

A.A.P.L. FORM 610  
MODEL FORM OPERATING AGREEMENT—1956  
Non-Federal Lands

OPERATING AGREEMENT

DATED

April 1st, \_\_\_\_\_, 1970,

FOR UNIT AREA IN TOWNSHIP 21 South, RANGE 25 East, N.M.P.M.,

Eddy COUNTY, STATE OF New Mexico.

AMERICAN ASSOCIATION OF PETROLEUM LANDMEN  
APPROVED FORM. A.A.P.L. NO. 610  
MAY BE ORDERED DIRECTLY FROM THE PUBLISHER  
ROSS-MARTIN COMPANY, BOX 800, TULSA 74101

EXHIBIT "A"

NEW MEXICO  
OIL CONSERVATION DIVISION

MOC EXHIBIT 3  
CASE NO. 11723 (de novo)

## TABLE OF CONTENTS

Paragraph Number	Title	Page
1.	Definitions .....	1
2.	Title Examination, Loss of Leases and Oil and Gas Interests .....	1
3.	Unleased Oil and Gas Interests .....	2
4.	Interests of Parties .....	2
5.	Operator of Unit .....	3
6.	Employees .....	3
7.	Test Well .....	3
8.	Costs and Expenses .....	3
9.	Operator's Lien .....	4
10.	Term of Agreement .....	4
11.	Limitation on Expenditures .....	4
12.	Operations by Less Than All Parties .....	5
13.	Right to Take Production in Kind .....	6
14.	Access to Unit Area .....	7
15.	Drilling Contracts .....	7
16.	Abandonment of Wells .....	7
17.	Delay Rentals and Shut-in Well Payments .....	8
18.	Preferential Right to Purchase .....	8
19.	Selection of New Operator .....	8
20.	Maintenance of Unit Ownership .....	9
21.	Resignation of Operator .....	9
22.	Liability of Parties .....	9
23.	Renewal or Extension of Leases .....	9
24.	Surrender of Leases .....	10
25.	Acreage or Cash Contributions .....	10
26.	Provision Concerning Taxation .....	10
27.	Insurance .....	11
28.	Claims and Lawsuits .....	11
29.	Force Majeure .....	11
30.	Notices .....	11
31.	Other Conditions .....	12

OPERATING AGREEMENT

THIS AGREEMENT, entered into this 1st day of April, 1970, between  
Monsanto Company

hereafter designated as "Operator", and the signatory parties other than Operator.

WITNESSETH, THAT:

WHEREAS, the parties to this agreement are owners of oil and gas leases covering and, if so indicated, unleased mineral interests in the tracts of land described in Exhibit "A", and all parties have reached an agreement to explore and develop these leases and interests for oil and gas to the extent and as hereinafter provided;

NOW, THEREFORE, it is agreed as follows:

1. DEFINITIONS

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

- (1) The words "party" and "parties" shall always mean a party, or parties, to this agreement.
- (2) The parties to this agreement shall always be referred to as "it" or "they", whether the parties be corporate bodies, partnerships, associations, or persons real.
- (3) The term "oil and gas" shall include oil, gas, casinghead gas, gas condensate, and all other liquid or gaseous hydrocarbons, unless an intent to limit the inclusiveness of this term is specifically stated.
- (4) The term "oil and gas interests" shall mean unleased fee and mineral interests in tracts of land lying within the Unit Area which are owned by parties to this agreement.
- (5) The term "Unit Area" shall refer to and include all of the lands, oil and gas leasehold interests and oil and gas interests intended to be developed and operated for oil and gas purposes under this agreement. Such lands, oil and gas leasehold interests and oil and gas interests are described in Exhibit "A".
- (6) The term "drilling unit" shall mean the area fixed for the drilling of one well by order or rule of any state or federal body having authority. If a drilling unit is not fixed by any such rule or order, a drilling unit shall be the drilling unit as established by the pattern of drilling in the Unit Area or as fixed by express agreement of the parties.
- (7) All exhibits attached to this agreement are made a part of the contract as fully as though copied in full in the contract.
- (8) The words "equipment" and "materials" as used here are synonymous and shall mean and include all oil field supplies and personal property acquired for use in the Unit Area.

2. TITLE EXAMINATION, LOSS OF LEASES AND OIL AND GAS INTERESTS

~~A. Title Examination:~~

~~There shall be no examination of title to leases, or to oil and gas interests, except that title to the lease covering the land upon which the exploratory well is to be drilled in accordance with Section 7, shall be examined on a complete abstract record by Operator's attorney, and the title to both the oil and gas lease and to the fee title of the lessors must be approved by the examining attorney, and accepted by all parties. A copy of the examining attorney's opinion shall be sent to each party immediately after the opinion is written, and, also, each party shall be given, as they are written, a copy of all subsequent supplemental attorney's reports. A good faith effort to satisfy the examining attorney's requirements shall be made by the party owning the lease covering the drillsite.~~

~~If title to the proposed drillsite is not approved by the examining attorney or the lease is not acceptable for a material reason, and all the parties do not accept the title, the parties shall select a new drillsite for the first exploratory well; provided, if the parties are unable to agree upon another drillsite, this agreement shall, in that case, come to an end and all parties shall then forfeit their rights and be relieved of obligations hereunder. If a new drillsite is selected, title to the oil and gas lease covering it and to the fee title of the lessor shall be examined, and title shall be approved or accepted or rejected in like manner as provided above concerning the drillsite first selected. If title to the oil and gas lease covering the second choice drillsite is not approved or accepted, other drillsites shall be successively selected and title examined, until a drillsite is chosen~~

42

~~to which title is approved or accepted, or until the parties fail to select another drillsite. As in the case of the drillsite first selected, so also with successive choices if the time comes that the parties have not approved title and are unable to agree upon an alternate drillsite, the contract shall, in that case and at that time, come to an end and all parties shall forfeit their rights and be relieved of obligations under this contract.~~

~~No well other than the first test shall be drilled in the Unit Area until after (1) the title to the lease covering the lands upon which such well is to be located has been examined by Operator's attorney, and (2) the title has been approved by the examining attorney and the title has been accepted by all of the parties who are to participate in the drilling of the well.~~

**B. Failure of Title:**

Should any oil and gas lease, or interest therein, be lost through failure of title, this agreement shall, nevertheless, continue in force as to all remaining leases and interests, and

- (1) The party whose lease or interest is affected by the title failure shall bear alone the entire loss and it shall not be entitled to recover from Operator or the other parties any development or operating costs which it may have theretofore paid, but there shall be no monetary liability on its part to the other parties hereto by reason of such title failure; and
- (2) There shall be no retroactive adjustment of expenses incurred or revenues received from the operation of the interest which has been lost, but the interests of the parties shall be revised on an acreage basis, as of the time it is determined finally that title failure has occurred, so that the interest of the party whose lease or interest is affected by the title failure will thereafter be reduced in the Unit Area by the amount of the interest lost; and
- (3) If the proportionate interests of the other parties hereto in any producing well theretofore drilled on the Unit Area is increased by reason of the title failure, the party whose title has failed shall receive the proceeds attributable to the increase in such interests (less operating costs attributable thereto) until it has been reimbursed for unrecovered costs paid by it in connection with such well; and
- (4) Should any person not a party to this agreement, who is determined to be the owner of any interest in the title which has failed, pay in any manner any part of the cost of operation, development, or equipment, or equipment previously paid under this agreement, such amount shall be proportionately paid to the party or parties hereto who in the first instance paid the costs which are so refunded; and
- (5) Any liability to account to a third party for prior production of oil and gas which arises by reason of title failure shall be borne by the party or parties whose title failed in the same proportions in which they shared in such prior production.

**C. Loss of Leases for Causes Other Than Title Failure:**

If any lease or interest subject to this agreement be lost through failure to develop or because express or implied covenants have not been performed, or if any lease be permitted to expire at the end of its primary term and not be renewed or extended, or if any lease or interest therein is lost due to the fact that the production therefrom is shut in by reason of lack of market, the loss shall not be considered a failure of title and all such losses shall be joint losses and shall be borne by all parties in proportion to their interests and there shall be no readjustment of interests in the Unit Area.

~~**S. UNLEASED OIL AND GAS INTERESTS**~~

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

**4. INTERESTS OF PARTIES (See Article 31 (E) )**

Exhibit "A" lists all of the parties, and their respective percentage or fractional interests under this agreement. Unless changed by other provisions, all costs and liabilities incurred in operations under this contract shall be borne and paid, and all equipment and material acquired in operations on the Unit Area shall be owned, by the parties as their interests are given in Exhibit "A". All production of oil and gas from the Unit Area, subject to the payment of lessor's royalties, shall also be owned by the parties in the same manner.

~~If the interest of any party in any oil and gas lease covered by this agreement is subject to an overriding royalty, production payment, or other charge over and above the usual one-eighth (1/8) royalty, such party shall assume and alone bear all such excess obligations and shall account for them to the owners thereof out of its share of the working interest production of the Unit Area.~~

5. OPERATOR OF UNIT

Monsanto Company shall be the Operator of the Unit Area, and shall conduct and direct and have full control of all operations on the Unit Area as permitted and required by, and within the limits of, this agreement. It shall conduct all such operations in a good and workmanlike manner, but it shall have no liability as Operator to the other parties for losses sustained, or liabilities incurred, except such as may result from gross negligence or from breach of the provisions of this agreement.

6. EMPLOYEES

The number of employees and their selection, and the hours of labor and the compensation for services performed, shall be determined by Operator. All employees shall be the employees of Operator.

