.

(d) The Grayburg Formation is defined and shall mean that heretofore established underground reservoir, the top of which is found at 1934 feet, and the base of which is found at 2324 feet, on the Radioactivity Log of the H & S Oil Company Wilson State 8-1 well located in the NW $\frac{1}{4}$ SE $\frac{1}{4}$ of Section 8 Township 18 South, Range 28 East, N.M.P.M. insofar as the same lies within the Unit Area,

(e) "Unitized Substance" means all oil, gas, gaseous substances, sulphur contained in gas, condensate, distillate and all associated and constituent liquid or liquefiable hydrocarbons within or produced from the Unitized Formation.

(f) "Unitized Formation" is defined as the portion of the Grayburg Formation effectively committed to this agreement.

(g) "Working Interest" is defined as the right to search for, produce and acquire Unitized Substances whether held as an incident ownership of mineral fee simple title, under an oil and gas lease and/or an interest in Unitized Substances which is a Working Interest as of the date the Owner thereof executes or ratifies this agreement, or which at any time thereafter becomes a Working Interest shall thence forth be treated as a Working Interest for all purposes of this agreement, or otherwise held.

(h) "Working Interest Owner" is defined as and shall mean any party hereto owning a Working Interest, including a carried working interest owner, holding an interest in Unitized Substances by virtue of a lease, operating agreement, fee title or otherwise, which interest is chargeable with and obligated to pay or bear, either in cash or out of production or otherwise, all or a portion of the cost of drilling, developing and producing the Unitized Substances.

(i) "Royalty Interest" or "Royalty" is defined as an interest other than a Working Interest in or right to receive a portion of the Unitized Substances or the proceeds thereof and includes the royalty interest reserved by the lessor by an oil and gas lease and any overriding royalty interest, oil payment interest, net profit contract, or any other payment or burden which does not carry with it the right to search for and produce Unitized Substances.

(j) "Royalty Owner" is defined as and shall mean the owner of a Royalty Interest.

(k) "Unit Operating Agreement" is defined as and shall mean any agreement or agreements (whether one or more) entered into (separately or collectively) by and between the Unit Operator and the Working Interest Owners as provided in Section 8, infra, and shall be styled "Unit Operating Agreement, WEST ARTESIA GRAYBURG UNIT, Eddy County, New Mexico".

(l) "Unit Manager" is defined as the person or corporation appointed by the Unit Working Interest Owners to perform the duties of the Unit Operator until the selection and qualification of a successor Unit Operator as provided for in Section 7 hereof.

(m) "Unit Operations" is defined as all operations conducted by Working Interest Owners or Unit Operator pursuant to this agreement and the Unit Operating Agreement for or on account of the development and operation of the Unitized Formation for the production of Unitized Substances.

(n) "Unit Equipment" is defined as all personal property, lease and well equipment, plants and other facilities and equipment taken over or otherwise acquired for the joint account for one in Unit Operations.

(o) "Unit Expense" is defined as all cost, expense or indebtedness incurred by Working Interest Owners or Unit Operator pursuant to this agreement and the Unit Operating Agreement for or on account of Unit Operations.

(p) "Outside Substances" is defined as all substances obtained from any source other than the Unitized Formation and which are injected into the Unitized Formation.

(q) "Phase I" is that period of time commencing on the 'Effective Date' of the Unit and ending at 7:00 A.M. on the first of the month following accumulated production from the Unitized Zone of 67,408 barrels of oil with associated Gases and Gas Liquids. During Phase I formula in Section 12 of Unit Agreement.

(r) "Phase II" is that period of time commencing at the end of Phase I and remain in effect so long thereafter as the Unit is in effect. During Phase II all production and all costs shall be allocated by Unit Participation as determined from Phase II formula in Section 12 of the Unit Agreement.

(s) "Unit Participation" of each Working Interest Owner is defined as the sum of the percentages obtained by multiplying such Working Interest Owner's fractional Working Interest in each tract by the tract participation of such tract, of Phase I or Phase II, whichever is in effect at the time.

(t) "Ultimate Primary" is the amount of oil produced from all tracts through the 'Effective Date' plus 67,408 barrels remaining primary from all tracts.

SECTION 2. EXHIBITS. Exhibit "A" attached hereto, is a map showing the Unit Area and the boundaries and indentivity of tracts and leases in said Unit Area to the extent known to the Unit Operator. Exhibit "B" attached hereto, is a schedule showing to the extent known to the Unit Operator the acreage comprising each tract, percentage ownership of each Working Interest Owner in each tract, and the percentage of participation, each tract has in the Unit Area. However, nothing herein or in said schedule or map shall be construed as a representation by any party hereto as to the ownersip of any interest other than such interest of interests as are shown in said map or schedule as owned by such party. Exhibits "A" and "B" shall be revised by the Unit Operator whenever changes in the Unit Area render such revision necessary, and copies of such revision shall be filed with and approved by the Land Commissioner as required.

