STATE OF NEW MEXICO
ENERGY, MINERALS AND NATURAL RESOURCES DEPARTMENT
OIL CONSERVATION DIVISION

APPLICATIONS OF FAE II OPERATING, LLC
FOR STATUTORY UNITIZATION,
LEA COUNTY, NEW MEXICO.

CASE NO. 22972

RESPONSE OF APACHE CORPORATION, CHEVRON U.S.A. INC., CITATION OIL & GAS CORP., COG OPERATING LLC, CONOCOPHILLIPS, OXY USA INC., XTO HOLDINGS, LLC, AND XTO ENERGY INC. TO APPLICANT'S MOTION FOR DETERMINATION ON RATIFICAITON REQUIREMENT OF PHASED ALLOCATION FORMULA UNDER THE STATUTORY UNITIZATION ACT

Apache Corporation, Chevron U.S.A. Inc., Citation Oil & Gas Corp., COG Operating LLC, ConocoPhillips, OXY USA Inc., XTO Holdings, LLC, and XTO Energy Inc. (collectively, "Respondents") submit this Response to FAE II Operating, LLC's ("FAE") Motion for Determination on Approval Requirements of Phased Allocation Formula Under the Statutory Unitization Act ("Motion"). For the reasons discussed herein, the New Mexico Oil Conservation Division ("Division") must reject FAE's suggestion that it can satisfy the voluntary ratification requirements of the New Mexico Statutory Unitization Act ("the Act") by cherry picking tracts within the proposed unit as "Phase I" tracts and demonstrating that "75% of the cost bearing and non-cost bearing interest have approved the first phase of FAE's proposed two-phase allocation formula." FAE Motion at p. 1; *see also* FAE Motion at p. 4 (contending the Division can impose statutory unitization "when at least 75% of interest owners in the *initial phase of unit operations* have ratified the operating plan." [emphasis own]).

INTRODUCTION AND SUMMARY OF ARGUMENT

FAE suggests the Division can force Respondents into a 19,369.77-acre unit by utilizing a gerrymandered two-phase allocation formula designed such that FAE owns most of the working interest in the limited tracts falling under "Phase I." *Id.* FAE's proposed tract allocation formula (yet to be approved by the Division) places non-contiguous tracts comprising less than one-third of the proposed unit area (approximately 6,200-acres) into Phase I.[1] The owners in these disjointed Phase I tracts will pay the cost and receive the revenues of the proposed unit operations for the first three years. However, the working interest owners in the remaining Phase II tracts (comprising over two-thirds of the proposed unit) incur the costs of development for the first three years, but do not share in any of the revenue. Instead, at the end of the first three years the Phase II owners, such as the Respondents, are required to pay in full their proportionate share of all incurred costs "plus compounded interest accrued at ten percent (10.00%) per annum as of the transition date to Phase II." *See* FAE Exhibit 2 to Application (proposed Unit Operating Agreement) at Section 2.1.3. Failure to pay these lump-sum incurred costs plus interest will result in the owners in the Phase II tracts being considered "non-participating Working Interest Owners" subject to "actual cost plus three hundred percent (300%) cost recoupment of all unpaid costs on the corresponding AFE or invoice." *Id.* In addition, Operations during that three-year period "will be conducted uniformly throughout the Unit in both phases," including the tracts falling within Phase II. *See* Exhibit A to FAE's Motion (Song Affidavit) at ¶ 7. Accordingly, FAE seeks to

[1] FAE does not specifically disclose in their Application or Motion the total acreage of the tracts included in Phase I. This information has been extrapolated from the Unit Agreement's Exhibit C "Schedule of Tract Participation" filed with FAE's Application. The acreage of the tracts designated by FAE with a "Phase I Participation Factor" add up to only 6,200-acres. *See* Attachment A (highlighted tracts). As demonstrated by Attachment A-1, these Phase II tracts are not contiguous and are scattered throughout the proposed unit area.

commence development of the entire proposed unit area resting solely on the approval from working interest owners in tracts comprising less than one-third of the proposed unit.

FAE has not shared with Respondents the data or methodology used to determine the Phase I and Phase II tracts, contending that information is proprietary. Instead, FAE has simply stated the Phase I tracts are based on six months of oil production in 2021 and the Phase II tracts are based on the remaining recoverable oil in place. *See* Exhibit A (Song Affidavit) to FAE's Motion at ¶ 6. FAE has not identified a factual basis for choosing six months of production from 2021 to determine the Phase I tracts, nor has FAE disclosed the methodology, data or analysis used to determine the Phase II tracts. Further, the only evidence FAE has provided to substantiate voluntary approval from the working interest owners in these limited Phase I tracts is to summarily state they have done so. FAE has not identified the consenting working interest owners in the Phase I tracts nor has FAE accounted for depth severances and other variables in the ownership of these limited tracts.

Nonetheless, FAE's motion seeks to convince the Division that it can force Respondents into the proposed unit, and begin development of any tract within the proposed 19,369.77-acre unit, by resting on the voluntary approval from undisclosed working interest owners in tracts comprising less than one-third of the proposed unit area. For support, FAE cites to the word "initially" in the first sentence of Section 70-7-8(A). However, FAE's interpretation of this single word is not consistent with the remainder of the Act, is not consistent with prior Division orders addressing statutory unitization, is not consistent with the treatises addressing statutory unitization, and undermines the core mandate of the Act to protect the correlative rights of all working interest owners in the proposed unit area and ensure the unit is fair, reasonable, and equitable to all owners.

ARGUMENT

THE NEW MEXICO STATUTORY UNITIZATION ACT REQUIRES THE NECESSARY APPROVAL FROM THE INIITAL WORKING INTEREST OWNERS IN "THE PROPOSED UNIT AREA," NOT THE INITIAL BENEFICIARIES UNDER A GERRYMANDERED TRACT ALLOCATION FORMULA.