7. TEST WELL

On or before the 15th day of June, 19 70, Operator shall commence the drilling of a well for oil and gas in the following location:

Lot 28, Section 1, T-21-S, R-25-E, Eddy County, New Mexico at a location approximately 3630' from the south line and 990' from the east line of said Section 1,

and shall thereafter continue the drilling of the well with due diligence to a subsurface depth of 10,400 feet or to the top of the Barnett shale, whichever is the lesser; with the option to drill said Test Well to a subsurface depth of 11,300 feet, or to a depth sufficient to recover fluid from the Devonian formation whichever is the lesser;

unless granite or other practically impenetrable substance is encountered at a lesser depth or unless all parties agree to complete the well at a lesser depth.

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

If in Operator's judgment the well will not produce oil or gas in paying quantities, and it wishes to plug and abandon the test as a dry hole, it shall first secure the consent of all parties to the plugging, and the well shall then be plugged and abandoned as promptly as possible.

8. COSTS AND EXPENSES

Except as herein otherwise specifically provided, Operator shall promptly pay and discharge all costs and expenses incurred in the development and operation of the Unit Area pursuant to this agreement and shall charge each of the parties hereto with their respective proportionate shares upon the cost and expense basis provided in the Accounting Procedure attached hereto and marked Exhibit "C". If any provision of Exhibit "C" should be inconsistent with any provision contained in the body of this agreement, the provisions in the body of this agreement shall prevail.

Operator, at its election, shall have the right from time to time to demand and receive from the other parties payment in advance of their respective shares of the estimated amount of the costs to be incurred in operations hereunder during the next succeeding month, which right may be exercised only by submission to each such party of an itemized statement of such estimated costs, together with an invoice for its share thereof. Each such statement and invoice for the payment in advance of estimated costs shall be submitted on or before the 20th day of the next preceding month. Each party shall pay to Operator its proportionate share of such estimate within fifteen (15) days after such estimate and invoice is received. If any party fails to pay its share of said estimate within said time, the amount due shall bear interest at the rate of ~~six percent (6%)~~ <sup>eight percent (8%)</sup> per annum until paid. Proper adjustment shall be made monthly between advances and actual cost, to the end that each party shall bear and pay its proportionate share of actual costs incurred, and no more.

### 9. OPERATOR'S LIEN

Operator is given a first and preferred lien on the interest of each party covered by this contract, and in each party's interest in oil and gas produced and the proceeds thereof, and upon each party's interest in material and equipment, to secure the payment of all sums due from each such party to Operator.

In the event any party fails to pay any amount owing by it to Operator as its share of such costs and expense or such advance estimate within the time limited for payment thereof, Operator, without prejudice to other existing remedies, is authorized, at its election, to collect from the purchaser or purchasers of oil or gas, the proceeds accruing to the working interest or interests in the Unit Area of the delinquent party up to the amount owing by such party, and each purchaser of oil or gas is authorized to rely upon Operator's statement as to the amount owing by such party.

In the event of the neglect or failure of any non-operating party to promptly pay its proportionate part of the cost and expense of development and operation when due, the other non-operating parties and Operator, within thirty (30) days after the rendition of statements therefor by Operator, shall proportionately contribute to the payment of such delinquent indebtedness and the non-operating parties so contributing shall be entitled to the same lien rights as are granted to Operator in this section. Upon the payment by such delinquent or defaulting party to Operator of any amount or amounts on such delinquent indebtedness, or upon any recovery on behalf of the non-operating parties under the lien conferred above, the amount or amounts so paid or recovered shall be distributed and paid by Operator to the other non-operating parties and Operator proportionately in accordance with the contributions theretofore made by them.

### 10. TERM OF AGREEMENT

This agreement shall remain in full force and effect for as long as any of the oil and gas leases subjected to this agreement remain or are continued in force as to any part of the Unit Area, whether by production, extension, renewal or otherwise; provided, however, that in the event the first well drilled hereunder results in a dry hole and no other well is producing oil or gas in paying quantities from the Unit Area, then at the end of ninety (90) days after abandonment of the first test well, this agreement shall terminate unless one or more of the parties are then engaged in drilling a well or wells pursuant to Section 12 hereof, or all parties have agreed to drill an additional well or wells under this agreement, in which event this agreement shall continue in force until such well or wells shall have been drilled and completed. If production results therefrom this agreement shall continue in force thereafter as if said first test well had been productive in paying quantities, but if production in paying quantities does not result therefrom this agreement shall terminate at the end of ninety (90) days after abandonment of such well or wells. It is agreed, however, that the termination of this agreement shall not relieve any party hereto from any liability which has accrued or attached prior to the date of such termination.

### 11. LIMITATION ON EXPENDITURES

Without the consent of all parties: (a) No well shall be drilled on the Unit Area except any well expressly provided for in this agreement and except any well drilled pursuant to the provisions of Section 12 of this agreement, it being understood that the consent to the drilling of a well shall include consent to all necessary expenditures in the drilling, testing, completing, and equipping of the well, including necessary tankage; (b) No well shall be reworked, plugged back or deepened except a well reworked, plugged back or deepened pursuant to the provisions of Section 12 of this agreement, it being understood that the consent to the reworking, plugging back or deepening of a well shall include consent to all necessary expenditures in conducting such operations and completing and equipping of said well to produce, including necessary tankage; (c) Operator shall not undertake any single project reasonably estimated to require an expenditure in excess of Five Thousand and no/100 Dollars (\$ 5,000.00 ) except in connection with a well the drilling, reworking, deepening, or plugging back of which has been previously authorized by or pursuant to this agreement; provided, however, that in case of explosion, fire, flood, or other sudden emergency, whether of the same or different nature, Operator may take such steps and incur such expenses as in its opinion are required to deal with the emergency and to safeguard life and property, but Operator shall, as promptly as possible, report the emergency to the other parties. Operator shall, upon request, furnish copies of its "Authority for Expenditures" for any single project costing in excess of \$ 2,500.00.

12. OPERATIONS BY LESS THAN ALL PARTIES

If all the parties cannot mutually agree upon the drilling of any well on the Unit Area other than the test well provided for in Section 7, or upon the <sup>completion of any well, or upon the</sup> reworking, deepening or plugging back of a dry hole drilled at the joint expense of all parties or a well jointly owned by all the parties and not then producing in paying quantities on the Unit Area, any party or parties wishing to drill, <sup>complete</sup> rework, deepen or plug back such a well may give the other parties written notice of the proposed operation, specifying the work to be performed, the location, proposed depth, objective formation and the estimated cost of the operation. The parties receiving such a notice shall have thirty (30) days (except as to <sup>completion attempts or</sup> reworking, plugging back or drilling deeper, where a drilling rig is on location, the period shall be limited to <sup>twenty-four (24)</sup> ~~six~~ hours exclusive of Saturday, ~~or~~ Sunday) <sup>or holidays</sup> after receipt of the notice within which to notify the parties wishing to do the work whether they elect to participate in the cost of the proposed operation. Failure of a party receiving such a notice to so reply to it within the period above fixed shall constitute an election by that party not to participate in the cost of the proposed operation.

If any party receiving such a notice elects not to participate in the proposed operation (such party or parties being hereafter referred to as "Non-Consenting Party"), then in order to be entitled to the benefits of this section, the party or parties giving the notice and such other parties as shall elect to participate in the operation (all such parties being hereafter referred to as the "Consenting Parties") shall, within thirty (30) days after the expiration of the notice period of thirty (30) days (or as promptly as possible after the expiration of the <sup>24 hour</sup> ~~six hour~~ period where the drilling rig is on location, as the case may be) actually commence work on the proposed operation and complete it with due diligence.

The entire cost and risk of conducting such operations shall be borne by the Consenting Parties in the proportions that their respective interests as shown in Exhibit "A" bear to the total interests of all Consenting Parties. Consenting Parties shall keep the leasehold estates involved in such operations free and clear of all liens and encumbrances of every kind created by or arising from the operations of the Consenting Parties. If such an operation results in a dry hole, the Consenting Parties shall plug and abandon the well at their sole cost, risk and expense. If any well drilled, reworked, deepened, <sup>completed</sup> or plugged back under the provisions of this section results in a producer of oil and/or gas in paying quantities, the Consenting Parties shall complete and equip the well to produce at their sole cost and risk, and the well shall then be turned over to Operator and shall be operated by it at the expense and for the account of the Consenting Parties. Upon commencement of operations for the drilling, reworking, deepening, <sup>completing</sup> or plugging back of any such well by Consenting Parties in accordance with the provisions of this section, each Non-Consenting Party shall be deemed to have relinquished to Consenting Parties, and the Consenting Parties shall own and be entitled to receive, in proportion to their respective interests, all of such Non-Consenting Party's interest in the well, its leasehold operating rights, and share of production therefrom until the proceeds or market value thereof (after deducting production taxes, royalty, overriding royalty, <sup>and other interests payable out of or measured by the production</sup> ~~and other interests payable out of or measured by the production~~ <sup>except those additional burdens described in Article 31</sup> from such well accruing with respect to such interest until it reverts) shall equal the total of the following: par her

- (A) 100% of each such Non-Consenting Party's share of the cost of any newly acquired surface equipment beyond the wellhead connections (including, but not limited to, stock tanks, separators, treaters, pumping equipment and piping), plus 100% of each such Non-Consenting Party's share of the cost of operation of the well commencing with first production and continuing until each such Non-Consenting Party's relinquished interest shall revert to it under other provisions of this section, it being agreed that each Non-Consenting Party's share of such costs and equipment will be that interest which would have been chargeable to each Non-Consenting Party had it participated in the well from the beginning of the operation; and
- (B) 200% of that portion of the costs and expenses of drilling, <sup>completing</sup> reworking, deepening or plugging back, testing and completing, after deducting any cash contributions received under Section 25, and 200% of that portion of the cost of newly acquired equipment in the well (to and including the wellhead connections), which would have been chargeable to such Non-Consenting Party if it had participated therein.

