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dp dugan production corp.

OIL CONSERVATION DIV.
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June 30, 2000

Mr. Mark Ashley
New Mexico Oil Conservation Division
2040 South Pacheco Street
Santa Fe, NM 87505

Mr. Pete Martinez
New Mexico State Land Office
PO Box 1148
Santa Fe, NM 87504-1148

Mr. Richard Dembowski
Bureau of Land Management - Farmington Field Office
1235 La Plata Highway
Farmington, NM 87401

Re: Add 2 wells to Dugan's Com 1E CDP (Tabor Gathering System)
Plus Surface Commingling, off-lease measurement and Sale of Natural Gas
Dugan Production's Jiggs No. 1 & Jiggs. No. 2
Federal Lease No. NM-0206995
San Juan County, New Mexico

Dear Mr. Ashley, Mr. Martinez, and Mr. Dembowski,

We are writing to request approvals to add two wells, Dugan's Jiggs No. 1 and Jiggs No. 2 to the central delivery sales meter (CDP) initially authorized for Dugan's Com No. 1E and No. 2 and recently expanded to include Dugan's Com No. 4, Federal I No. 99 and Tabor Com No. 90 wells. This will also require the surface commingling of natural gas and water, plus the off lease measurement and sale of natural gas produced from the Jiggs No. 1 and 2. We do not anticipate any condensate or oil to be produced from either of these wells but should any ever occur, it will be separated, stored and sold at the individual well sites and will not be included in the Tabor Gathering System.

The Com No. 1E CDP (located in Unit A, Section 2, T-29N, R-14W, at the Com No. 1E well site) and surface commingling of natural gas from the Com No. 1E and Com No. 2 was approved by the New Mexico State Land Office (NMSLO) on 7-17-96, the Bureau of Land Management (BLM) on 7-30-96 and the New Mexico Oil Conservation Division (NMOCD) on 8-19-96 (NMOCD Order R-10655). This CDP was initially placed into service during 9/96 and has allowed the Com No. 1E and Com No. 2 to be produced using only one compressor. By application dated March 29, 2000 we proposed the addition of three wells to the Com 1E CDP; Dugan Production's Com No. 4, Federal I No. 99 and Tabor Com No. 90. The addition of these three wells was approved by the NMSLO on 4/27/00, the NMOCD on 5/25/00 (Order R-10655-A) and is pending with the BLM. Since this application to add Dugan's Jiggs No. 1 and No. 2 wells only involves one Federal lease, it is our understanding that this application only requires approvals from the BLM and NMOCD. There will be no changes to the gathering system with regards to State leases and thus we are providing this application to the NMSLO to update their records regarding the Com 1E CDP,

however NMSLO approval should not be necessary.

NMOCD approvals to date (Order R-10655 dated 8-19-96 and Order R-10655-A dated 5/25/00) have been the result of formal examiner hearings. We are not sure why the initial application in 1996 was set for hearing, but since the Com No. 1E CDP was initially authorized by an OCD hearing order, our 3/29/2000 application to expand the system to include three wells was also set for hearing. For both hearings, the OCD docket advertised that Dugan's application would be considered and taken under advisement in the absence of objection. Dugan Production provided all interest owners involved with copies of the applications and hearing notices. Neither hearing received any objection and both orders were issued without a formal appearance by Dugan Production. We appreciate the NMOCD allowing our prior two applications to be handled in this manner, however compared to the administrative approval process, this process was tedious on both occasions and definitely created an extra work effort, not only for Dugan Production, but also for the NMOCD. We do not understand why this CDP required a hearing initially and considering that we will likely be adding additional wells in the future, we request that the NMOCD consider an administrative approval of this application as well as all future applications to add wells to the Tabor Gathering System. Dugan Production operates several other similar gathering systems and has been able to use the administrative approval process not only for the initial application, but also for subsequent applications to add wells. If this application for some reason cannot be processed administratively and will require a formal hearing, then we request that provisions for an administrative approval process for the addition of future wells be included in the matters considered at the hearing.

