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SETTLEMENT

AGREEMENT

January 23rd 2004

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SETTLEMENT AGREEMENT

FEB 12 2004

This Settlement Agreement is entered into as of the 23rd day of February, 2004, by and between Controlled Recovery, Inc. ("CRI") and the New Mexico Oil Conservation Division of the Energy Minerals and Natural Resources Department ("Division").

WHEREAS, CRI operates a commercial surface waste management facility in Lea County, New Mexico, under the authority of Division Order R-9166;

WHEREAS, by letters dated July 3, 2000; September 27, 2000; and July 6, 2001, the Division sought to "re-permit" CRI's facility, impose new operational conditions, and revoke certain netting exemptions CRI has operated under since 1991;

WHEREAS, on August 17, 2001, CRI filed a Complaint for Declaratory and Injunctive Relief in the Fifth Judicial District Court of the State of New Mexico, Lea County, against the Division, its director and its district supervisor seeking declaratory and injunctive relief in a case styled *Controlled Recovery Inc., v. Chris Williams et al.*, Cause No. CV 2001-310G ("CRI's Complaint");

WHEREAS, without admission of liability or fault, the parties desire to resolve the issues raised by the Division's letters and CRI's Complaint without the necessity of further litigation and the costs associated with such litigation.

NOW, THEREFORE, in consideration of the mutual covenants and agreements of the parties and other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, and for the purpose of fully and completely resolving the claims asserted in CRI's Complaint and all other claims, known or unknown, arising out of or concerning the operation of CRI's facility in Lea County, the parties agree as follows:

- A. **Withdrawal of Prior Letters and Recognition of No Violations.** The letters issued by the Division to CRI Dated July 3, 2000; September 27, 2000; and July 6, 2001 are hereby withdrawn and shall have no force or effect. The Division acknowledges that to the best of its knowledge, pending formal inspection, CRI's facility is in full compliance with all applicable rules and orders of the Division.
- B. **Netting Exemptions Remain.** The netting exemptions issued by the Division for CRI's facility in July of 1991 under Permit No. H-76 and by letter dated April 7, 1997, remain in full force and affect.
- C. **Closure Plan, Bonding, and Closure of Pit Nos. 13 and 16.** The Division accepts and approves the closure plan submitted by CRI on September 1, 2000. CRI shall immediately increase its closure bond with the Division to the total amount of \$53,000 plus tax. In addition, CRI shall close within six months storage pits Nos. 13 and 16 pursuant to CRI's closure plan. In the event that these storage pits are not closed within 6 months of the execution of this Settlement Agreement,

then CRI shall further increase its closure bond to a total amount of \$73, 000 plus tax.

- D. Operational Conditions.** In addition to the operational conditions imposed on CRI's facility by Order R-9166 and Division Rule 711.C and 711.D as presently codified and enacted, CRI agrees to abide by the following additional operational conditions:

Overall Facility Operation

1. The facility must be fenced and have a sign at each entrance. The sign must be legible from at least 50 feet and contain the following information: a) name of the facility; b) location by section, township and range; c) emergency phone number; and d) OCD order number.
2. The facility will be maintained, contoured, and bermed to prevent runoff and runoff of the portion of the facility containing contaminated solids and liquids.
3. All above ground tanks and fuel tanks will be bermed, the current berm height will be maintained, and the tanks will be labeled as to the contents with standard hazard labels.
4. Sumps and below grade tanks without leak detection systems shall have their integrity tested annually. Sumps and below grade tanks that can be removed from their emplacements may be tested by visual inspection. Other sumps and below grade tanks shall be tested by appropriate mechanical means.
5. Sumps and below grade tanks will be inspected weekly and fluid will be removed as necessary to prevent overflow. If any defects are noted, repairs must be made as soon as possible.
6. All saddle tanks and drums containing materials other than fresh water must be labeled as to contents with standard hazard labels.
7. A checklist of all inspections at CRI's facility will be kept and maintained for Division review.
8. The OCD shall be notified prior to the installation of any pipes or wells or other construction within the boundaries of the facility that are not associated with the operation of the facility.
9. Any major design changes to CRI's facility must be submitted to the Division's Santa Fe Office for approval.

Pond and Pit Operation

10. All produced water must be unloaded into tanks. The produced water must reside in the tank and skim pit system long enough to allow for oil separation. Oil recovered must be stored in above-ground storage tanks.
11. All pits and ponds that contain liquids must have sufficient freeboard to prevent overtopping and a minimum freeboard of (1) one foot.
12. Free oil within the ponds and pits must be removed as soon as possible.
13. Ponds and pits will be inspected on a weekly basis and, if any defect is noted, repairs must be made as soon as possible.
14. A sign or other such marker with the pit/pond number must be clearly posted at each pit/pond location.