*4/6*

In the case of any reworking, plugging back <sup>completing</sup> or deeper drilling operation, the Consenting Parties shall be permitted to use, free of cost, all casing, tubing and other equipment in the well, but the ownership of all such equipment shall remain unchanged; and upon abandonment of a well after such reworking, plugging back <sup>completing</sup> or deeper drilling, the Consenting Parties shall account for all such equipment to the owners thereof, with each party receiving its proportionate part in kind or in value.

Within sixty (60) days after the completion of any operation under this section, the party conducting the operations for the Consenting Parties shall furnish each Non-Consenting Party with an inventory of the equipment in and connected to the well, and an itemized statement of the cost of drilling, deepening, plugging back, testing, completing, and equipping the well for production; or, at its option, the operating party, in lieu of an itemized statement of such costs of operation, may submit a detailed statement of monthly billings. Each month thereafter, during the time the Consenting Parties are being reimbursed as provided above, the Consenting Parties shall furnish the Non-Consenting Parties with an itemized statement of all costs and liabilities incurred in the operation of the well, together with a statement of the quantity of oil and gas produced from it and the amount of proceeds realized from the sale of the well's working interest production during the preceding month. Any amount realized from the sale or other disposition of equipment newly acquired in connection with any such operation which would have been owned by a Non-Consenting Party had it participated therein shall be credited against the total unreturned costs of the work done and of the equipment purchased, in determining when the interest of such Non-Consenting Party shall revert to it as above provided; if there is a credit balance it shall be paid to such Non-Consenting Party.

If and when the Consenting Parties recover from a Non-Consenting Party's relinquished interest the amounts provided for above, the relinquished interests of such Non-Consenting Party shall automatically revert to it and from and after such reversion such Non-Consenting Party shall own the same interest in such well, the operating rights and working interest therein, the material and equipment in or pertaining thereto, and the production therefrom as such Non-Consenting Party would have owned had it participated in the drilling, reworking, deepening <sup>completing</sup> or plugging back of said well. Thereafter, such Non-Consenting Party shall be charged with and shall pay its proportionate part of the further costs of the operation of said well in accordance with the terms of this agreement and the accounting procedure schedule, Exhibit "C", attached hereto.

Notwithstanding the provisions of this Section 12, it is agreed that without the mutual consent of all parties, no wells shall be completed in or produced from a source of supply from which a well located elsewhere on the Unit Area is producing, unless such well conforms to the then-existing well spacing pattern for such source of supply.

The provisions of this section shall have no application whatsoever to the drilling of the initial test well on the Unit Area as provided for in Section 7 hereof, but shall apply to the completion, reworking, deepening, or plugging back of the said test well after it has been drilled to the point of running production casing, and to all other wells drilled, reworked, deepened, or plugged back, or proposed to be drilled, reworked, deepened, or plugged back, upon the Unit Area subsequent to the drilling of the said test well referred to in Section 7 hereof.

### 13. RIGHT TO TAKE PRODUCTION IN KIND

Each party shall take in kind or separately dispose of its proportionate share of all oil and gas produced from the Unit Area, exclusive of production which may be used in development and producing operations and in preparing and treating oil for marketing purposes and production unavoidably lost. <sup>Operator</sup> without liability other than the exercise of reasonable diligence, shall upon request ~~shall~~ pay or deliver, or cause to be paid or delivered, all royalties, overriding royalties, or other payments of any non-operator identified on Exhibit "A" that may become due on ~~his~~ share of such production, and shall hold the ~~other parties~~ <sup>other non-operators</sup> free from any liability therefor. Any <sup>such non-operator's</sup> extra expenditure incurred in the taking in kind or separate disposition by any party of its proportionate share of the production shall be borne by such party.

Each party shall execute all division orders and contracts of sale pertaining to its interest in production from the Unit Area, and shall be entitled to receive payment direct from the purchaser or purchasers thereof for its share of all production.

In the event any party shall fail to make the arrangements necessary to take in kind or separately dispose of its proportionate share of the oil and gas produced from the Unit Area, Operator shall have the right, subject to revocation at will by the party owning it, but not the obligation, to purchase such oil and gas or sell it to others for the time being, at not less than the market price prevailing in the area, which shall in no event be less than the price which Operator receives for its portion of the oil and gas produced from the Unit Area. Any such purchase or sale by Operator shall be subject always to the right of the owner of the production to exercise at any time its right to take in kind, or separately dispose of, its share of all oil and gas not previously delivered to a purchaser. Notwithstanding the foregoing, Operator shall not make a sale into interstate commerce of any other party's share of gas production without first ~~obtaining the written consent of the other party.~~ obtaining the written consent of the other party.

#### 14. ACCESS TO UNIT AREA

Each party shall have access to the Unit Area at all reasonable times, at its sole risk, to inspect or observe operations, and shall have access at reasonable times to information pertaining to the development or operation thereof, including Operator's books and records relating thereto. Operator shall, upon request, furnish each of the other parties with copies of all drilling reports, well logs, tank tables, daily gauge and run tickets and reports of stock on hand at the first of each month, and shall make available samples of any cores or cuttings taken from any well drilled on the Unit Area.

#### 15. DRILLING CONTRACTS

All wells drilled on the Unit Area shall be drilled on a competitive contract basis at the usual rates prevailing in the area. Operator, if it so desires, may employ its own tools and equipment in the drilling of wells, but its charges therefor shall not exceed the prevailing rates in the field, and the rate of such charges shall be agreed upon by the parties in writing before drilling operations are commenced, and such work shall be performed by Operator under the same terms and conditions as shall be customary and usual in the field in contracts of independent contractors who are doing work of a similar nature.

#### 16. ABANDONMENT OF WELLS

No well, other than any well which has been drilled or reworked pursuant to Section 12 hereof for which the Consenting Parties have not been fully reimbursed as therein provided, which has been completed as a producer shall be plugged and abandoned without the consent of all parties; provided, however, if all parties do not agree to the abandonment of any well, those wishing to continue its operation shall tender to each of the other parties its proportionate share of the value of the well's salvable material and equipment, determined in accordance with the provisions of Exhibit "C", less the estimated cost of salvaging and the estimated cost of plugging and abandoning. Each abandoning party shall then assign to the non-abandoning parties, without warranty, express or implied, as to title or as to quantity, quality, or fitness for use of the equipment and material, all of its interest in the well and its equipment, together with its interest in the leasehold estate as to, but only as to, the interval or intervals of the formation or formations then open to production. The assignments so limited shall encompass the "drilling unit" upon which the well is located. The payments by, and the assignments to, the assignees shall be in a ratio based upon the relationship of their respective percentages of participation in the Unit Area to the aggregate of the percentages of participation in the Unit Area of all assignees. There shall be no readjustment of interest in the remaining portion of the Unit Area.

After the assignment, the assignors shall have no further responsibility, liability, or interest in the operation of or production from the well in the interval or intervals then open. Upon request of the assignees, Operator shall continue to operate the assigned well for the account of the non-abandoning parties at the rates and charges contemplated by this agreement, plus any additional cost and charges which may arise as the result of the separate ownership of the assigned well.

## 17. DELAY RENTALS AND SHUT-IN WELL PAYMENTS

Delay rentals/<sup>minimum royalties</sup> and shut-in well payments which may be required under the terms of any lease shall be paid by the party who has subjected such lease to this agreement, at its own expense. Proof of each payment shall be given to Operator at least ten (10) days prior to the rental or shut-in well payment date. Operator shall furnish similar proof to all other parties concerning payments it makes in connection with its leases. Any party may request, and shall be entitled to receive, proper evidence of all such payments. If, through mistake or oversight, any delay rental/<sup>minimum royalty</sup> or shut-in well payment is not paid or is erroneously paid, and as a result a lease or interest therein terminates, there shall be no monetary liability against the party who failed to make such payment. Unless the party who failed to pay a rental or shut-in well payment secures a new lease covering the same interest within ninety (90) days from the discovery of the failure to make proper payment, the interests of the parties shall be revised on an acreage basis effective as of the date of termination of the lease involved, and the party who failed to make proper payment will no longer be credited with an interest in the Unit Area on account of the ownership of the lease which has terminated. In the event the party who failed to pay the rental or the shut-in well payment shall not have been fully reimbursed, at the time of the loss, from the proceeds of the sale of oil and gas attributable to the lost interest, calculated on an acreage basis, for the development and operating costs theretofore paid on account of such interest, it shall be reimbursed for unrecovered actual costs theretofore paid by it (but not for its share of the cost of any dry hole previously drilled or wells previously abandoned) from so much of the following as is necessary to effect reimbursement:

- (1) Proceeds of oil and gas, less operating expenses, theretofore accrued to the credit of the lost interest, on an acreage basis, up to the amount of unrecovered costs;
- (2) proceeds, less operating expenses thereafter incurred attributable to the lost interest on an acreage basis, of that portion of oil and gas thereafter produced and marketed (excluding production from any wells thereafter drilled) which would, in the absence of such lease termination, be attributable to the lost interest on an acreage basis, up to the amount of unrecovered costs, the proceeds of said portion of the oil and gas to be contributed by the other parties in proportion to their respective interests; and
- (3) any moneys, up to the amount of unrecovered costs, that may be paid by any party who is, or becomes, the owner of the interest lost, for the privilege of participating in the Unit Area or becoming a party to this contract.