Citing solely to the word "initially" in Section 70-7-8(A), FAE contends the Division can force Respondents into its proposed unit by simply showing that "75% of interest owners in the *initial phase of unit operations* have ratified the operating plan." FAE Motion at p. 4 (emphasis own). However, the word "initially" in Section 70-7-8(A) cannot be read in isolation and must be interpreted in the context of the remainder of this section and other provisions of the Act. *See* ***Grisham v. Reeb***, 2021-NMSC-006, ¶ 12, 480 P.3d. 852 (courts must "construe a statute according to its obvious spirit or reason" and particular language must be read "in the context of the statute as a whole, including its purposes and consequences."); ***Key v. Chrysler Motors Corp***., 1996-NMSC-038, ¶ 14, 121 N.M. 764, 918 P.2d 350 ("[A]ll parts of a statute must be read together to ascertain legislative intent" and "[courts] are to read the statute in its entirety and construe each part in connection with every other part to produce a harmonious whole."). When viewed in the context of the entire Act, the word "initially" cannot be read to ignore the correlative rights of the Respondents and the other working interest owners in the tracts comprising over two-thirds of the proposed unit. Instead, the Division must determine whether the necessary voluntary approval has been obtained from the initial working interest owners in the entire proposed unit area.

A. The Act Requires 75% Voluntary Approval From The Initial Working Interest Owners In The Entire Proposed Unit Area.

Any application for statutory unitization must provide "a description of the proposed unit area and the vertical limits to be included therein …." NMSA 1978, § 70-7-5(A). The term "unit area" is defined as the "legal description in terms of surface area of the pool or part of the pool to

be operated as a unit and the vertical limits to be included ….” NMSA 1978, § 70-7-7(A). The Act requires the Division to ultimately enter an order ensuring “correlative rights [are] protected of all owners of mineral interests in each unitized area” and is “upon terms and conditions that are fair, reasonable and equitable” to all owners in the proposed unit area. *See* NMSA 1978, §§ 70-7-1 and 70-7-7.

A separate component of the Division’s order must also address how production and costs are “allocated to the separately owned tracts in the unit area….” NMSA 1978, § 70-7-7(C). The Division must find that the proposed tract allocation formula “allocates the produced and saved unitized hydrocarbons to the separately owned tracts in the unit area on a fair, reasonable and equitable basis.” NMSA 1978, § 70-7-6(A)(6). Ultimately, “the production allocated to each tract shall be the proportion that the relative value of each tract so determined bears to the relative value of all tracts in the unit area.” NMSA 1978, § 70-7-6(A)(6). The tract allocation formula is a different examination by the Division and independent of the voluntary approval threshold required by the Act.

Against this background, FAE conflates the tract allocation formula with the voluntary approval threshold, isolates the word “initially” from the rest of the statute and offers an interpretation that ignores—in this case—the correlative rights of working interest owners in over two-thirds of the proposed unit. The Act does not support such an absurd result.

Attachment B hereto provides a complete copy of Section 70-7-8 that highlights in yellow the phrase relied upon by FAE and highlights in blue the remaining language referencing the necessary percentage of voluntary joinder. That remaining language discusses the necessary percentage in relation to the “unit area,” defined in Section 70-7-7(A) as the “legal description in terms of surface area of the pool or part of the pool to be operated as a unit and the vertical limits

to be included." (emphasis added). The Act clearly contemplates an examination of the voluntary approval reached with the initial working interest owners in the entire surface of the proposed unit area (here, over 19,000-acres) and not just the voluntary approval of the working interest owners in tracts placed within various "phases" of a proposed tract allocation formula. The 75% approval threshold required by the Act is separate and apart from the proposed tract allocation formula, which must eventually be approved by the Division after receiving evidence on the "relative value of all tracts in the unit area." *See* NMSA 1978, Section 70-7-6(B) (emphasis added).

B. Requiring 75% Approval From The Initial Working Interest Owners In The Entire Proposed Unit Area Does Not Write The Term "Initially" Out Of The Statute.

A common sense reading of the Division's authority that protects the correlative rights of all the working interest owners in the proposed unit area does not write the term "initially" out of the statute as suggested by FAE. *See* Motion at p. 4.

1. The term "initially" cannot be read to ignore the correlative rights of the working interest owners in over two-thirds of the proposed unit area and refers to the initial working interest owners in the proposed unit area.

Section 70-7-8 is a restriction on the Division's authority to exercise the police power of the state to force mineral owners into a proposed unit. Accordingly, this restriction must be broadly construed to protect the correlative rights of the working interest owners in the proposed unit area. *See* ***Grisham v. Reeb***, 2021-NMSC-006, ¶ 12, 480 P.3d. 852 (courts "will not be bound by literal interpretation[s] of the words if such strict interpretation would defeat the intended objective of the legislature," and "where statutory language is doubtful, ambiguous, or an adherence to the literal use of the words would lead to injustice, absurdity, or contradiction, [courts] construe a statute according to its obvious spirit or reason."); 5 Summers, Oil and Gas, § 952 ("As to compulsory poolings and unitizations, no definition should be attempted beyond noting that these have the consequences imposed by law through valid exercises of the police power, and these

consequences should be held to the minimum to accomplish the police power purposes of prevention of waste and protection of correlative rights."), *id* § 962 ("As a general proposition neither voluntary nor compulsory poolings and unitizations are supposed to have any greater effect on other relationships than necessary to accomplish the operational purpose of pooled production, the former because this is the purpose of the agreement and the latter because the statutory structure should be interpreted in a manner consistent with the limited purpose of the state's police power.") (emphasis added). The objective of the legislature declared in the Act mandates that the Division's authority be used in a fashion that protects the correlative rights of all mineral interests in the proposed unit:

> **70-7-1. Purpose of act.**
>
> The legislature finds and determines that it is desirable and necessary under the circumstances and for the purposes hereinafter set out to authorize and provide for the unitized management, operation and further development of the oil and gas properties to which the Statutory Unitization Act is applicable, to the end that greater ultimate recovery may be had therefrom, waste prevented, *and correlative rights protected of all owners of mineral interests in each* ***unitized area***. It is the intention of the legislature that the Statutory Unitization Act apply to any type of operation that will substantially increase the recovery of oil above the amount that would be recovered by primary recovery alone and not to what the industry understands as exploratory units. [emphasis added]

See also NMSA 1978, Section 70-7-7 (requiring the Division to ultimately enter an order approving unitization "upon terms and conditions that are fair, reasonable and equitable" to all owners in the proposed unit area.)

The correlative rights of the working interest owners in the proposed "unitized area" are not protected by looking only at the level of voluntary participation by the working interest owners in the limited tracts comprising Phase I. Rather, the necessary protection is accomplished when the phrase "initially to pay" in Section 70-7-8(A) is construed to mean the Division examines the level of voluntary participation by the initial working interest owners in the proposed unitized area.

The phrase "initially to pay" prevents parties who may develop a future working interest in the unit area from either blocking or consenting to the proposed unit operations.

A good example is a standard farmout agreement. Under such agreements, the farmor may relinquish a working interest for a period of time or retain a non-cost bearing interest that can be converted to a working interest. Another example is provided under Attachment C, a form Assignment of Interest in Oil and Gas Leases. Paragraph 3 of this form document provides for the assignment of a working interest upon the specified payout event. These are merely examples of the various contractual arrangements that exist wherein a third-party is not required "initially to pay" the costs of development but may eventually obtain a cost-bearing interest. The phrase "initially to pay" in the first sentence of Section 70-7-8 makes it clear that future or back-in working interest owners are not considered in determining compliance with the 75% voluntary approval required by the cost-bearing owners in the unit area.

2. Under FAE's Proposed Unit Agreement, Respondents and the other working interest owners in the Phase II tracts are initially responsible for payment of unit operations.

Putting aside for a moment the statutory interpretation issue raised by FAE's Motion, it should be noted that under FAE's proposed Unit Operating Agreement the Respondents and the other Phase II owners are initially responsible for payment of the costs incurred during the three-year Phase I period. *See* FAE Exhibit 2 to Application (proposed Unit Operating Agreement) at Section 2.1.3. From the first day of unit operations, the Respondents and other Phase II owners are credited with their share of the costs "plus compounded interest accrued at ten percent (10.00%) per annum as of the transition date to Phase II." Failure of the Phase II owners to pay their share of the costs and interest imposed and credited to them from the start of unit operations at the end of the Phase I period will result in those owners being considered "non-participating Working

Interest Owners" subject to proposed cost plus 300% risk penalty. *Id.* Accordingly, under FAE's proposed Operating Agreement, Respondents and the other Phase II working interest owners in the proposed unit area will not share in the revenues for the first three years of operations, but "will be required initially to pay" the costs of the unit operations at the end of that three-year period plus yearly compounded accrued interest. *See* NMSA 1978, § 70-7-8(A).

In any event, the Act does not support FAE's suggestion that it can force Respondents into the proposed unit, and begin development of any tract within the proposed 19,369.77-acre unit, by resting on the voluntary approval from working interest owners in tracts comprising less than one-third of the proposed unit area.

D. Division Orders Have Uniformly Examined The Voluntary Approval From All Initial Working Interest Owners In The Proposed Unit Area, Not A Subset Of Owners Selected By The Applicant's Proposed Tract Allocation Formula.

In Division Case No. 15792, FAE sought approval from the Division for its proposed West Eumont Unit. In that case, FAE's landman testified that the company had obtained 80% approval of the working interest owners in the entire proposed unit, not those initially benefiting from a proposed allocation formula:

> Q. And how many interest owners of all types are there in the proposed unit?
> A. Oh, over 100.
> Q. Let's talk first about working interest owners. Does Exhibit 4 contain a listing of working interest owners in the proposed unit?
> A. Yes. Exhibit 4 is the working interest owners.
> Q. What is the approximate current approval overall unit of working interest owners? What percentage interest have currently approved the unit?
> A. Well in excess of 80 percent.

Case 15792, 9/14/17 Tr. at 10. Subsequently the Division issued its Order finding: "At the time of the hearing, Applicant had obtained approval of the Unit by more than 75 percent of the cost bearing interests." Order R-14615 at p. 3, finding 7(d).

Division Order R-10460 (issued in 1995 under Division Cases Nos. 11297 and 11298) likewise discussed the tracts and working interests in the "proposed Unit Area":

> (7) The proposed Unit Area contains twelve separate tracts of land, the working interests in which are owned by forty-eight different interest owners. Exxon operates five of the twelve tracts, five tracts are operated by Yates Petroleum Corporation ("Yates"), one tract is operated by Premier Oil & Gas, Inc. ("Premier"), and one tract operated by MWJ Producing Company. There are twenty-four royalty and overriding royalty interest owners in the proposed Unit Area. [emphasis added]

Order R-10460, at p. 3 ¶ 7 (findings). The Division ultimately issued the following ordering paragraph:

> (5) Since the persons owning the required statutory minimum percentage interest in the Unit Area have approved, ratified, or indicated their preliminary approval of the Unit Agreement and the Unit Operating Agreement, the interests of all persons within the Unit Area are hereby unitized whether or not such persons have approved the Unit Agreement or the Unit Operating Agreement in writing. [emphasis added]

Order R-10460 at p. 11, Ordering ¶ 5.