SECTION 3. EXPANSION. The above described Unit Area may when practicable be expanded to include therein any additional tract or tracts regarded as reasonably necessary or advisable to conform with the purposes of this agreement. Such expansion shall be effected in the following manner.

(a) The owner or owners of the Working Interest of a tract or tracts desiring to bring such tract or tracts into the unit, shall file an application therefore with Unit Operator requesting such admission.

(b) Unit Operator shall circulate a notice to each Working Interest Owner of the proposed expansion, setting out the basis for admission the participation to be assigned on the basis of admission of such tract or tracts, and other pertinent data. After negotiation (at Working Interest Owners' meeting or otherwise) if at least three Working Interest Owners having in the aggregate eighty percent (80%) on the basis of Unit Participation have agreed to such tract or tracts being brought into the unit, then the Unit Operator shall:

(1) After preliminary concurrence by the Land Commissioner a notice of proposed expansion describing the contemplated changes in the boundaries of the Unit Area, the reason therefore, the basis for admission of the additional tract or tracts, participations to be assigned thereto and the proposed effective date thereof; and

(2) Deliver copies of said notice to the Land Commissioner, each Working Interest Owner and to the lessee and lessor whose interests are affected, advising such parties that thirty (30) days will be allowed for submission to the Unit Operator of any objection to such proposed expansion; and

(3) Upon the expiration of said thirty(30) day period as set out in (2) immediately above, file with the Land Commissioner the following; (a) Evidence of mailing or delivering copies of said notice of expansion; (b) An application for such expansion; (c) an instrument containing the appropriate joinders reflecting the qualifications of the new tract in the same manner required for the qualification of tracts under Section 14 hereof; and (d) Copies of any objections received.

The expansion shall, after due consideration of all pertinent information and approval by the Land Commissioner, become effective as of the date prescribed in the notice thereof, preferably the first day of the month subsequent to the date of notice, or on such other date as set by the Land Commissioner in the order or instrument approving such expansion.

There shall never be any retroactive allocation or adjustment of operating expenses or of interests in the Unitized Substances produced (or the proceeds of the sale thereof) by reason of an expansion of the Unit Area; provided, however, this limitation shall not prevent any adjustment of investment necessitated by such expansion.

SECTION 4. UNITIZED LAND AND UNITIZED SUBSTANCES. All land committed to this agreement as to the Unitized Formation shall constitute land referred to herein as "Unitized Land" or "land subject to this agreement". Nothing herein shall be construed to unitize, pool, or in any way affect the oil, gas and other minerals contained in or that may be produced from any formation other than the Unitized Formation as above described.

The Unit Operator and all working interest owners shall have the right of ingress and egress to all properties covered by this agreement.

SECTION 5. UNIT OPERATOR. H & S Oil Company is hereby designated the Unit Operator, and by signing this instrument as Unit Operator it agrees and consents to accept the duties and obligations of Unit Operator for the operation, development and production of Unitized Substances as herein provided. Whenever reference is made herein to the Unit Operator, such reference means the Unit Operator acting in that capacity and not as an owner of interests in Unitized Substances, and the term "Working Interest Owner" when used herein shall include or refer to the Unit Operator as the owner of a Working Interest when such an interest is owned by him.

SECTION 6. RESIGNATION OR REMOVAL OF UNIT OPERATOR. Unit Operator shall have the right to resign at any time, but such resignation shall not become effective so as to release Unit Operator from the duties and obligations of Unit Operator and terminate Unit Operator's rights as such for a period of six (6) months after written notice of intention to resign has been given by Unit Operator to all Working Interest Owners and the Land Commissioner, less a new Unit Operator shall have taken over and assumed the duties and obligations of Unit Operator prior to the expiration of said period.

The resignation of Unit Operator shall not release Unit Operator from any liability for any default by him hereunder occurring prior to the effective date of its resignation.

The Unit Operator shall upon default or failure in the performance of his duties hereof shall be subject to removal by at least two of the working interest owners having in the aggregate seventy-five percent (75%) or more of the Phase I or Phase II Unit Participation whichever is in effect at the time, exclusive of the working interest owner who is the Unit Operator. Such removal shall be effective upon notice thereof to the Land Commissioner.

In all such instances of effective resignation or removal, until a successor Unit Operator is selected and accepted as hereinafter provided, the Working Interest Owners shall be jointly responsible for the performance of the duties of the Unit Operator and shall, not later than thirty (30) days before such resignation or removal becomes effective, appoint a Unit Manager to represent them in any action to be taken hereunder.