We believe that the surface commingling issues for Dugan's Tabor Gathering System and Com 1E CDP should be approvable administratively since even though the ownership in each well is not common, Dugan Production has installed (and will install on all future wells) conventional gas metering equipment on each well to meter the natural gas produced from each well prior to commingling with production from other wells. These meters are maintained to regulatory standards used for gas sales meters and the continuous recording charts are integrated monthly by a commercial chart service. The volumes recorded by these wellsite meters are used to compute monthly allocation factors which are then used to allocate the CDP gas sales volumes and BTU's back to each individual well.

Dugan Production has recently drilled the Jiggs No. 2, (which is currently waiting to be completed), and plans to drill the Jiggs No. 1 in the very near future. Both wells will require wellhead compression to deliver gas into El Paso's system which is currently being operated at a pressure of ±250 psi and at times the pressure will approach 350 psi. We are proposing to add these two wells to Dugan's recently installed Tabor Gathering System and to deliver production (water and natural gas) to the central battery for the Com No. 1E CDP. Each of these two wells will be completed in the Harper Hill Fruitland Sand-Pictured Cliffs Gas Pool, and will likely produce a significant volume of water along with natural gas. Neither of the wells is anticipated to produce any condensate or oil. We are proposing to operate these two wells in a similar manner as are the five other wells currently approved for the system, i.e. produce natural gas from each well up the casing-tubing annulus and after metering the gas at the individual well site using a conventional meter run and Barton dry flow meter, transport the gas to the central battery where it will be collected and compressed using a central compressor for delivery to the Com No. 1E CDP sales meter. The CDP sales meter is on El Paso Field Service's system and is maintained by El Paso.

The water from each well, plus any natural gas that is associated with the water production, will be produced up the tubing (likely with rod pump artificial lift equipment) and will be transported to the central battery in a separate line. At the central battery, the produced water streams will be commingled and any associated natural gas will be separated. The water will be transferred to water storage tanks at the central battery and then transferred to Dugan Production's Stella Needs A Com Water Disposal System using a

water injection pump also located at the central battery. The natural gas separated from the water at the central battery will be metered using a conventional gas meter run equipped with a Barton dry flow meter, and after metering, the gas will be delivered to the central compressor for compression and sale. This meter will be of similar design to the gas metering equipment located at each well. The gas recovered from the central battery water separator will be allocated to the individual wells contributing production to the separator based upon the volumes of water each well produced. Attachment No. 6 presents a sketch of the central battery which is unchanged from the sketch included with our 3/29/00 application other than being modified to include the Jiggs No. 1 & 2 wells. The proposed allocation procedures for water and gas are presented on Attachment No. 5 which is also unchanged from the procedure previously approved for the Com No. 1E CDP. The water production rates will be periodically tested at each well using Dugan's portable, 3 phase test unit. The test frequency will be based upon need as determined by volumes at the central battery; i.e. any changes of significance in the total volume will indicate the need for retesting each well.

Attachment No. 1 was reproduced from portions of the Youngs Lake and Kirtland USGS Quadrangle Topography maps and presents Dugan Production's Tabor Gathering System. In addition, the wells connected to the system along with Dugan's leases are also identified. The Jiggs No. 1 & 2 plus the associated proposed pipeline additions are highlighted in blue. Also presented on Attachment No. 1 is Dugan Production's proposed King Gathering System which will deliver gas to Dugan's Com No. 91 CDP (currently the Com No. 1 CDP). This system is separate from the Tabor Gathering System (and Com No. 1E CDP) and is only presented on Attachment No. 1 for informational purposes since the two systems are in close proximity to one another and both systems send produced water to Dugan's Stella Needs A Com No. 1E SWD well located in Unit D of Section 36, T-30N, R-14W.