A review of the oil and gas treatises on statutory unitization confirm the Division's long-standing practice to look at the voluntary approval of the initial working interest owners in the entire proposed unit area, not the initial beneficiaries under a proposed phased-in tract allocation formula. Professor Kuntz instructs: "In those states where unitization can be imposed upon the owners of minority interests, the order has the effect of unitizing the area included after the plan of unitization has been ratified by the owners of the required percentage of the area covered by the plan." 5 Kuntz, Law of Oil and Gas, § 78.2 (emphasis added). Professors Williams & Myers similarly notes that statutes forcing parties into a unit generally "require that owners of specified percentages of the operating and nonoperating interests in the unitized area join in the plan within a specified period of time (usually six months) after the entry of the unitization order." 6 Williams & Meyers, Oil and Gas Law, § 913.5 (emphasis added). None of these treatises support the interpretation of the Act offered by FAE.

The Division should not accept FAE's invitation to depart from its precedence when a wholistic reading of the Act, the legislative purpose and the treatises support these decisions.

E. Approval Of Operations Across The Entire Unit Area Based On Ratification By The Working Interest Owners In One-Third Of The Surface Acreage Is Not Only Inequitable, But Will Incentivize Gerrymandering To Meet Voluntary Unitization Threshold Requirements.

FAE admits it seeks to use the joinder of the working interest owners in the Phase I tracts where it holds most—if not all—of the working interest to commence development of the entire proposed unit area:

> Although FAE has proposed a two-phased allocation formula, development will be conducted uniformly throughout the Unit in both phases….

Exhibit A to FAE's Motion (Song Affidavit) at ¶7. During the initial three-year period, the working interest owners in the Phase II tracts (comprising over two-thirds of the development area) do not receive any revenue from unit operations on their tracts but accrue the costs of all development (plus yearly compounded interest at 10%) for a three-year period. *See* FAE Exhibit 2 to Application (proposed Unit Operating Agreement) at Section 2.1.3. Yet, FAE seeks to force these Phase II owners into the proposed 19,369.77-acre unit, and conduct operations on their tracts, by looking only to the voluntary level of approval from the working interest owners in the Phase I tracts comprising less than one-third of the proposed unit area. There is nothing "fair, reasonable, and equitable" about this interpretation of the Act, nor does FAE's interpretation protect the correlative rights of all initial working interest owners in the proposed unit area. *See* NMSA 1978, §§ 70-7-1 and 70-7-7. Rather, as the adage goes, FAE "wants to have their cake and eat it too."

New Mexico courts conduct statutory interpretation in a reasonable manner that aligns with the obvious spirit of the statute—not in a manner that results in an inequitable and absurd outcome. The Division must follow an interpretation of its authority under the Act that protects the

correlative rights of all the initial working interest owners in the proposed unit area. To adopt FAE's position on the meaning of Section 70-7-8 will incentivize operators to gerrymander tracts into "phased-in" allocation formulas designed to meet the voluntary approval threshold but, in this case, leave the working interest owners in thousands of acres with no voice in approving or disapproving the statutory unitization. FAE's interpretation of the approval threshold required by Section 70-7-8 clearly does not align with the legislative intent expressed in the Act.

III. CONCLUSION

FAE's interpretation of Section 70-7-8(A) is not correct and must be rejected by the Division.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that on October 20, 2022 I served a copy of the foregoing document to the following counsel of record via Electronic Mail to:

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ATTACHMENT A

EXHIBIT "C"
SCHEDULE OF TRACT PARTICIPATION
Attached to and made a part of the Unit Agreenment
for the South Jal (Yates - Seven Rivers - Queen) Unit Area
Lea County, New Mexico

Tract No.	Acreage	Phase I Participation Factor	Phase II Participation Factor
1	80.00	0.00762816	0.00553141
2	320.00	0.02663926	0.01919136
3	320.10	0.00000000	0.00853031
4	600.00	0.00000000	0.00935523
5	480.00	0.00000000	0.03805478
6	80.31	0.00000000	0.00224016
7	80.00	0.00000000	0.00504578
8	960.30	0.00347812	0.02243809
9	1,120.00	0.00000000	0.04947447
10	320.00	0.00000000	0.00932606
11	80.00	0.00000000	0.00123584
12	718.87	0.16169321	0.03604184
13	640.00	0.06450338	0.02126373
14	240.00	0.00000000	0.00846371
15	481.00	0.01466345	0.00788536
16	640.00	0.12276195	0.01346946
17	119.93	0.00324098	0.00653134
18	80.00	0.00000000	0.00464394
19	160.00	0.00043477	0.01333175
20	640.00	0.00000000	0.03622143
21	600.00	0.00000000	0.03410094
22	40.00	0.00000000	0.00118589
23	520.00	0.00000000	0.03843847
24	920.00	0.00000000	0.03638394
25	80.00	0.00233192	0.00198119
26	160.00	0.00000000	0.01021661
27	200.00	0.00000000	0.01674371
28	40.00	0.00000000	0.00291909
29	240.00	0.02841785	0.01137948
30	159.86	0.00000000	0.00608998
31	160.00	0.00000000	0.01237581
32	160.00	0.00000000	0.00758346
33	160.00	0.00000000	0.01040038
34A	118.17	0.00000000	0.00943075
34B	39.75	0.00000000	0.00326593
35A	80.00	0.00000000	0.00726294
35B	80.00	0.00000000	0.00410594
35C	160.00	0.00000000	0.00961710
36A	40.00	0.00000000	0.00095806
36B	40.00	0.00000000	0.00044843
36C	80.00	0.00000000	0.00195888
37A	160.00	0.00000000	0.01173725
37B	80.00	0.00000000	0.00542239
37C	80.00	0.00000000	0.00676911
38	80.00	0.00592862	0.00619401
39A	80.00	0.00000000	0.00720950
39B	40.00	0.00000000	0.00301962