The resignation or removal of Unit Operator under this agreement shall not terminate his right, title or interest as the owner of a Working Interest or other interest in Unitized Substances, but upon resignation or removal of Unit Operator becoming effective, such Unit Operator shall deliver possession of all equipment, books, and records, materials, appurtenances and any other assets, used in connection with Unit Operations and owned by the Working Interest Owners to the new duly qualified successor Unit Operator, or to the Unit Manager if no such new Unit Operator is elected, to be used for the purpose of conducting Unit Operations hereunder. Nothing herein shall be construed as authorizing the removal of any material, equipment or appurtenances needed for the preservation of any wells. Nothing herein contained shall be construed to relieve or discharge any Unit Operator who resigns or is removed hereunder from any liability or duties accruing or performable by him prior to the effective date of such resignation or removal.

SECTION 7. SUCCESSOR UNIT OPERATOR. Whenever the Unit Operator shall tender his resignation as Unit Operator or shall be removed as hereinabove provided, the Working Interest Owners shall select a successor Unit Operator as herein provided. Such selection shall not become effective until (a) a Unit Operator so selected shall accept in writing the duties and responsibilities of Unit Operator, and (b) the selection shall have been approved by the Land Commissioner. If no successor Unit Operator or Unit Manager is selected and qualified as herein provided, the Land Commissioner at his election, may declare this agreement terminated.

In selecting a successor Unit Operator the majority vote of the Working Interest Owners shall prevail, provided that in the event one Working Interest Owner should own more than forty-five percent (45%) voting interest, its vote shall not be regarded as sufficient unless supported by the vote of two or more Working Interest Owners having a combined voting interest of at least six percent (6%). If the Unit Operator who is removed votes only to succeed himself or fails to vote, the successor Unit Operator shall be selected by the affirmative vote of at least seventy-five percent (75%) of the voting interest remaining. In voting under this Section 7 each Working Interest Owner shall have a voting interest equal to their interest in Phase I or Phase II Unit Participation, whichever is in effect at the time.

SECTION 8. ACCOUNTING PROVISIONS AND UNIT OPERATING AGREEMENT. Costs and expenses incurred by Unit Operator in conducting Unit Operations hereunder shall be paid, apportioned among and borne by the Working Interest Owners in accordance with the Unit Operating Agreement. Such Unit Operating Agreement shall also provide the manner in which the Working Interest Owners shall be entitled to receive their respective proportionate and allocated share of the benefits accruing hereto in conformity with their underlying operating agreements, leases or other independent contracts and such other rights and obligations as between Unit Operator and the Working Interest Owners as may be agreed upon by the Unit Operator and the Working Interest Owners; however, no such Unit Operating Agreement shall be deemed either to modify any of the terms and conditions of this Unit Agreement or to relieve the Unit Operator of any right or obligation established under this agreement, and in case of any inconsistency or conflict between this agreement, and the Unit Operating Agreement, this Unit Agreement shall prevail. Two copies of the Unit Operating Agreement shall be filed with the Land Commissioner as required prior to approval of this agreement.

SECTION 9. RIGHTS AND OBLIGATIONS OF UNIT OPERATOR. Except as otherwise specifically provided herein, the exclusive right, privilege and duty of exercising any and all rights of the parties hereto which are necessary or convenient for prospecting for, producing, storing, allocating and distributing the Unitized Substances are hereby delegated to and shall be exercised by the Unit Operator as herein provided. Upon request by Unit Operator acceptable evidence of title to said rights shall be deposited with said Unit Operator, and together with this agreement, shall constitute and define the rights, privileges and obligations of Unit Operator. Nothing herein, however, shall be construed to transfer title to any land or to any lease or operating agreement, it being understood that under this agreement the Unit Operator, in its capacity as Unit Operator, shall exercise the rights of possession and use vested in the parties hereto only for the purposes herein specified.

SECTION 10. PLAN OF OPERATIONS. The initial plan of operation shall be filed with the Land Commissioner and the Commission concurrently with the filing of this Unit Agreement for final approval. Said initial plan of operation and all revisions thereof shall be as complete and adequate as the Land Commissioner and the Commission may determine to be necessary for timely operation consistent herewith. Reasonable diligence shall be exercised in complying with the obligations of the approved plan of operation.

It is recognized and agreed by the parties that all of the land subject to this agreement, is reasonably proved to be productive of Unitized Substances in paying quantities and that the object and purpose of this agreement is to formulate and to put into effect a secondary recovery project in order to effect additional recovery of Unitized Substances, prevent waste and conserve natural resources. The parties hereto agree that the Unit Operator may, subject to the consent and approval of a plan of operation by the Working Interest Owners, the Land

Commissioner and the Commission, inject into the Unitized Formation through any well or wells completed therein, brine, water, air gas, liquefied petroleum gases and any one or more other substances or combination of substances whether produces from the Unit Area or not, and that the location of input wells, the rates of injection therein and the rate of production shall be governed by standards of good geologic and petroleum engineering practices and conservation methods. Subject to like approval the plan of operation may be revised as conditions may warrant.