Attachment No. 2 presents individual well and lease information and attachment No. 3 presents the C-102 for the Jiggs No. 1 & 2 wells, along with the dedicated spacing units and associated lease. The same Federal lease, NM-0206995, comprises all of the spacing units for each well. Dugan Production Corp. is the operator of both wells and holds 100% of the working interest. The ownership for the Jiggs No. 1 & 2 along with all other wells on the system is presented in Attachment No.4. Page No. 1 of Attachment No. 4 presents a summary for all wells and pages two through seven present the specific data for each well.

Since the Jiggs No. 2 has been drilled but has not been completed and the Jiggs No. 1 is not yet drilled, we do not have production from either well. We do expect that both wells will have production characteristics similar to the adjacent and recently completed Com No. 4 which is currently averaging ±350 MCFD plus 100 BWPD from the Harper Hill Fruitland Sand-Pictured Cliffs gas pool.

Production from the Jiggs No. 1 & 2 should be similar in quality and composition to the two other Harper Hill Fruitland Sand-PC wells on the system and mixing should not create any operational problems. In addition, since revenues from the CDP will be allocated to the individual wells using allocation factors based upon individual well BTU's, mixing of these gases will not affect the value to any of the wells.

We are sending copies of this application to all interest owners in the Jiggs No. 1 & 2 wells and Attachment No. 7 presents a copy of the transmitted letter to the overriding royalty interest owners. All working interest is held by Dugan Production and all royalty interest in these two wells is Federal.

In summary, we are proposing to add two wells to Dugan's Tabor Gathering System and Com No. 1E CDP sales meter. This will allow the Jiggs No. 1 & 2 wells to share the Tabor Gathering System central compressor and will allow produced water from these two wells to be transported for disposal by pipeline rather than truck. By adding these two wells to the Tabor Gathering System, it will eliminate the need to