ATTACHMENT A

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Tract No.	Acreage	Phase I Participation Factor	Phase II Participation Factor
40A	80.00	0.00000000	0.00820514
40B	80.00	0.00000000	0.00797981
41A	40.00	0.00000000	0.00130326
41B	120.00	0.00000000	0.00438602
42	240.00	0.00000000	0.01118573
43	1,240.00	0.46859808	0.09205046
44	160.00	0.00000000	0.00564398
45	40.00	0.00000000	0.00159119
46	160.00	0.00000000	0.00528341
47	160.00	0.00000000	0.00831945
48	40.00	0.00000000	0.00255035
49	33.18	0.00000000	0.00378836
50	153.12	0.00000000	0.01406579
51	40.00	0.00000000	0.00281170
52	40.00	0.00000000	0.00282143
53	40.00	0.00000000	0.00089463
54	80.00	0.00000000	0.00220701
55	40.00	0.00000000	0.00197614
56	80.00	0.00000000	0.00592019
57	40.00	0.00000000	0.00183514
58	106.10	0.00000000	0.01052318
59	80.00	0.00000000	0.00398626
60	80.00	0.00000000	0.00346263
61	40.00	0.00000000	0.00325811
62	40.00	0.00000000	0.00385451
63	160.00	0.00000000	0.01127101
64	40.00	0.00229240	0.00344590
65	40.00	0.00000000	0.00277878
66	40.00	0.00000000	0.00300126
67	160.00	0.00000000	0.01242996
68	80.00	0.01292439	0.00587191
69	160.00	0.00000000	0.00963241
70	40.00	0.00000000	0.00057751
71	80.00	0.00000000	0.00206950
72	40.00	0.00000000	0.00099366
73	160.00	0.00000000	0.00551377
74	160.00	0.00000000	0.01097068
75	320.00	0.00000000	0.02575839
76	80.00	0.00000000	0.00259400
77	80.00	0.00000000	0.00490806
78	39.08	0.00000000	0.00261236
79	80.00	0.00000000	0.00735234
80	160.00	0.00000000	0.01417373
81	120.00	0.00000000	0.00663488
82	60.00	0.00000000	0.00543041
83	20.00	0.00000000	0.00196857
84	20.00	0.00000000	0.00164965
85	160.00	0.00000000	0.00877607

ATTACHMENT A

EXHIBIT "C"
SCHEDULE OF TRACT PARTICIPATION
Attached to and made a part of the Unit Agreenment
for the South Jal (Yates - Seven Rivers - Queen) Unit Area
Lea County, New Mexico

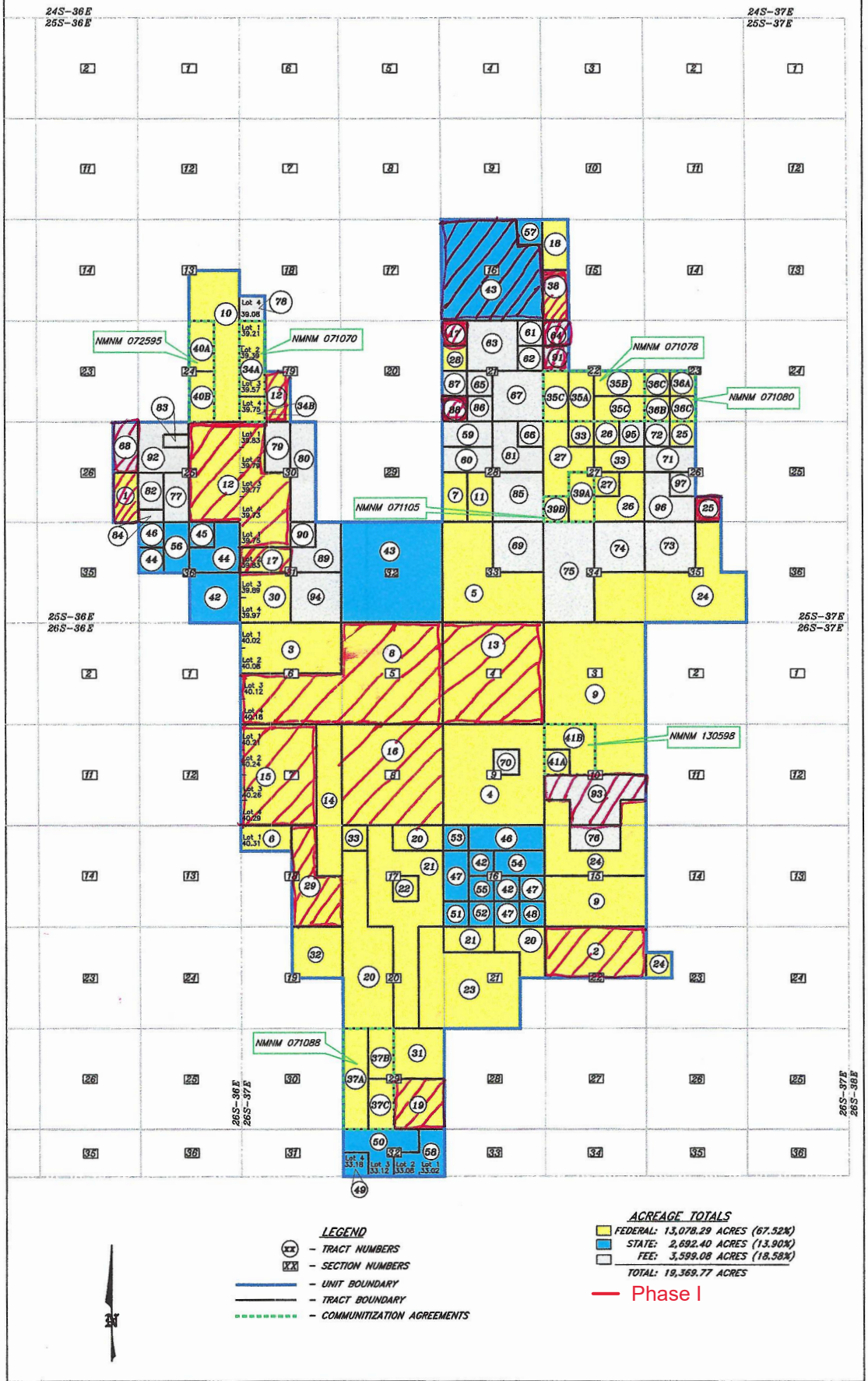
Tract No.	Acreage	Phase I Participation Factor	Phase II Participation Factor
86	40.00	0.00000000	0.00255132
87	40.00	0.00000000	0.00193529
88	40.00	0.01924825	0.00139920
89	120.00	0.00000000	0.00861516
90	40.00	0.00000000	0.00274330
91	40.00	0.00505909	0.00377398
92	140.00	0.00000000	0.01302697
93	240.00	0.05015612	0.00815987
94	160.00	0.00000000	0.00591965
95	40.00	0.00000000	0.00074562
96	120.00	0.00000000	0.00423068
97	40.00	0.00000000	0.00110536
TOTAL:	**19,369.77**	**1.00000000**	**1.00000000**