SECTION 11. EASEMENTS OR USE OF SURFACE. The parties hereto, to the extent of their rights and interest, hereby grant to Working Interest Owners the right to use as much of the surface of the land within the Participating Area as may reasonably be necessary for unit operations including the free use of water from, any formation in, above or below the Participating Area for unit operations.

SECTION 12. TRACT PARTICIPATION. In Exhibit "B" attached hereto, there are listed and numbered the various tracts within the Unit Area and set forth opposite each tract there are two figures the first preceded by "I" for Phase I and the second preceded by "II" for Phase II, which represents the percentage participation allocated to such tract calculated on one hundred percent (100%) tract commitment.

The percentage of participation of each tract was determined in accordance with the following formulas:

Percentage Participation of Each Tract for

PHASE I

$$\frac{\text{Tract Total Production from May, 1964 through October, 1964}}{\text{Unit Total Production from May, 1964 through October, 1964}}$$

Phase I is to be in effect until the total oil recovered after the Effective Date is 67,408 barrels.

Percentage Participation of Each Tract for

PHASE II

$$\frac{\text{Tract Ultimate Primary Recovery}}{\text{Unit Ultimate Primary Recovery}}$$

Phase II is to become effective at the end of Phase I and remain in effect so long thereafter as the Unit is in effect.

However, if the Unit Agreement is approved with less than One hundred (100%) percent commitment of the Unit Area, said participation percentage; shall be revised pursuant to Section 13 (Tracts Qualified for Unit Participation) to fit the Commitment Status as of the effective date hereof, and hereafter as needed pursuant to Section 14 (Allocation of Unitized Substance), and Phase I total oil recovery volume shall be revised as to the committed tracts remaining primary production, including PHASE II participation factor.

SECTION 13. TRACTS QUALIFIED FOR PARTICIPATION. On and after the effective date hereof, the tracts within the Unit Area which shall be entitled to participation in the production of Unitized Substances therefrom shall be those tracts within the Unit Area and more particularly described in Exhibit "B" that otherwise qualify as follows:

(a) Each tract as to which Working Interest Owners owning one hundred percent (100%) of the Working Interest have become parties to this agreement and as to which Royalty Owners owning seventy-five percent (75%) of the Royalty Interest have become parties to this agreement.

(b) Each tract as to which Working Interest Owners owning not less than eighty-five percent (85%) of the Working Interest have become parties to this agreement, regardless of the percentage of Royalty Interest therein that is committed hereto, and as to which the Working Interest Owners in said tract who have executed

this agreement have agreed to indemnify and hold harmless all other parties hereto in a manner satisfactory to the Working Interest Owners qualified under Section 13 (a) against any and all claims and demands that may be made by the non-joining interest owners on account of the inclusion of such tract in the Unit Area and the operation of the Unit Area on the basis herein provided. In the event less than eighty-five percent (85%) of the Working Interest Owners qualified under Section 13 (a) have approved the inclusion of such tract in the Unit Area, said tract shall not be considered qualified to be included in the Unit. Upon the inclusion of such tract in the Unit Area, the Participation that would have been attributed to the Working Interest Owners in such tract who have become parties to this agreement, in proportion to their respective Working Interest in the tract.

If, on the effective date of this agreement, there is any tract or tracts within the unit area which have not been effectively committed to or made subject to this agreement by qualifying as above provided, then such tract or tracts shall not be entitled to participate hereunder. Unit Operator shall, when submitting this agreement for final approval by the Land Commissioner, or as soon thereafter as practicably, file therewith a schedule of those tracts which have been committed and made subject to this agreement and are entitled to participate in the production from the participating area hereunder. Said schedule shall set forth opposite each such committed tract the lease number and assignment number, the owner of record of the lease, and the percentage participation of such tract which shall be computed according to the participation formula set out in Section 12 (Tract Participation) above. This schedule of participation shall be a part of Exhibit "B" and, upon approval thereof by the Land Commissioner, shall become a part of this agreement and shall govern the allocation of production of Unitized Substances until the effective date of a new schedule approved by the Land Commissioner.

SECTION 14. ALLOCATION OF UNITIZED SUBSTANCES. All Unitized Substances produced and saved from the committed tracts within the Unit Area (less, save and except any part of such Unitized Substances used in conformity with good operating practices on Unitized Land for drilling, operating, camp, and other production or development purposes and for pressure maintenance or unavoidable loss) shall be apportioned among and allocated to the committed tracts within the Unit Area in accordance with the respective tract participation effective hereunder during the respective periods such Unitized Substances were produced, as set forth in the schedule of participation in Exhibit "B" or any revision thereof. The amount of Unitized Substances so allocated to each tract, and only that amount (regardless of whether it be more or less than the amount of the actual production of Unitized Substances from the well or wells, if any, on such tract), shall for all intents and purposes be deemed to have been produced from such tract.