Operator shall attempt to notify all parties when a gas well is shut-in or returned to production, but assumes no liability whatsoever for failure to do so.

~~18. PREFERENTIAL RIGHT TO PURCHASE~~

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

## 19. SELECTION OF NEW OPERATOR

Should a sale be made by Operator of its rights and interests, the other parties shall have the right within sixty (60) days after the date of such sale, by majority vote in interest,\*to select a new Operator. If a new Operator is not so selected, the transferee of the present Operator shall assume the duties of and act as Operator. In either case, the retiring Operator shall continue to serve as Operator, and discharge its duties in that capacity under this agreement, until its successor Operator is selected and begins to function, but the present Operator shall not be obligated to continue the performance of its duties for more than 120 days after the sale of its rights and interests has been completed. (\*As set forth in Col. 5, page 3 of Exhibit "A"

## 20. MAINTENANCE OF UNIT OWNERSHIP

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

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

Every such sale, encumbrance, transfer or other disposition made by any party shall be made expressly subject to this agreement, and shall be made without prejudice to the rights of the other parties.

If at any time the interest of any party is divided among and owned by four or more co-owners, Operator may, at its discretion, require such co-owners to appoint a single trustee or agent with full authority to receive notices, approve expenditures, receive billings for and approve and pay such party's share of the joint expenses, and to deal generally with, and with power to bind, the co-owners of such party's interests within the scope of the operations embraced in this contract; however, all such co-owners shall enter into and execute all contracts or agreements for the disposition of their respective shares of the oil and gas produced from the Unit Area and they shall have the right to receive, separately, payment of the sale proceeds thereof.

## 21. RESIGNATION OF OPERATOR

Operator may resign from its duties and obligations as Operator at any time upon written notice of not less than ninety (90) days given to all other parties. In this case, all parties to this contract shall select by majority vote in interest,\*not in numbers, a new Operator who shall assume the responsibilities and duties, and have the rights, prescribed for Operator by this agreement. The retiring Operator shall deliver to its successor all records and information necessary to the discharge by the new Operator of its duties and obligations. (\*As set forth in Col. 5, Page 3 of Exhibit "A")

## 22. LIABILITY OF PARTIES

The liability of the parties shall be several, not joint or collective. Each party shall be responsible only for its obligations, and shall be liable only for its proportionate share of the costs of developing and operating the Unit Area. Accordingly, the lien granted by each party to Operator in Section 9 is given to secure only the debts of each severally. It is not the intention of the parties to create, nor shall this agreement be construed as creating, a mining or other partnership or association, or to render them liable as partners.

## 23. RENEWAL OR EXTENSION OF LEASES

If any party secures a renewal of any oil and gas lease subject to this contract, each and all of the other parties shall be notified promptly, and shall have the right to participate in the ownership of the renewal lease by paying to the party who acquired it their several proper proportionate shares of the acquisition cost, which shall be in proportion to the interests held at that time by the parties in the Unit Area.

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

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

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

The provisions in this section shall apply also and in like manner to extensions of oil and gas leases.

## 24. SURRENDER OF LEASES

The leases covered by this agreement, in so far as they embrace acreage in the Unit Area, shall not be surrendered in whole or in part unless all parties consent.

However, should any party desire to surrender its interest in any lease or in any portion thereof, and other parties not agree or consent, the party desiring to surrender shall assign, without express or implied warranty of title, all of its interest in such lease, or portion thereof, and any well, material and equipment which may be located thereon and any rights in production thereafter secured, to the parties not desiring to surrender it. Upon such assignment, the assigning party shall be relieved from all obligations thereafter accruing, but not theretofore accrued, with respect to the acreage assigned and the operation of any well thereon, and the assigning party shall have no further interest in the lease assigned and its equipment and production. The parties assignee shall pay to the party assignor the reasonable salvage value of the latter's interest in any wells and equipment on the assigned acreage, determined in accordance with the provisions of Exhibit "C", less the estimated cost of salvaging and the estimated cost of plugging and abandoning. If the assignment is in favor of more than one party, the assigned interest shall be shared by the parties assignee in the proportions that the interest of each bears to the interest of all parties assignee.

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

## 25. ACREAGE OR CASH CONTRIBUTIONS

If any party receives while this agreement is in force a contribution of cash toward the drilling of a well or any other operation on the Unit Area, such contribution shall be paid to the party who conducted the drilling or other operation and shall be applied by it against the cost of such drilling or other operation. If the contribution be in the form of acreage, the party to whom the contribution is made shall promptly execute an assignment of the acreage, without warranty of title, to all parties to this agreement in proportion to their interests in the Unit Area at that time, and such acreage shall become a part of the Unit Area and be governed by all the provisions of this contract. Each party shall promptly notify all other parties of all acreage or money contributions it may obtain in support of any well or any other operation on the Unit Area.

## 26. PROVISION CONCERNING TAXATION

Each of the parties hereto elects, under the authority of Section 761(a) of the Internal Revenue Code of 1954, to be excluded from the application of all of the provisions of Subchapter K of Chapter 1 of Subtitle A of the Internal Revenue Code of 1954. If the income tax laws of the state or states in which the property covered hereby is located contain, or may hereafter contain, provisions similar to those contained in the Subchapter of the Internal Revenue Code of 1954 above referred to under which a similar election is permitted, each of the parties agrees that such election shall be exercised. Each party authorizes and directs the Operator to execute such an election or elections on its behalf and to file the election with the proper governmental office or agency. If requested by the Operator so to do, each party agrees to execute and join in such an election.

Operator shall render for ad valorem taxation all property subject to this agreement which by law should be rendered for such taxes, and it shall pay all such taxes assessed thereon before they become delinquent. Operator shall bill all other parties for their proportionate share of all tax payments in the manner provided in Exhibit "C".

If any tax assessment is considered unreasonable by Operator, it may at its discretion protest such valuation within the time and manner prescribed by law, and prosecute the protest to a final determination, unless all parties agree to abandon the protest prior to final determination. When any such protested valuation shall have been finally determined, Operator shall pay the assessment for the joint account, together with interest and penalty accrued, and the total cost shall then be assessed against the parties, and be paid by them, as provided in Exhibit "C".

## 27. INSURANCE

At all times while operations are conducted hereunder, Operator shall comply with the Workmen's Compensation Law of the State where the operations are being conducted. Operator shall also carry or provide insurance for the benefit of the joint account of the parties as may be outlined in Exhibit "D" attached to and made a part hereof. Operator shall require all contractors engaged in work on or for the Unit Area to comply with the Workmen's Compensation Law of the State where the operations are being conducted and to maintain such other insurance as Operator may require.

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

## 28. CLAIMS AND LAWSUITS

If any party to this contract is sued on an alleged cause of action arising out of operations on the Unit Area, or on an alleged cause of action involving title to any lease or oil and gas interest subjected to this contract, it shall give prompt written notice of the suit to the Operator and all other parties.

The defense of lawsuits shall be under the general direction of a committee of lawyers representing the parties, with Operator's attorney as Chairman. Suits may be settled during litigation only with the joint consent of all parties. No charge shall be made for services performed by the staff attorneys for any of the parties, but otherwise all expenses incurred in the defense of suits, together with the amount paid to discharge any final judgment, shall be considered costs of operation and shall be charged to and paid by all parties in proportion to their then interests in the Unit Area. Attorneys, other than staff attorneys for the parties, shall be employed in lawsuits involving Unit Area operations only with the consent of all parties; if outside counsel is employed, their fees and expenses shall be considered Unit Area expense and shall be paid by Operator and charged to all of the parties in proportion to their then interests in the Unit Area. The provisions of this paragraph shall not be applied in any instance where the loss which may result from the suit is treated as an individual loss rather than a joint loss under prior provisions of this agreement, and all such suits shall be handled by and be the sole responsibility of the party or parties concerned.

Damage claims caused by and arising out of operations on the Unit Area, conducted for the joint account of all parties, shall be handled by Operator and its attorneys, the settlement of claims of this kind shall be within the discretion of Operator so long as the amount paid in settlement of any one claim does not exceed one thousand (\$1000.00) dollars and, if settled, the sums paid in settlement shall be charged as expense to and be paid by all parties in proportion to their then interests in the Unit Area.

## 29. FORCE MAJEURE

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

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

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

## 30. NOTICES

All notices authorized or required between the parties, and required by any of the provisions of this agreement, shall, unless otherwise specifically provided, be given in writing by United States mail or Western Union Telegram, postage or charges prepaid, and addressed to the party to whom the notice is given at the

52

addresses listed on Exhibit "A". The originating notice to be given under any provision hereof shall be deemed given only when received by the party to whom such notice is directed and the time for such party to give any notice in response thereto shall run from the date the originating notice is received. The second or any responsive notice shall be deemed given when deposited in the United States mail or with the Western Union Telegraph Company, with postage or charges prepaid. Each party shall have the right to change its address at any time, and from time to time, by giving written notice thereof to all other parties.

31. OTHER CONDITIONS, IF ANY, ARE:

(A) The following numbered articles have been deleted from this Operating Agreement prior to the execution of said agreement: Paragraph A of Article 2, Article 3, Paragraph 2 of Article 4 and Article 18.