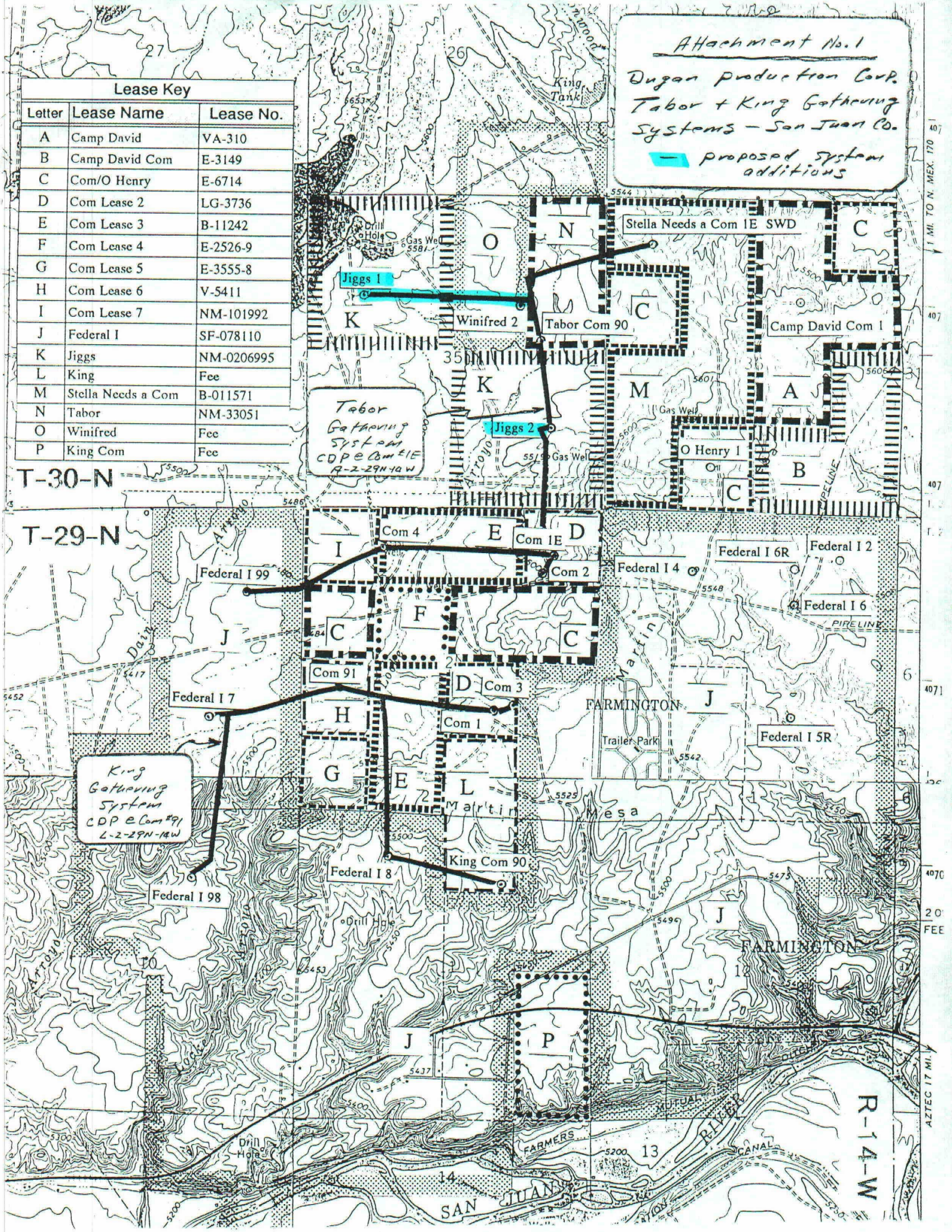
install wellhead compressors at each well and the trucking of two to three loads of water per day. This should reduce the volumes of gas needed for compressor fuel (with a corresponding increase in gas volumes available for sale) and will reduce compressor noise, exhaust emissions and truck traffic. These two wells will be operated consistent with the procedures already approved for the five existing wells and should have no affect upon the existing wells.

Should you have any questions or need additional information, please let me know.

Sincerely,

John D. Roe
Engineering Manager

cc: All interest owners
NMOCD - Aztec


Attachment No. 1
Dugan production Corp.
Tabor + King Gathering Systems – San Juan Co.
— proposed system additions
Lease Key
Letter | Lease Name | Lease No.
A | Camp David | VA-310
B | Camp David Com | E-3149
C | Com/O Henry | E-6714
D | Com Lease 2 | LG-3736
E | Com Lease 3 | B-11242
F | Com Lease 4 | E-2526-9
G | Com Lease 5 | E-3555-8
H | Com Lease 6 | V-5411
I | Com Lease 7 | NM-101992
J | Federal I | SF-078110
K | Jiggs | NM-0206995
L | King | Fee
M | Stella Needs a Com | B-011571
N | Tabor | NM-33051
O | Winifred | Fee
P | King Com | Fee
Tabor Gathering System CDP e Com 1E A-2-29N-14W
King Gathering System CDP e Com #91 L-2-29N-14W
Stella Needs a Com 1E SWD
Jiggs 1
Winifred 2
Tabor Com 90
Camp David Com 1
Jiggs 2
O Henry 1
Com 4
Com 1E
Com 2
Federal I 99
Federal I 4
Federal I 6R
Federal I 2
Federal I 6
Com 91
Com 3
Com 1
Federal I 7
Federal I 5R
King Com 90
Federal I 8
Federal I 98
T-30-N
T-29-N
R-14-W
FARMINGTON
Trailer Park
Martin Mesa
Drill Hole
Gas Well
Arroyo
Dairy
PIPELINE
MUTUAL
RILEY
FARMERS
CANAL
SAN JUAN
1 MI. TO N. MEX. 170
AZTEC 17 MI.