The Unitized Substances allocated to each tract shall be distributed among, or accounted for to, the parties executing, consenting to or ratifying this agreement entitled to share in the production from such tract in the same manner, in the same proportions and upon the same conditions as they would have participated and shared in the production from such tract had this agreement not been entered into and with the same legal force and effect.

No tract committed to this agreement and qualified for participation as above provided shall be subsequently excluded from participation hereunder on account of depletion of Unitized Substances, and nothing herein contained shall be construed as requiring any retroactive adjustment for production obtained prior to the effective date of the joinder of any tract.

If the Working Interest or the Royalty Interest in any tract are divided with respect to separate parcels or portions of such tract and owned severally by different persons, the percentage participation assigned to such tract shall, in the absence of a recordable instrument executed by all owners and furnished to Unit Operator fixing the divisions of ownership, be divided among such parcels or portions in proportion to the number of surface acres in each.

The Unitized Substances allocated to each tract shall be delivered in kind to the respective Working Interest Owners and parties entitled thereto by virtue of the ownership of oil and gas rights therein or by purchase from such owners. Each Working Interest Owner and the parties entitled thereto shall have the continuing right to receive such production in kind at a common point within the

Unit Area and to sell or dispose of the same as it sees fit. Each such party shall have the right to construct, maintain and operate all necessary facilities for that purpose on Unitized Land, provided the same are so constructed, maintained and operated as not to interfere with operation carried on pursuant hereto, Subject to Section 15 hereof, any extra expenditure incurred by Unit Operator by reason of the delivery in kind of any portion of the Unitized Substances shall be borne by the party receiving the same in kind. In the event any party hereto shall fail to take or otherwise adequately dispose of its proportionate share of the production from the Unit Area currently, as and when produce, then so long as such conditions continue, Unit Operator, for the account and at the expense of such party and in order to avoid curtailing the operation of the Unit Area, may sell or otherwise dispose of such production to itself or others on a day-to-day basis at not less than the prevailing market price in the area for like production, and the account of such party shall be charged therewith as having received such production. The net proceeds, if any, of the Unitized Substances so disposed of by Unit Operator shall be paid to the party entitled thereto. Notwithstanding the foregoing, Unit Operator shall not make a sale into interstate commerce of any other party's share of gas production without first giving such other party sixty (60) days notice of such intended sale.

Any party receiving in kind or separately disposing of all or any part of the Unitized Substances allocated to any tract, or receiving the proceeds therefrom if the same is sold or purchased by Unit Operator, shall be responsible for the payment of all royalty on the lease or leases and tracts contributed by it and received into the Unit, and each such party shall hold each other party hereto harmless against all claims, demands and causes of action for such royalty on the lease or leases and tracts contributed by it to the Unit Area.

If, after the effective date of this agreement, there is any tract or tracts that are subsequently committed hereto, as provided in Section 3 (Expansion) hereof, or any tract or tracts within the Unit Area not committed hereto as of the effective date hereof but which are subsequently committed hereto under the provisions of Section 29 (Nonjoinder and Subsequent Joinder), or if any tract is excluded from the Unit as provided for in Section 28 (Loss of Title), the schedule of participation as shown in Exhibit "B", subject to Section 12 (Tract Participation) or Section 29 (Nonjoinder and Subsequent Joinder) whichever is appropriate, shall be revised by the Unit Operator and distributed to the Working Interest Owners and the Land Commissioner, to show the new percentage participation of all the then effectively committed tracts; and the revised Exhibit "B", upon approval by the Land Commissioner, shall govern all the allocation of production from and after the effective date thereof until a new revised Exhibit "B" is filed and approved as hereinabove provided.

SECTION 15. ROYALTY SETTLEMENT. The State of New Mexico, all Royalty Owners who, under an existing contract, are entitled to take in kind a share of the substances produced from any tract unitized hereunder, shall continue to be entitled to such right to take in kind their share of the Unitized Substances allocated to such tract, and Unit Operator shall make deliveries of such Royalty share taken in kind in conformity with the applicable contracts, laws and regulations. Settlement for Royalty interest not taken in kind shall be made by Working Interest Owners responsible therefor under existing contracts, laws and regulations, on or before the last day of each month for Unitized Substances produced during the preceding calendar month; provided, however, that nothing herein contained shall operate to relieve the lessees of any land from their respective lease obligations for the payment of any royalty due under their leases, except that such royalty shall be computed in accordance with the terms of this Unit Agreement.

If gas obtained from lands not subject to this agreement is introduced into the Unitized Formation, for use in repressuring, stimulation of production or increasing ultimate recovery in conformity with a plan approved pursuant to Section 10 (Plan of Operations), a like amount of gas, less appropriate deductions for loss from any cause, may be withdrawn from the Unitized Formation, Royalty free as to dry gas but not as to the products extracted therefrom; provided such withdrawal shall be at such times as may be provided in the approved plan of operations or as otherwise may be consented to by the commissioner as conforming to good petroleum engineering practice; and provided further, that such right of withdrawal shall terminate on the termination date of this Unit Agreement.