(B) Prior to the commencement of any well on the Unit Area other than the well described in Article 7 hereof, Operator shall secure current abstracts of title and, at working-interest owners' request, will make them available to working-interest owners for title examination. Operator shall pay all costs incurred with respect to such abstracts, and each working-interest owner agrees to reimburse Operator for its proportionate share (which shall be that party's interest as set forth on Page 3, Column 5 of Exhibit "A" hereto) of such costs upon being invoiced therefor. No well shall be drilled on the Unit Area for the joint account until both Operator and each working-interest owner have approved title to the land upon which the well is to be drilled, provided, however, that should operations by one or more of the parties hereto be conducted under Article 12 of this Agreement, such approval need not be secured from these parties who elect not to participate in such operations.

As to the initial well described in Article 7 hereof, Operator shall secure current title materials and secure a title opinion. Title examination costs pertaining to said initial well shall be shared proportionately by the parties participating in the costs of drilling said initial well as may be mutually agreed upon.

(C) Supplemental to the provision of Article 7 hereof, if in the drilling of the Test Well and prior to the time such well has been drilled to one of the depths specified in Article 7 hereof, there shall be encountered a formation condition which is impossible or impracticable to penetrate by use of methods normally used by the industry, or mechanical difficulties are encountered which reasonably prevent the further drilling of such well, Operator shall have the option but not the obligation to drill a well in substitution therefore to satisfy the terms and conditions of this agreement. In the event Operator elects to drill such substitute well, the actual drilling thereof must be commenced within 30 days after abandonment of the Test Well. The substitute well must be drilled at a location of Operator's choice on the quarter-quarter section described in Article 7 in connection with the Test Well and thereafter drilled with due diligence and in a good workmanlike manner to one of the depths provided for with respect to the Test Well. If the substitute well is so drilled, it will be treated for all purposes of this agreement as if it were the Test Well.

(D) After the initial Test Well drilled under Article 7 hereof has been drilled to a subsurface depth of 10,400 feet or to the top of the Barnett shale, Operator shall promptly give notice to the other parties who participated in the costs of drilling said well, of its election as to whether such well should be plugged and abandoned as a dry hole and that such well not be drilled deeper to a subsurface depth of 11,300 feet or to a depth sufficient to test the Devonian formation, or such well should be considered to be a dry hole down to its present depth and be drilled deeper to the aforesaid depth, or casing be set in an attempt to complete the well as a producer and said well not be drilled deeper to the aforesaid depth, or casing be set in an attempt to complete said well as a producer and said well be drilled deeper to the aforesaid depth. The other participating parties shall within twenty-four (24) hours (exclusive of Saturdays, Sundays or holidays) after receipt of the aforementioned notice from Operator, notify Operator of their election as herein provided. Failure of the other participating parties to so notify Operator within the above specified period of time shall be deemed concurrence with Operator's election. If one or more but less than all, of the participating parties elect either to set casing and attempt to complete the well or to deepen the well, the provision of Article 12 hereof shall apply to that portion of such operations thereafter conducted by less than all of the participating parties. If all of the participating parties elect to plug and abandon said well and not drill deeper, Operator shall plug and abandon same at the expense of all of the said participating parties.

(E) 1. There is attached hereto, made a part hereof and for purposes of identification marked Exhibit "A", a schedule showing the tracts of the parties hereto committed to this agreement and the gross acreage committed by the parties hereto as well as the beneficial interest of each of said parties after taking into consideration the contributions to be made in connection with the drilling of the initial test well. The beneficial interests of the respective parties hereto, as shown on Exhibit "A", have been determined as to each party on an adjusted surface acreage basis. The adjustment in surface area has been made by determining the fraction of the total unit area substances produced from or allocated to any tract which may be required to meet all royalties, overriding royalties, production payments or other obligations payable out of production from or allocated to such tract and multiplying that fraction by the number of acres contained in such tract and deducting the product from the total number of acres in said tract, the remainder being the adjusted surface acreage in each such tract. The beneficial interest of each party shown on Exhibit "A" represents the sum of the net acre interests of each party in all tracts committed to this Operating Agreement divided by the total number of net acres within the unit area.

2. All costs incurred in connection with drilling, completing and placing the initial test well on production, if it is completed as a well capable of producing oil and gas in paying quantities, or plugging and abandoning said well if it is completed as a dry hole (subject to the provisions of Article 31 (D)), shall be borne by Monsanto Company, David Fasken and Texaco Inc. (herein referred to as "participating parties"), in the proportions shown in Column 3 on page 3 of Exhibit "A" attached hereto. The other parties hereto are herein referred to as "non-participating parties."

3. The non-participating parties shall promptly and within 30 days after the completion of the initial test well as a well capable of producing oil and gas in paying quantities assign to Monsanto Company and David Fasken an undivided 1/2 interest in and to their respective leasehold interests committed to this Agreement. The non-participating parties shall reserve lease rights below 100 feet below the total depth drilled in the initial Test Well. In addition, Monsanto Company and David Fasken shall have the right to receive and own all of the interest of the non-participating parties in and to all oil and gas which may be produced, saved and marketed from the initial Test Well until said well has paid out with respect to such interests; provided, however, the non-participating parties shall be entitled to receive an overriding royalty in proportion to their respective beneficial interests of 1/16 of 8/8 of all of the oil and gas produced, saved and marketed from the initial Test Well until payout as hereinafter defined. The term "payout" as used herein shall be that period of time beginning with the date of first production from the initial Test Well and ending on that date on which the value of the gross production of oil and gas from said well attributable to the respective interests of the non-participating parties had they participated in the cost of said well, after deducting all royalty, production payments and overriding royalties including the overriding royalty to be paid to the non-participating parties and other lease burdens with which production may as of this date be encumbered and also after deducting their respective proportionate parts of all severance, ad valorem and production taxes (all in accordance with the accounting procedure attached to this Operating Agreement), shall equal the actual costs incurred by Monsanto Company and David Fasken attributable to the respective interests of the non-participating parties had they participated in the cost of drilling, testing, completing, equipping and operating the initial Test Well during the payout period. Effective as of 7:00 a.m. Mountain Standard Time on the date following that date upon which payout as to each of the non-participating parties has occurred each of the non-participating parties shall have the right and option to convert their respective overriding royalty interest into working interests equivalent to that shown in Column 6, page 3 of Exhibit "A". Operator shall give written notice to each non-participating party when the initial Test Well has paid out as defined herein and the non-participating parties shall have 15 days from the receipt of such notice within which to advise operator of their election with respect to the conversion of said overriding royalty interest to a working interest as herein provided. Should any non-participating party fail to advise Operator of such party's election, it shall be presumed that such party has elected to convert said overriding royalty interest to a working interest and such conversion shall be effective as of the time of payout of the initial Test Well. Upon the conversion of said overriding royalty interest to a working interest as herein provided, each of said parties shall own their proportionate parts of the equipment in and installed in connection with said well as shown in Column 5, page 3 of Exhibit "A", and shall thereafter bear their proportionate parts of the

operating costs as therein provided.

All operating costs incurred in connection with the initial Test Well until payout as herein provided shall be borne by Monsanto Company, David Fasken and Texaco Inc. in the same proportions as their participation in the cost of drilling and completing the initial Test Well as shown in Column 3 on page 3 of Exhibit "A".

Should the initial Test Well be completed as a producing well but is plugged and abandoned before payout as herein provided, the parties participating in the cost thereof shall have the right to salvage all equipment in and installed in connection with said well and to credit the salvage value thereof in proportion to their respective participating interests on the unrecovered portion of the cost of drilling, completing, plugging and abandoning said well.

4. For the purpose of computing and paying all obligations which are to be computed and paid under the terms of this Agreement and for the purpose of allocation of production under and pursuant to this Agreement insofar as the parties hereto are concerned, the acreage within the unit area shall be considered as if embraced within a single tract or lease with the right of the parties hereto to participate therein in the proportions shown on Exhibit "A" attached hereto and such participating interests shall remain in effect throughout the life of this agreement except that there shall be a readjustment of the adjusted surface acres among the parties hereto on the basis set forth in Section 1 of this Article 31 (E) and the interests of the parties recomputed upon the occurrence of any of the following events:

(i) Any tract is eliminated from this Agreement through failure of title or loss through failure to pay rentals in conformity with the provisions of this Agreement.

(ii) On satisfaction or payment in full of each production payment shown on Exhibit "A".

If any leasehold interest of the parties hereto becomes burdened with any additional overriding royalties, production payments or like obligations after being committed to this Agreement other than those shown on Exhibit "A" attached thereto, the burden thereof shall be borne exclusively by the owner or owners of each such tract.

All charges to the joint account of the parties hereto shall be governed by and made in accordance with the accounting procedure attached to this Operating Agreement.

(F) The provisions of Article 25 relative to "Acreage or Cash Contributions" shall not apply to the initial Test Well. Any cash contributions received shall be shared proportionately by the participating parties; acreage contributions set forth on page 3 of Exhibit "A" shall be made solely to Monsanto Company and David Fasken.

(G) This Agreement and the respective rights and obligations of the parties hereunder shall be subject to all valid and applicable State and Federal laws, rules, regulations and orders, and in the event this agreement or any provision hereof is, or the operations contemplated hereby are, found to be inconsistent with or contrary to any such law, rule, regulation or order, the latter shall be deemed to control and this Agreement shall be regarded as modified accordingly, and as so modified, to continue in full force and effect. Operator shall prepare and furnish to any duly constituted authority having jurisdiction in the premises through its proper agency or department any and all reports, statements and information that may be requested when such reports are required to be filed by Operator.

(H) Geological Requirements: With respect to the drilling of the Test Well required in Article 7 hereof or any substitute well as mentioned in Article 31 (C), Operator agrees:

(1) To furnish a daily drilling report to non-operators which shall include full information regarding the drilling progress of the well, with full and complete information as to all drillstem or other tests made within the

time covered by that report and any and all further pertinent information with respect thereto.