ATTACHMENT A-1

EXHIBIT "A"

SOUTH JAL (YATES – SEVEN RIVERS – QUEEN) UNIT

Lea County, New Mexico



Drawn By: K. Goad	File: JAL SECTION MAP
Survey Date:	Date: 02-17-2022
Checked By: G.L.J.	Last Rev. Date: 02-17-2022
Survey Job No.	SCALE: 1" = 6000'
Sheet 1 of 1 Sheets	

BASIN LLC

FAE II OPERATING, LLC

ATTACHMENT B

70-7-8. Ratification or approval of plan by owners.

A. No order of the division providing for unit operations shall become effective unless and until the plan for unit operations prescribed by the division has been approved in writing by those persons who, under the division's order, will be required initially to pay at least seventy-five percent of the costs of the unit operations, and also by the owners of at least seventy-five percent of the production or proceeds thereof that will be credited to interests which are free of cost such as royalties, overriding royalties and production payments, and the division has made a finding either in the order providing for unit operations or in a supplemental order that the plan for unit operations has been so approved. Notwithstanding any other provisions of this section, if seventy-five percent or more of the unit area is owned, as to working interest, by one working interest owner, such working interest owner must be joined by at least one other working interest owner in ratifying and approving the plan of unit operations, unless such working interest owner is the owner of one hundred percent of the working interest in said unit area; provided, however, if a single owner is one who, under the division's order will be required initially to pay at least twenty-five percent, but not more than fifty percent, of the costs of unit operation, such owner must be joined by at least one other owner of the same type interest in disapproving, or failure to approve, the plan of unit operations to defeat the plan.

B. If one owner is the owner of at least twenty-five percent, but not more than fifty percent, of the production or proceeds thereof that will be credited to interests which are free of costs, such owner must be joined by at least one other owner of the same type interest in disapproving, or failure to approve, the plan of unit operations to defeat the plan.

C. If the persons owning the required percentage of interest in the unit area do not approve the plan for unit operations within a period of six months from the date on which the order providing for unit operations is made, such order shall cease to be of further force and effect and shall be revoked by the division, unless the division shall extend the time for ratification for good cause shown.

D. When the persons owning the required percentage of interest in the unit area have approved the plan for unit operations, the interests of all persons in the unit are unitized whether or not such persons have approved the plan of unitization in writing.

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28A West's Legal Forms, Specialized Forms § 22:93

West's Legal Forms | November 2021 Update

Specialized Forms

Richard Gillman [a4], William B. Burford (Chapter 22) [a5]

Chapter 22. Minerals, Oil and Gas

Part II. Oil and Gas Forms

B. Assignments

2. Assignment Forms

§ 22:93. Partial assignment with reservation of overriding royalty interest and optional "back-in" interest in initial well

ASSIGNMENT OF INTEREST IN OIL AND GAS LEASES

This agreement (this "Assignment") is made and entered into on the date hereinafter set forth by and between *[name of assignor]* (collectively referred to herein as "Assignor"), whose address is *[address of assignor]*, and *[name of assignee]* ("Assignee"), whose address is *[address of assignee]*.

1. Assignment.

For consideration paid, the receipt and sufficiency of which are hereby acknowledged, Assignor hereby grants, bargains, assigns, and conveys to Assignee, subject to the exceptions and reservations hereinafter set forth, the following interests:

(a) An undivided seventy-five percent (75%) of Assignor's right, title, and interest, as set forth in Exhibit *[designation of exhibit]* hereto, in and to the oil and gas leases described in Exhibit *[designation of exhibit]* attached hereto and made a part hereof, insofar and only insofar as said leases cover all or any part of the lands described in said Exhibit *[designation of exhibit]* (the "Subject Lands"), together with a like percentage interest in all rights, titles, and interests of Assignor in and to the oil and gas leasehold estate in the Subject Lands, including contractual rights under operating agreements and other agreements, easements, and in oil and gas production sales agreements, pooling and communitization agreements, and other rights and interests necessary or useful to the operation of the Subject Lands for the production of oil and gas.