All royalty due the State of New Mexico, and the other Royalty Owners hereunder shall be computed and paid in accordance with the terms of the leases on the basis of the Unitized Substances allocated to the respective tract or tracts committed hereto, in lieu of actual production from such tract or tracts.

Each Royalty Owner (other than the State of New Mexico) who ratifies this agreement represents and warrants that he is the owner of a Royalty Interest in a tract or tracts within the Unit Area as his interest appears in Exhibit "B" attached hereto. If any Royalty Interest in a tract or tracts should be lost by title failure or otherwise in whole or in part during the term of this agreement then the Royalty Interest of the party representing himself to be the owner thereof shall be reduced proportionately and the interest of all parties shall be adjusted accordingly.

SECTION 16. RENTAL SETTLEMENT. Rental due on leases committed hereto shall be paid by Working Interest Owners responsible therefor under existing contracts, laws and regulations; provided that nothing herein contained shall operate to relieve the lessees of any land from their respective lease obligations for the payment of any rental in lieu thereof, due under their leases. Rental for lands of the State of New Mexico subject to this agreement shall be paid at the rate specified in the respective leases from the State of New Mexico.

All rentals, if any due under any leases embracing lands other than the State of New Mexico, shall be paid by the respective lease owners in accordance with the terms of their leases and all royalties due under the terms of any such leases shall be paid on the basis of all unitized substances allocated to the respective leases committed hereto.

SECTION 17. CONSERVATION. Operations hereunder and production of Unitized Substances shall be conducted to provide for the most economical and efficient recovery of said substances without waste, as defined by or pursuant to State laws and regulations.

SECTION 18. DRAINAGE. The Unit Operator shall take appropriate and adequate measures to prevent drainage of Unitized Substances from Unitized Land by wells on land not subject to this agreement.

SECTION 19. LEASES AND CONTRACTS CONFORMED AND EXTENDED. The terms, conditions and provisions of all leases, subleases and other contracts relating to exploration, drilling, development or operation for oil or gas on lands committed to this agreement are hereby expressly modified and amended to the extent necessary to make the same conform to the provisions hereof, but otherwise to remain in full force and effect.

Without limiting the generality of the foregoing, all leases, subleases and contracts are particularly modified in accordance with the following:

(a) The development and operation of lands subject to this agreement under the terms hereof shall be deemed full performance of all obligations for development and operation with respect to each and every part or separately owned tract subject to this agreement, regardless of whether there is any development of any particular part or tract of the Unit Area, notwithstanding anything to the contrary in any lease, operating agreement or other contract by and between the parties hereto, or their respective predecessors in interest, or any of them.

(b) Drilling, producing or secondary recovery operations performed hereunder upon any tract of Unitized Lands shall be accepted and deemed to be performed upon and for the benefit of each and every tract Unitized Land, and no lease shall be deemed to expire by reason of failure to drill or produce wells situated on land therein embraced.

(c) Each lease, sublease, or contract relating to the exploration, drilling, development or operation for oil and gas which by its terms might expire prior to the termination of this agreement, is hereby extended beyond any such term so provided therein, so that it shall be continued in full force and effect for and during the term of this agreement.

(d) Termination of this agreement shall not affect any lease which, pursuant to the terms thereof or any applicable laws, shall continue in force and effect thereafter.

(e) Any lease embracing lands of the State of New Mexico, which is made subject to this agreement, shall continue in force beyond the term provided therein as to the lands committed hereto until the termination hereof.

(f) Any lease embracing lands of the State of New Mexico having only a portion of its land committed hereto, shall be segregated as to that portion committed and that portion not committed, and the terms of such lease shall apply separately to such segregated portions commencing as of the effective date hereof. Notwithstanding any of the provisions of this agreement to the contrary any lease embracing lands of the State of New Mexico having only a portion of its land committed hereto shall continue in full force and effect beyond the term provided therein as to all lands embraced in such lease (whether within or without the Unit Area), (1) if, and for so long as oil or gas are capable of being produced in paying quantities from some part of the lands embraced in such lease committed to this agreement; or (2) if, and for so long as some part of the lands embraced in such lease committed to this agreement are allocated Unitized Substances; or (3) if, at the expiration of the secondary term the leasee or the Unit Operator is then engaged in bonafide drilling or reworking operations on some part of the lands embraced therein and for so long as such operations are being diligently prosecuted, and if they result in the production of oil or gas said lease shall continue in full force and effect as to all the lands embraced therein so long thereafter as oil or gas in paying quantities is being produced from any portion of said lands.