- (2) To furnish notice of intent to drill along with a survey plat including the distances and directions of the well from at least two governmental survey lines.
- (3) To make thorough drillstem tests of all formations encountered showing possibility for oil and/or gas production, such tests to be made in a manner and for the period of time necessary for prudent operation.
- (4) To run an induction-ES log from the base of the intermediate casing to total depth and to conduct a complete electrical survey of the well including a gamma ray-sonic log with caliper from the base of the surface casing to total depth; to catch samples at 10 foot intervals from the surface to total depth, keeping same available to non-operator at the well location at all times and in absence of instructions to the contrary, to deliver such samples upon completion of the well to the New Mexico sample cut service in Hobbs, New Mexico.
- (5) To give advance notice to non-operators at their respective addresses as set forth in Exhibit "A" in sufficient time for non-operators to arrange to have representatives present should non-operators desire to witness any and all coring, testing, (whether by drillstem or otherwise) running of any and all logs and surveys, and measuring the depth upon completion or plugging operations.
- (6) To furnish promptly to the offices of the non-operators as set forth in Exhibit "A" complete reports of the results of any and all tests conducted on the test well together with reports of all surveys of the hole however made and to furnish a copy of any and all core analysis, and drillstem test charts.
- (7) To specifically furnish non-operators with one field print copy and a sepia and two final prints of all electrical well surveys and any other surveys conducted on such wells.

This agreement may be signed in counterpart, and shall be binding upon the parties and upon their heirs, successors, representatives and assigns.

ATTEST:

\_\_\_\_\_

MONSANTO COMPANY

By: Frank Richardson  
Attorney-in-Fact  
Tax Ident. No. 43-0420020

~~XXXXXXXXXXXX~~

GULF OIL CORPORATION

~~ATTEST:~~

\_\_\_\_\_  
DAVID FASKEN

By: \_\_\_\_\_  
Attorney-in-Fact  
Tax Ident. No. \_\_\_\_\_

~~ATTEST:~~

\_\_\_\_\_  
LEN MAYER

ATLANTIC RICHFIELD COMPANY

\_\_\_\_\_  
ROBERT L. HAYNIE

By: S. L. Smith  
ATTORNEY IN FACT  
Tax Ident. No. 23-C371610

STATE OF NEW MEXICO )  
COUNTY OF CHAVES )

ss.

The foregoing instrument was acknowledged before me this 15th day of April, 1970, by S. L. Smith, Attorney in Fact of Atlantic Richfield Company, a Pennsylvania corporation, on behalf of said corporation.

Kattie Rae Magle  
Notary Public

My Commission Expires:  
November 20, 1970

By: \_\_\_\_\_  
Tax Ident. NO. \_\_\_\_\_

51

EXHIBIT "A"

(Attached to that certain Operating Agreement dated April 1, 1970, covering lands in Eddy County, New Mexico, by and between Monsanto Company and David Fasken, Len Mayer, Robert L. Haynie, Robert L. Haynie, Gulf Oil Corporation, Atlantic Richfield Company, Union Oil Company of California and Texaco Inc.)

LANDS SUBJECT TO THIS AGREEMENT: All of Section 1, Township 21 South, Range 25 East, N.M.P.M. Eddy County, New Mexico

RESTRICTION AS TO DEPTH: From surface down to a subsurface depth of 100 feet below total depth drilled in Test Well described in Article 7 hereof.

SCHEDULE SHOWING LEASEHOLD INTEREST WITHIN UNIT AREA; GROSS COMMITTED ACREAGE; PERCENTAGE OF BENEFICIAL INTEREST OF EACH WORKING INTEREST OWNER WITHIN UNIT AREA AND PARTICIPATION OF RESPECTIVE PARTIES IN OPERATIONS AND PRODUCTION

Working Interest Owners	Tract Nos.	Gross Acreage Committed	Percentage Acreage Committed	Overrides and			Net Working Interest (Acreage)	Net Percentage (Beneficial Interests)
				Basic Royalty	Other Lease Burdens			
Monsanto Company	2	18.300		12.5	\$500/Ac. out of 5%		15.0975	19.60053
	5	<u>151.065</u> 169.365	19.840795	12.5	5% ORR		<u>124.6286</u> 139.7261	
David Fasken	2	18.300		12.5	\$500/Ac. out of 5%		15.0975	19.60053
	5	<u>151.065</u> 169.365	19.840795	12.5	5% ORR		<u>124.6286</u> 139.7261	
Texaco Inc.	4	34.980		12.5	3% ORR		29.5581	17.85597
	7	<u>115.830</u> 150.810	17.667110	12.5	3.125% ORR		<u>97.7316</u> 127.2897	

58

	Col. 1	Col. 2	Col. 3	Col. 4	Col. 5	Col. 6
Working Interest Owners	Acreage Contributions initial test Well	Beneficial interests contributed initial test Well	Cost participation initial test well and operating costs until paid out	Participation from production initial test well until paid out	Participation cost all subsequent wells; operating costs including initial test well after payout, and ownership of equipment	Participation after payout initial test well and in all subsequent wells (2)
Monsanto Company			41.166445	41.072015 (1)	30.503620	30.336275
David Fasken			41.166445	41.072015 (1)	30.503620	30.336275
Texaco Inc.			17.667110	17.855970	17.667110	17.855970
Gulf Oil Corporation	38.020	4.40004			4.453980	4.400040
Atlantic Richfield Company	65.725	7.79073			7.699560	7.790730
Union Oil of California	65.725	7.79073			7.699560	7.790730
Len Mayer and Robert L. Haynie	12.570 182.040	1.48998		100.000000	1.472550 100.000000	1.489980 100.000000

(1) The interests of Monsanto Company and David Fasken are subject to an overriding royalty equal to 1/16th of 8/8ths of production from the initial Test Well until payout proportionately reduced to the interests of Gulf Oil Corporation, Atlantic Richfield Company, Union Oil Company of California, Len Mayer and Robert L. Haynie, subject to option to convert upon payout to a working interest. (2) Subject to conversion option provided for in Article 31 (E) hereof regarding the initial well, except as to the interest of Texaco Inc.

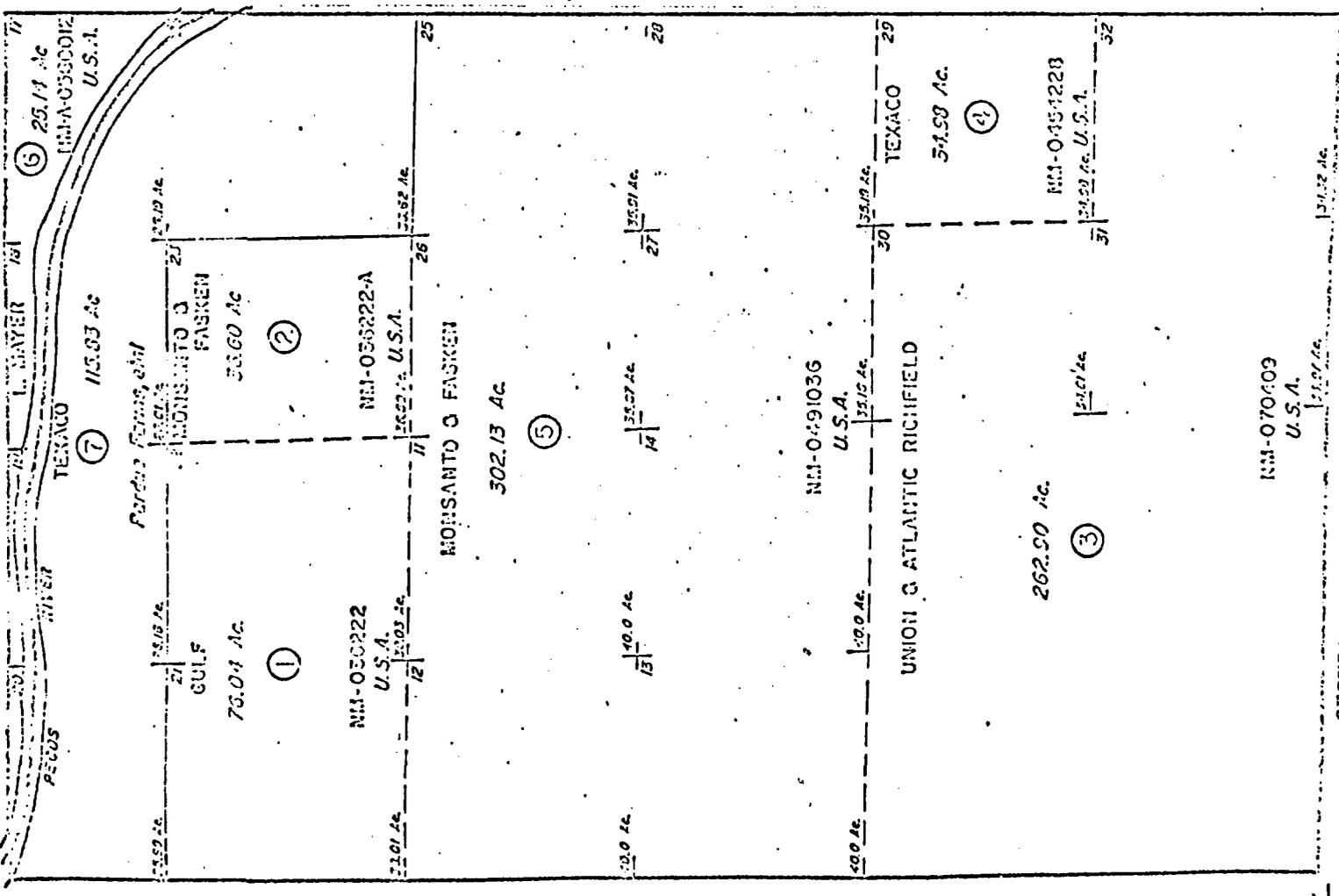
## ADDRESSES OF PARTIES TO WHICH NOTICES SHOULD BE SENT:

Monsanto Company 101 North Marienfeld Midland, Texas 79701	Texaco Inc. P. O. Box 3109 Midland, Texas 79701	Atlantic Richfield Company P. O. Box 1978 Roswell, New Mexico 88201	Len Mayer and Robert L. Haynie 260 Lincoln Tower Building 1860 Lincoln Street Denver, Colorado 80203
David Fasken 608 First National Bank Building Midland, Texas 79701	Gulf Oil Corporation P. O. Box 1938 Roswell, New Mexico 88201	Union Oil Company of California Security National Bank Building Roswell, New Mexico 88201	

LEASES COMMITTED

<u>Tract No.</u>	<u>Lessor</u>	<u>Lessee of Record</u>	<u>Date</u>	<u>Description</u>
1.	U.S.A. NM-036222	Gulf Oil Corporation	6-1-59	Lots 21 & 22
2.	U.S.A. NM-036222-A	Monsanto Company & David Fasken	6-1-59	Lot 23
3.	U.S.A. NM-070409	Atlantic Richfield Co. & Union Oil Co. of California	10-1-51	SW 1/4 & Lots 30, 31, 32
4.	U.S.A. NM-0454228	Texaco Inc.	1-1-64	Lot 29
5.	U.S.A. NM-0491036	Monsanto Company & David Fasken	4-1-64	Lots 11, 12, 13, 14, 25, 26, 27, 28
6.	U.S.A. NM-A 0560012	Len Mayer	6-1-66	That portion of Lots 17, 18, 19, 20 & 24 on the left or East bank of the Pecos River
7. (1)	Pardue Farms, etal	Texaco Inc.	10-14-65	( That portion of Lots 17, 18, 19, 20 & 24
(2)	Bohdan Hallas, etal	Texaco Inc.	3-12-70	( lying South & West of the Pecos River
(3)	Melton Winfield, et al	Texaco Inc.	3-23-70	(
(4)	First Nat'l. Bank of Birmingham, Successor Tr.	Texaco Inc.	3-12-70	(

All lands being in Section 1, T-21-S, R-25-E, Eddy County, New Mexico



SECTION 1, T-21-S, R-25-E, N.M.P.M.  
EDDY COUNTY, NEW MEXICO

8

## EXHIBIT " C "

Attached to and made a part of that certain Operating Agreement dated April 1, 1970, covering lands in Eddy County, New Mexico, by and between Monsanto Co. and David Fasken, Len Mayer, Robert L. Haynie, Gulf Oil Company, Atlantic Richfield Company, Union Oil Company of California and Texaco Inc.

## ACCOUNTING PROCEDURE (JOINT OPERATIONS)

### I. GENERAL PROVISIONS

#### 1. Definitions

"Joint Property" shall mean the real and personal property subject to the agreement to which this "Accounting Procedure" is attached.

"Joint Operations" shall mean all operations necessary or proper for the development, operation, protection and maintenance of the Joint Property.

"Operator" shall mean the party designated to conduct the Joint Operations.

"Non-Operators" shall mean the nonoperating parties, whether one or more.

"Joint Account" shall mean the account showing the charges and credits accruing because of the Joint Operations and which are to be shared by the Parties.

"Parties" shall mean Operator and Non-Operators.

"Material" shall mean personal property, equipment or supplies acquired or held for use on the Joint Property.

"Controllable Material" shall mean material which at the time is so classified in the Material Classification Manual as most recently recommended by the Council of Petroleum Accountants Societies of North America.

#### 2. Conflict with Agreement

In the event of a conflict between the provisions of this Accounting Procedure and the provisions of the agreement to which this Accounting Procedure is attached, the provisions of the agreement shall control.

#### 3. Collective Action by Non-Operators

Where an agreement or other action of Non-Operators is expressly required under this Accounting Procedure and if the agreement to which this Accounting Procedure is attached contains no contrary provisions in regard thereto, the agreement or action of a majority in interest of the Non-Operators shall be controlling on all Non-Operators.

#### 4. Statements and Billings

Operator shall bill Non-Operators on or before the last day of each month for their proportionate share of costs and expenses, for the preceding month. Such bills will be accompanied by statements reflecting the total charges and credits as set forth under Subparagraph C 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. Statement of all charges and credits to the Joint Account summarized by appropriate classifications indicative of the nature thereof, except that items of Controllable Material and unusual charges and credits shall be detailed.

#### 5. Payment and Advances by Non-Operators

Each Non-Operator 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~~ eight per cent (8%) per annum until paid.

#### 6. Adjustments

Payment of any such bills shall not prejudice the right of any Non-Operators to protest or question the correctness thereof; provided however, all bills and statements rendered to Non-Operators by Operator during any calendar year shall conclusively be presumed to be true and correct after twenty-four (24) months following the end of any such calendar year, unless within the said twenty-four (24) month period a Non-Operator takes written exception thereto and makes claim on Operator for adjustment. No adjustment favorable to Operator shall be made unless it is made within the same prescribed period. The provisions of this paragraph shall not prevent adjustments resulting from a physical inventory of the Joint Property as provided for in Section VII.

#### 7. Audits

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 for any calendar year within the twenty-four (24) month period following the end of such calendar year; provided however, the making of an audit shall not extend the time for the taking of written exception to and the adjustment of accounts as provided for in Paragraph 6 of this Section I. Where there are two or more Non-Operators, the Non-Operators shall make every reasonable effort to conduct joint or simultaneous audits in a manner which will result in a minimum of inconvenience to the Operator.

### II. DIRECT CHARGES

Subject to limitations hereinafter prescribed, Operator shall charge the Joint Account with the following items:

#### 1. Rentals and Royalties

Delay or other rentals and royalties when such rentals and royalties are paid by Operator for the Joint Account of the Parties.

#### 2. Labor

A. Salaries and wages of Operator's employees directly engaged on the Joint Property in the conduct of the Joint Operations, and salaries or wages of technical employees who are temporarily assigned to and directly employed on the Joint Property.

B. Operator's cost of holiday, vacation, sickness and disability benefits and other customary allowances paid to the employees whose salaries and wages are chargeable to the Joint Account under Paragraph 2A of this Section II and Paragraph 1 of Section III; except that in the case of those employees only a pro rata portion of whose salaries and wages are chargeable to the Joint Account under Paragraph 1 of Section III, not more than the same pro rata portion of the benefits and allowances herein provided for shall be charged to the Joint Account. Cost under this Paragraph 2B may be charged on a "when and as paid basis" or by "percentage assessment" on the amount of salaries and wages chargeable to the Joint Account under Paragraph 2A of this Section II and Paragraph 1 of Section III. If percentage assessment is used, the rate shall be based on the Operator's cost experience.

C. Expenditures or contributions made pursuant to assessments imposed by governmental authority which are applicable to Operator's labor cost of salaries and wages chargeable to the Joint Account under Paragraphs 2A and 2B of this Section II and Paragraph 1 of Section III.

D. Reasonable personal expenses of those employees whose salaries and wages are chargeable to the Joint Account under Paragraph 2A of this Section II and for which expenses the employees are reimbursed under Operator's usual practice.

**3. Employee Benefits**

Operator's current cost of established plans for employees' group life insurance, hospitalization, pension, retirement, stock purchase, thrift, bonus, and other benefit plans of a like nature, applicable to Operator's labor cost; provided however, the total of such charges shall not exceed ten percent (10%) of Operator's labor costs chargeable to the Joint Account under Paragraphs 2A and 2B of this Section II and Paragraph 1 of Section III.

**4. Material**

Material purchased or furnished by Operator for use on 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 may be required for immediate use; and the accumulation of surplus stocks shall be avoided.

**5. Transportation**

Transportation of employees and Material necessary for the Joint Operations but subject to the following limitations:

- A. If Material is moved to the Joint Property from the Operator's warehouse or other properties, no charge shall be made to the Joint Account for a distance greater than the distance from the nearest reliable supply store or railway receiving point where like material is available, except by agreement with Non-Operators.
- B. If surplus Material is moved to Operator's warehouse or other storage point, no charge shall be made to the Joint Account for a distance greater than the distance to the nearest reliable supply store or railway receiving point, except by agreement with Non-Operators. No charge shall be made to Joint Account for moving Material to other properties belonging to Operator, except by agreement with Non-Operators.
- C. In the application of subparagraphs A and B above, there shall be no equalization of actual gross trucking costs of \$100 or less.

**6. Services**

- A. The cost of contract services and utilities procured from outside sources other than services covered by Paragraph 8 of this Section II and Paragraph 2 of Section III.
- B. Use and service of equipment and facilities furnished by Operator as provided in Paragraph 5 of Section IV.

**7. Damages and Losses to Joint Property**

All costs or expenses necessary for the repair or replacement of Joint Property made necessary because of damages or losses incurred by fire, flood, storm, theft, accident, or any other cause, except to the extent that the damage or loss could have been avoided through the exercise of reasonable diligence on the part of Operator. Operator shall furnish Non-Operators written notice of damages or losses incurred as soon as practicable after a report thereof has been received by Operator.