(b) All of the right, title, and interest attributable to the remaining twenty-five percent (25%) of the interest of Assignor in the Subject Lands, insofar and only insofar as such interest covers and pertains to the first well (the "Earning Well") drilled by Assignee in the Subject Lands and completed as a well capable of producing oil or gas, and in and to the oil and gas produced therefrom, subject to the overriding royalty interest and reversionary working interest hereinafter referred to, together with a like interest in and to such contractual rights, easements, and other rights held by Assignor as are necessary or useful to the drilling and operation of such well. The interest conveyed in this Subparagraph 1(b), to the extent it is in addition to the interest conveyed in Subparagraph 1(a) above, shall be limited to the operation of and production from the Earning Well and to no other

ATTACHMENT C

well that may be hereafter drilled in the Subject Lands, provided that the rights and interests of Assignee under this Subparagraph 1(b), and Assignor's reserved overriding royalty therein, shall extend to all depths and horizons in the wellbore of such well, as initially drilled or to which it may thereafter be deepened or extended, vertically or horizontally.

2. Overriding Royalties.

This Assignment is made proportionately subject to all royalty, overriding royalty, and other burdens affecting the Subject Lands that are disclosed of record as of the date of this Assignment. In addition, Assignor excepts from this Assignment and reserves to itself the following overriding royalty interests:

(a) With respect to all of the Subject Lands and the interests hereby conveyed therein, an overriding royalty interest equal to one-half (1/2) of the difference, if any, between: (i) twenty-five (25%) of 8/8 of the market value at the wells of the oil and gas that may be produced, saved, and marketed from the Subject Lands; and (ii) the aggregate of all royalty, overriding royalty, production payment, and other non-cost-bearing interests now existing as burdens against such production; and

(b) In addition, an overriding royalty interest in the oil and gas produced from the Earning Well only equal to the difference, if any, between: (i) twenty-five percent (25%) of 8/8 of the market value at the well of the oil and gas that may be produced, saved, and marketed from the Earning Well; and (ii) the aggregate of all royalty, overriding royalty, production payment, and other non-cost-bearing interests now existing as burdens against such production, including the overriding royalty interest in the Subject Lands reserved in Subparagraph (a) of this Paragraph 2 immediately above.

The overriding royalty interests reserved to Assignor shall bear their proportionate share of all taxes and assessments levied upon or against or measured by the production of oil and gas therefrom and shall be proportionately reduced if and to the extent that this Assignment conveys to Assignee less than the full and undivided oil and gas working interest leasehold in the Subject Lands (or, with respect to the overriding royalty interest referred to in Subparagraph (b) above, in the right to drill and operate the Earning Well). If Assignor's interest in the Subject Lands is now subject to overriding royalty and other lease burdens equal to or greater than said 25% of 8/8 of the oil and gas attributable to Assignor's interest, then Assignor shall be entitled to no overriding royalty interest hereunder. On all oil and gas sold by Assignee in an arms-length sale, the market value shall be the amount realized by Assignee from such sale.

3. Optional Reversionary Interest in Earning Well.

Upon the occurrence of payout of the Earning Well, Assignee shall give written notice thereof to Assignor, and Assignor shall have thirty (30) days after receipt of such notice within which to elect either: (a) to retain the overriding royalty interest in the Earning Well reserved in Subparagraph (b) within Paragraph 2 above in addition to the overriding royalty interest in all of the Subject Lands reserved in Subparagraph (a) of Paragraph 2 above, or (b) relinquish said overriding royalty interest reserved in Subparagraph (b) of Paragraph 2 hereof and receive from Assignee a reassignment of an undivided twenty-five percent (25%) interest in and to the Earning Well, proportionately reduced according to the working interest now owned by Assignor in the Subject Lands (i.e., the interest in the Earning Well hereby assigned over and above the working interest hereby assigned in the remainder of the Subject Lands). Assignor's failure to notify Assignee of its election within such time period shall be deemed an election to retain its entire overriding royalty interest in the Earning Well and not to receive a reassignment of said working interest. “Payout” is defined as the point in time when the “net proceeds” from the sale of all oil and gas production from the Earning Well attributable to the interest assigned by Assignor to Assignee equal the sum of: (1) 100% of the cost and expense, both tangible and intangible, attributable to such interest of the drilling, testing, completing, equipping, and operating of such well prior to payout, (2) 100% of all costs and expenses attributable to such interest of reworking, plugging back, and recompleting said well prior to payout, and (3) 100% of the cash sum, if any, paid by Assignee to Assignor upon the execution of this Assignment. As used herein, “net proceeds” shall be the total proceeds received from or credited to oil and gas production, after deducting severance, production, and other taxes payable on or measured by production, together with all royalties, rentals, shut-in gas royalties, overriding royalties (including those reserved to Assignor hereunder), and payments out of production in effect on the date of this assignment. Every three months during the payout period, Assignee agrees to furnish Assignor a statement reflecting the charges and credits to the payout account.

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4. Term.

This assignment shall extend for a term of two years from the effective date hereof (the "Primary Term") and for so long, and only so long, thereafter as: (a) there is a well capable of producing oil or gas in paying quantities located on the Subject Lands or lands pooled or communitized therewith; (b) Assignee is engaged in drilling or reworking operations at the end of the end of the Primary Term on the Subject Lands or lands pooled or communitized therewith, or has commenced drilling or reworking operations within sixty (60) days after cessation of production of oil or gas from the Subject Lands, or lands pooled or communitized therewith, and is thereafter engaged in drilling or reworking operations, either on the same well or on different wells, without cessation of more than sixty (60) consecutive days until there has been completed a well capable of production oil or gas in paying quantities; or (c) Assignee is engaged in Continuous Drilling Operations as provided below. At any time this Assignment terminates, either in whole or in part, Assignee shall reassign to Assignor all of the rights and interests as to which such termination has occurred, free of any liens, encumbrances, overriding royalty interests, and other burdens other than those in effect at the time of the execution hereof.