SECTION 20 CORRECTION OF ERRORS. It is hereby agreed by all parties to this agreement that Unit Operator is empowered to correct any mathematical or clerical errors which may exist in the pertinent exhibits to this agreement; provided, however, that correction of any error other than mathematical or clerical shall be made by Unit Operator only after first having obtained approval of Working Interest Owners and the Land Commissioner.

SECTION 21. COVENANTS RUN WITH LAND. The covenants herein shall be construed to be covenants running with the land with respect to the interest of the parties hereto and their successors in interest until this agreement terminates, and any grant, transfer or conveyance of interest in land or leases subject hereto shall be and hereby is conditioned upon the assumption of all privileges and obligations hereunder by the grantee, transferee or other successor in interest. No assignment or transfer of any Working Interest subject hereto shall be binding upon Unit Operator until the first day of the calendar month after Unit Operator is furnished with the original, or an acceptable photostatic or certified copy of the recorded instrument of transfer; and no assignment or transfer of any Royalty Interest subject hereto shall be binding upon the Working Interest Owner responsible therefor until the first day of the calendar month after said Working Interest Owner is furnished with the original or an acceptable photostatic or certified copy of the recorded instrument of transfer.

SECTION 22 EFFECTIVE DATE. This agreement shall become binding upon each party who executes or ratifies it as of the date of execution or ratification by such party and shall become effective as of 7:00 o'clock A.M. on the first day of the calendar month next following:

(a) The execution or ratification of this agreement and the Unit Operating Agreement by Working Interest Owners owning a combined Unit Participation of at least 85%, and the execution or ratification of the agreement by Royalty Owners owning a combined interest of at least 65% of the Royalty Interest, in said Unit Area, and

(b) The approval of this agreement by the land Commissioner, and the Commission; and

(c) The filing of at least one counterpart of this agreement for record in the office of the County Clerk of Eddy County, New Mexico, by the Unit Operator.

If (a), (b), and (c) above are not accomplished on or before July 1, 1967 this agreement shall ipso facto expire on said date (hereinafter called "expiration date") and thereafter be of no further force or effect, unless prior thereto this agreement has been executed or ratified by Working Interest Owners owning a combined Unit Participation of at least 80% and the Working Interest Owners owning a combined Unit Participation of at least 80% committed to this agreement have decided to extend said expiration date for a period not to exceed six months (hereinafter called "extended expiration date"). If said expiration date is so extended and (a), (b) and (c) are not accomplished on or before said extended expiration date, this agreement shall ipso facto expire on said extended expiration date and thereafter be of no further force or effect.

Unit Operator shall, within thirty (30) days after the effective date of this agreement, file for record in the office where a counterpart of this agreement is recorded, a certificate to the effect that this agreement has become effective according to its terms and stating further the effective date.

SECTION 23. TERM. The term of this agreement shall be for the time that Unitized Substances are produced in quantities sufficient to pay for the cost of producing same and as long thereafter as Unit Operations are conducted without a cessation of more than sixty (60) consecutive days, unless sooner terminated by Working Interest Owners in the provided manner in the next paragraph. Termination under this paragraph shall be effective as of the first day of the month after the Unit Operator determines, on confirmatory data satisfactory to the Land Commissioner, that the unit is no longer paying.

This agreement may be terminated at any time by Working Interest Owners having a combined Unit Participation of at least ninety percent (90%). Notice of termination shall be given to all parties and filed with the Land Commissioner, and the Commission and filed for record with the County Clerk of Eddy County, New Mexico.

Upon termination of this agreement the further development and operation of the Unit Area as a unit shall be abandoned, Unit Operations shall cease, and thereafter the parties hereto shall be governed by the terms and provisions of the leases and contracts affecting the separate tracts just as if this agreement had never been entered into.

If not otherwise covered by the leases unitized under this agreement, Royalty Owners hereby grant Working Interest Owners a period of six (6) months after termination of this agreement in which to salvage, sell, distribute or otherwise dispose of the personal property and facilities used in connection with Unit Operations.

SECTION 24. APPEARANCES. Unit Operator shall have the right to appear for or on behalf of any and all interests affected hereby before the Land Commissioner, and the Commission, and to appeal from any order issued under the rules regulations of the Land Commissioner or the Commission, or to apply for relief from any of said rules and regulations or in any proceedings relative to operations before the Land Commissioner or the Commission, or any other legally constituted authority; provided, however, the affected Working Interest Owner or Owners shall approve such appearance; provided, further, that any other interested party shall also have the right at his or its own expense to be heard in any such proceeding.

SECTION 25. NOTICES. All notices, demands, objections or statements required hereunder to be given or rendered to the parties hereto shall be deemed fully given if made in writing and personally delivered to the party or parties or sent by postpaid certified mail addressed to such party or parties at their respective addresses set forth in connection with the signatures hereto or to the ratification or consent hereof or to such other address as any such party or parties may have furnished in writing to the party sending the notice, demand or statement.