**8. Legal Expense**

All costs and expenses of handling, investigating and settling litigation or claims arising by reason of the Joint Operations or necessary to protect or recover the Joint Property, including, but not limited to, attorneys' fees, court costs, cost of investigation or procuring evidence and amounts paid in settlement or satisfaction of any such litigation or claims; provided, (a) no charge shall be made for the services of Operator's legal staff or other regularly employed personnel (such services being considered to be Administrative Overhead under Section III), except by agreement with Non-Operators, and (b) no charge shall be made for the fees and expenses of outside attorneys unless the employment of such attorneys is agreed to by Operator and Non-Operators.

**9. Taxes**

All taxes of every kind and nature assessed or levied upon or in connection with the Joint Property, the operation thereof, or the production therefrom, and which taxes have been paid by the Operator for the benefit of the Parties.

**10. Insurance Premiums**

Premiums paid for insurance required to be carried on the Joint Property for the protection of the Parties.

**11. Other Expenditures**

Any other expenditure not covered or dealt with in the foregoing provisions of this Section II, or in Section III, and which is incurred by the Operator for the necessary and proper conduct of the Joint Operations.

**III. INDIRECT CHARGES**

Operator may charge the Joint Account for indirect costs either by use of an allocation of district expense items plus a fixed rate for administrative overhead, and plus the warehousing charges, all as provided for in Paragraphs 1, 2, and 3 of this Section III OR by combining all three of said items under the fixed rate provided for in Paragraph 4 of this Section III, as indicated next below:

**OPERATOR SHALL CHARGE THE JOINT ACCOUNT UNDER THE TERMS OF:**

- Paragraphs 1, 2 and 3. (Allocation of district expense plus fixed rate for administrative overhead plus warehousing.)
- Paragraph 4. (Combined fixed rate)

**1. District Expense**

Operator shall charge the Joint Account with a pro rata portion of the salaries, wages and expenses of Operator's production superintendent and other employees serving the Joint Property and other properties of the Operator in the same operating area, whose time is not allocated directly to the properties, and a pro rata portion of the cost of maintaining and operating a production office known as Operator's ..... office located at or near ..... (or a comparable office if location changed), and necessary sub-offices (if any), maintained for the convenience of the above-described office, and all necessary camps, including housing facilities for employees if required, used in connection with the operations of the Joint Property and other properties in the same operating area. The expense of, less any revenue from, such facilities may, at the option of Operator, include depreciation of investment or a fair monthly rental in lieu of depreciation. Such charges shall be apportioned to all properties served on some equitable basis consistent with Operator's accounting practice.

**2. Administrative Overhead**

Operator shall charge administrative overhead to the Joint Account at the following rates, which charge shall be in lieu of the cost and expense of all offices of the Operator not covered by Paragraph 1 of this Section III, including salaries, wages and expenses of personnel assigned to such offices. Such charges shall be in addition to the salaries, wages and expenses of employees of Operator authorized to be charged as direct charges as provided in Paragraphs 2 and 8 of Section II.

**WELL BASIS (RATE PER WELL PER MONTH)**

Well Depth	DRILLING WELL RATE (Use Total Depth)		PRODUCING WELL RATE (Use Current Producing Depth)		
	Each Well		First Five	Next Five	All Wells Over Ten
.....	.....	.....	.....	.....	.....
.....	.....	.....	.....	.....	.....
.....	.....	.....	.....	.....	.....

The cost and expense of services from outside sources in connection with matters of taxation, traffic, accounting, or matters before or involving governmental agencies shall be considered as included in the overhead rates provided for in this Paragraph 2 of Section III, unless such cost and expense are agreed upon between Operator and Non-Operators as a direct charge to the Joint Account.

23

some other purpose, shall be priced on a basis comparable with the items normally used for such other purpose.

(4) Material involving erecting or repairing shall be charged at applicable percentage of the current knocked-down price of new Material.

### 3. Premium Prices

Whenever Material is not readily obtainable at prices specified in Paragraphs 1 and 2 of this Section IV because of national emergencies, strikes or other unusual causes over which the Operator has no control, the Operator may charge the Joint Account for the required Material at the Operator's actual cost incurred in procuring such Material, in making it suitable for use, and in moving it to the Joint Property, provided, that notice in writing is furnished to Non-Operators of the proposed charge prior to billing Non-Operators for such Material. Each Non-Operator shall have the right, by so electing and notifying Operator within 10 days after receiving notice from Operator, to furnish in kind all or part of his share of such Material suitable for use and acceptable to Operator.

### 4. Warranty of Material Furnished by Operator

Operator does not warrant the Material furnished. In case of defective Material, credit shall not be passed to the Joint Account until adjustment has been received by Operator from the manufacturers or their agents.

### 5. Equipment and Facilities Furnished by Operator

A. Operator shall charge the Joint Account for use of equipment and facilities at rates commensurate with cost of ownership and operation. Such rates shall include cost of maintenance, repairs, other operating expense, insurance, taxes, depreciation and interest on investment not to exceed six per cent (6%) per annum, provided such rates shall not exceed those currently prevailing in the immediate area within which the Joint Property is located. Rates for automotive equipment shall generally be in line with the schedule of rates adopted by the Petroleum Motor Transport Association, or some other recognized organization, as recommended uniform charges against Joint Property operations. Rates for laboratory services shall not exceed those currently prevailing if performed by outside service laboratories. Rates for trucks, tractors and well service units may include wages and expenses of operator.

B. Whenever requested, Operator shall inform Non-Operators in advance of the rates it proposes to charge.

C. Rates shall be revised and adjusted from time to time when found to be either excessive or insufficient.

## V. DISPOSAL OF MATERIAL

The Operator may purchase, but shall be under no obligation to purchase, interest of Non-Operators in surplus Condition "A" or "B" Material. The disposition of surplus Controllable Material, not purchased by Operator, shall be subject to agreement between Operator and Non-Operators, provided Operator shall dispose of normal accumulations of junk and scrap Material either by transfer or sale from the Joint Property.

### 1. Material Purchased by the Operator or Non-Operators

Material purchased by either the Operator or Non-Operators shall be credited by the Operator to the Joint Account for the month in which the Material is removed by the purchaser.

### 2. Division in Kind

Division of Material in kind, if made between Operator and Non-Operators, shall be in proportion to the respective interests in such Material. The Parties will thereupon be charged individually with the value of the Material received or receivable. Proper credits shall be made by the Operator in the monthly statement of operations.

### 3. Sales to Outsiders

Sales to outsiders of Material from the Joint Property shall be credited by Operator to the Joint Account at the net amount collected by Operator from vendee. Any claim by vendee related to such sale shall be charged back to the Joint Account if and when paid by Operator.

## VI. BASIS OF PRICING MATERIAL TRANSFERRED FROM JOINT ACCOUNT

Material purchased by either Operator or Non-Operators or divided in kind, unless otherwise agreed to between Operator and Non-Operators shall be priced on the following basis:

### 1. New Price Defined

New price as used in this Section VI shall be the price specified for New Material in Section IV.

### 2. New Material

New Material (Condition "A"), being new Material procured for the Joint Property but never used, at one hundred per cent (100%) of current new price (plus sales tax if any).

### 3. Good Used Material

Good used Material (Condition "B"), being used Material in sound and serviceable condition, suitable for reuse without reconditioning:

A. At seventy-five per cent (75%) of current new price if Material was charged to Joint Account as new, or

B. At sixty-five per cent (65%) of current new price if Material was originally charged to the Joint Account as secondhand at seventy-five percent (75%) of new price.

### 4. Other Used Material

Used Material (Condition "C"), at fifty per cent (50%) of current new price, being used Material which:

A. Is not in sound and serviceable condition but suitable for reuse after reconditioning, or

B. Is serviceable for original function but not suitable for reconditioning.

### 5. Bad-Order Material

Material (Condition "D"), no longer suitable for its original purpose without excessive repair cost but usable for some other purpose at a price comparable with that of items normally used for such other purpose.

### 6. Junk Material

Junk Material (Condition "E"), being obsolete and scrap Material, at prevailing prices.

### 7. Temporarily Used Material

When the use of Material is temporary and its service to the Joint Property does not justify the reduction in price as provided for in Paragraph 3 B of this Section VI, such Material shall be priced on a basis that will leave a net charge to the Joint Account consistent with the value of the service rendered.

## VII. INVENTORIES

The Operator shall maintain detailed records of Material generally considered controllable by the Industry.

### 1. Periodic Inventories, Notice and Representation

At reasonable intervals, inventories shall be taken by Operator of the Joint Account Material, which shall include all such Material as is ordinarily considered controllable. Written notice of intention to take inventory shall be given by Operator at least thirty (30) days before any inventory is to begin so that Non-Operators may be represented when any inventory is taken. Failure of Non-Operators to be represented at an inventory shall bind Non-Operators to accept the inventory taken by Operator, who shall in that event furnish Non-Operators with a copy thereof.

### 2. Reconciliation and Adjustment of Inventories

Reconciliation of inventory with charges to the Joint Account shall be made, and a list of overages and shortages shall be jointly determined by Operator and Non-Operators. Inventory adjustments shall be made by Operator with the Joint Account for overages and shortages, but Operator shall be held accountable to Non-Operator only for shortages due to lack of reasonable diligence.

### 3. Special Inventories

Special inventories may be taken whenever there is any sale or change of interest in the Joint Property. It shall be the duty of the party selling to notify all other Parties as quickly as possible after the transfer of interest takes place. In such cases, both the seller and the purchaser shall be governed by such inventory.