5. Continuous Drilling Operations.

Regardless of whether or not oil or gas production has been established within the Primary Term, this Assignment shall remain in effect as to all of the Subject Lands so long as Assignee is engaged in Continuous Drilling Operations on the Subject Lands or on lands pooled or communitized therewith. "Continuous Drilling Operations," as that term is used herein, shall be deemed to be in progress so long as the drilling of an additional well is commenced on the Subject Lands, or lands pooled or communitized therewith, no more than one hundred eighty (180) days after the completion of the last previous well drilled hereunder, "completion" being the date a dry hole is plugged and abandoned or, for a well capable of production, the date the well is completed as set out in the official governmental report of completion. The drilling of the first well under such Continuous Drilling Operations shall be commenced as follows:

(a) If at the end of the Primary Term there is no well capable of producing oil or gas in paying quantities on the Subject Lands, then on or before the end of the Primary Term, or within one hundred eighty (180) days after the completion of the last well drilled during the Primary Term, whichever is later;

(b) If at the end of the Primary Term there is a well capable of producing oil or gas in paying quantities on lands within the Subject Lands, and completion of the last well drilled during the Primary Term was more than one hundred eighty (180) days prior to the end of the Primary Term, then on or before the end of the Primary Term; or

(c) If at the end of the Primary Term there is a well capable of producing oil or gas in paying quantities on the Subject Lands, and completion of the last well drilled during the Primary Term was less than one hundred eighty (180) days prior to the end of the Primary Term, then within one hundred eighty (180) days from the completion of the last well drilled during the Primary Term.

The commencement or continuation of Continuous Drilling Operations shall be at Assignee's option and shall not be an obligation or covenant of Assignee, If Continuous Drilling Operations are not commenced within the time above specified or if, at any time after commencement of Continuous Drilling Operations, more than one hundred eighty (180) days elapse between the completion of one well and the commencement of the drilling of the next well, this Assignment shall, at the end of the period of time in which Assignee was required to commence a well, terminate as to all of the Subject Lands except those portions included within a proration unit established under the well spacing and density rules of any governmental body having jurisdiction assigned to a well then capable of producing oil or gas in paying quantities or on which Assignee is then engaged in bona fide operations to establish or restore production of oil or gas. If this Assignment is continued in force under the immediately preceding sentence as to a proration unit on which operations are being conducted in an effort to establish or restore production but on which there is no well then capable of producing oil or gas, this Assignment shall likewise terminate upon cessation of such operations for a period of sixty (60) consecutive days unless such operations (on the same or on an additional well or wells in the same proration unit) have resulted in restoration or establishment of a well capable of producing oil or gas in paying quantities on such proration unit. If the applicable well spacing and density rules do not prescribe the amount

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of acreage that may be assigned to a proration unit for a well drilled by Assignee hereunder, such proration unit shall consist of forty (40) acres for an oil well or one hundred sixty (160) acres for a gas well, as designated in writing by Assignee in an instrument filed for record in the county where said lands are located.

6. Operating Agreement.

This Assignment is made subject to that certain Operating Agreement dated *[date of agreement]*, between Assignee, as operator, and Assignor, as nonoperator, which shall apply to any lands and operations in which both Assignee and Assignor jointly own working interest leasehold interests, and shall further govern the calculation of costs that may be applied in determining payout of the Earning Well.

7. Communitization.

The Subject Lands and Assignor's interests therein shall be subject to any pooling or communitization by Assignee of the Subject Lands or any portion thereof with other lands for the purpose of forming a well spacing or proration unit in accordance with the rules of any governmental authority or to any extent authorized by the leases described herein. In the event of any such pooling or communitization in a manner that is binding on the interests of the lessor or lessors under the leases assigned hereby, Assignor's overriding royalty interests in the oil and gas produced from the pooled or communitized area shall be paid in the proportion that the amount of surface acreage to which such overriding royalty interest or interests apply within the pooled or communitized unit bears to the total surface acreage of such unit. Operations on or production of oil or gas from a well located anywhere in any such unit shall be deemed, for purposes of perpetuating the term hereof, to be located on the Subject Lands.

8. Information and Access.

During the drilling of any well by Assignee, including the Earning Well, Assignor's authorized representatives shall have access at all times to each such well, at Assignor's sole risk and expense. In addition, Assignor shall have access to all cores, cuttings, logs and other information of whatever nature obtained during the drilling of such well. Assignee further agrees to furnish Assignor daily drilling reports and other pertinent well information and data as specified in Schedule *[designation of schedule]* attached hereto and made a part hereof (if there is such a Schedule I attached hereto), with respect to any well drilled hereunder. It is understood, however, that Assignor's right to information hereunder shall not extend to any interpretive data or other proprietary data that Assignor may prepare for its own use with respect to any such well.

9. Special Warranty; Successors and Assigns.

Assignor warrants and agrees to defend title to the interests assigned hereby against all persons claiming or to claim the same by, through, and under Assignor, but not otherwise. This assignment shall be binding on the parties hereto and their respective successors and assigns.

EXECUTED on the dates of Assignor's and Assignee's respective acknowledgments annexed hereto, but effective as of *[effective date of assignment]*.

ASSIGNOR:

_____

[Name of assignor]

ASSIGNEE:

_____

[Name of assignee]

[Acknowledgments]

Notes

Commentary

This form of assignment and that at § 22:91 above may be used in lieu of a farmout agreement of the type envisioned in §§ 22:99 to 22:102 below. The use of an assignment such as this addresses the concern an assignee may have that its interest is not presently vested and shown of record so as to provide constructive notice.

Footnotes

a4 St. Paul, Minnesota, Member of the Minnesota Bar.

a5 Hinkle, Hensley, Shanor & Martin, L.L.P., Midland Texas.

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