SECTION 26. NO WAIVER OF CERTAIN RIGHTS. Nothing in this agreement contained shall be construed as a waiver by any party hereto of the right to assert any legal or constitutional right or defense as to the validity or invalidity of any Federal or State law or rule or regulation issued thereunder in any way affecting such party, or as a waiver by any such party or any right beyond his or its authority to waive.

SECTION 27. UNAVOIDABLE DELAY. All obligations under this agreement requiring the Unit Operator to commence or continue secondary recovery operations or to operate on or produce Unitized Substances from any of the land 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, acts of God, Federal, State or municipal law or agency, unavoidable accident, 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.

SECTION 28. LOSS OF TITLE. In the event title to any tract of Unitized Land shall fail so that the tract is no longer committed hereto or qualified for participation in the production of Unitized Substances under Section 13 of this agreement, and the true owner cannot be induced to join this Unit Agreement, such tract shall be no longer subject to this Unit Agreement effective as of the first day of the calendar month in which the failure of title is finally determined and there shall be readjustment of future costs and benefits and such revision of Exhibits "A" and "B" as may be required on account of the loss of such title. In the event of a dispute as to the title or right of any Royalty or Working Interest Owner the payment for (or deliver in kind of) Unitized Substances on account thereof may be withheld (or marketed and the proceeds impounded) without liability for interest until the dispute is finally settled; provided, that as to State land or leases, no payments of funds due the State of New Mexico shall be withheld but such funds shall be deposited as directed by the Land Commissioner to be held as unearned money pending final settlement of the title dispute and then applied as earned or returned in accordance with such final settlement.

Unit Operator as such is relieved from any responsibility for any defect or failure of any title hereunder.

SECTION 29. NONJOINER AND SUBSEQUENT JOINER. If the owner of any substantial interest in a tract within the Unit Area fails or refused to subscribe, ratify, or consent in writing to this Agreement, the Working Interest Owner in that tract who has executed or ratified this Agreement may withdraw said tract from this Agreement by written notice to the Land Commissioner, and Unit Operator prior to the effective date of this Agreement. Joinder by any Royalty Owner at any time must be accompanied by appropriate joinder of the corresponding Working Interest Owner in order for the interest of such Royalty Owner to be regarded as effectively committed. Joinder of the Unit Agreement by a Working Interest Owner at any time must be accompanied by appropriate joinder to the Unit Operating Agreement in order for such interest to be regarded as effectively committed to this Unit Agreement.

Any oil or gas interest in the lands in the Unit Area not committed hereto prior to submission of this Agreement to the Land Commissioner for final approval may thereafter be committed hereto upon compliance with the applicable provisions of this Section and of Section 13 (Tracts Qualified for Unit Participation) hereof, at any time up to the effective date hereof and for a period to and including six (6) months thereafter, on the same basis of participation as provided in said Section 13, by the owner or owners thereof subscribing, ratifying or consenting in writing to this Agreement and, if the interest is a Working Interest, by the owner of such interest subscribing also to the Unit Operating Agreement.

It is understood and agreed, however, that from and after said six months after the effective date hereof the right of subsequent joinder as provided in this Section shall be subject to such requirements or approvals and on such basis as may be agreed upon by ninety (90%) of the Working Interest Owners (based upon percentage participation in the Unit Area). Such joinder by a proposed Working Interest Owner must be evidenced by his execution or ratification of this Agreement and the Unit Operating Agreement. Such joinder by a proposed Royalty Owner must be evidenced by his execution, ratification or consent of this Agreement and must be consented to in writing by the Working Interest Owner responsible for the payment of any benefits that may accrue hereunder in behalf of such proposed Royalty Owner. Except as may be otherwise herein provided, subsequent joinder to this Agreement shall be effective at 7:00 A.M. as of the first day of the month following the approval by the Commissioner of duly executed counterparts of any and all documents necessary to establish effective commitment of any tract or interest to this Agreement, unless objection to such joinder by the Land Commissioner is duly made within sixty (60) days after such filing.

IN WITNESS WHEREOF, the parties hereto have caused this agreement to be executed and have set opposite their respective names the dates of execution.

Date: _____

R. R. Hensel
H & S OIL COMPANY, UNIT OPERATOR

STATE OF NEW MEXICO)
 : ss.
COUNTY OF EDDY)

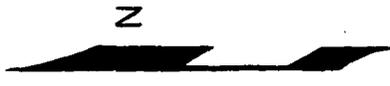
The foregoing instrument was acknowledged before me this _____ day of _____, 1967, by _____.

My commission expires: _____

Notary Public

R-28-E

T-18-S



9

H AND S
OIL COMPANY

WEST ARTESIA GRAYBURG UNIT

EXHIBIT 'A'

PROPOSED UNITIZED AREA

UNIT TRACT NUMBER

E-11000 LEASE NUMBER

ADMINS. ST. 17

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