H2S Prevention & Contingency Plan

15. CRI personnel will wear H2S personnel monitors under circumstances in which H2S may be present, including the unloading of materials that may contain H2S. The monitors shall issue a visual and audible signal at 10 ppm of H2S in the ambient air that becomes more rapid at 20 ppm. An inspection for the presence of H2S shall be conducted weekly and reported on the inspection checklist.
16. In the event that a reading of 10 ppm is registered at CRI's facility, CRI personnel will evacuate the area and CRI will monitor H2S levels along the downwind boundary of the facility. If H2S levels reach 20 ppm, the facility will be closed and notification will be given to the following:

New Mexico State Police
Lea County Sheriff
The Division's Hobbs District office
17. CRI will notify Calaway Safety in Hobbs to provide personnel, equipment, and supplies to mitigate the source of an H2S reading of 10 ppm or greater.
18. CRI will log and report to the Division all incidences where a reading of 10 ppm H2S or greater is registered at CRI's facility.

Treating Plant Operations

19. The treating plant will be inspected weekly and if any defect is noted repairs will be made as soon as possible. If the defect will jeopardize the integrity of the plant, the plant will be shut down until repairs have been completed.
20. The treating plant may use diesel and gasoline from storage tanks that are to be pulled, repaired, or replaced. This material may only be used in the treating plant as a product to aid in the chemical treatment and blending of crude oil.
21. CRI shall submit to the Division a functional diagram or engineering schematic that depicts the functioning of the treating plant as a whole, and each major element thereof.

Solid Waste Disposal

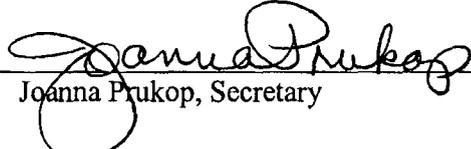
22. CRI shall submit to the Division a general plan of operations for solid waste disposal areas 50 and 51 that will provide a written description of the ongoing excavation and closure operations. CRI will also submit an updated plat showing all current disposal cells and past burial operations.
 23. Mechanical stabilization of liquids may be used prior to disposal.
 24. Free liquids will not be disposed of in the solid waste disposal pits.
 25. The solid waste disposal area will be inspected on a weekly basis and, if any defect is noted, repairs must be made as soon as possible.
 26. The solid waste disposal area will be bermed to prevent runoff and runoff of rain and storm water.
 27. All trash accepted at the facility that has the potential for blowing away or being transported by other vectors must be covered with soil within 24 hours of disposal into the solid waste pit.
 28. The Division will be notified before any new cells or expansion of existing cells in the solid waste disposal area are constructed.
- E. **Dismissal of Complaint.** Upon the execution of this agreement, CRI's Complaint shall be dismissed, with each party bearing their own attorneys' fees, costs, expenses, and disbursements. The parties will cooperate to promptly file all documents necessary to accomplish such dismissal.

- F. **No admission.** This Agreement represents the settlement of disputed claims, and does not constitute an admission of the correctness of any position asserted by any party, or an admission of liability of any wrongdoing by any party.
- G. **Construction.** This Agreement shall be construed based upon its terms and stated intent, including the recitals, and shall not be construed in the favor of one or another party based upon who may have contributed to its drafting, or on any other basis.
- H. **Counterparts.** This Agreement may be executed in counterparts, each of which is hereby deemed an original, but all of which together shall constitute one and the same instrument.
- I. **Entire Agreement.** This Agreement constitutes the entire agreement between the parties, and any modification of or addition to this agreement must be in writing and signed by all parties hereto.
- J. **Authority.** The signatories to this agreement represent and warrant that they have full power and authority to enter into this Agreement on behalf of the parties indicated.
- K. **Advice of Counsel.** The parties acknowledge that they have been and are fully advised by competent legal counsel of their own choice, that they have read this entire agreement and fully understand its terms and conditions of this Agreement, and that their execution of this Agreement is with the advice of counsel and of their own free will and desire.
- L. **Binding on Successors.** This agreement shall bind and benefit the successors and assigns of CRI's facility, provided this provision should not authorize transfer of CRI's facility or permit without permission of OCD in accordance with Order No. R-9166 and Rule 711.

IN WITNESS WHEREOF, the parties have executed this Agreement by their duly authorized representatives, whose signatures appear below.

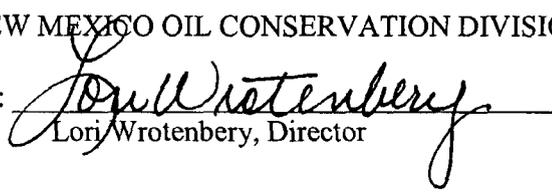
NEW MEXICO ENERGY MINERALS AND
NATURAL RESOURCES DEPARTMENT

By: _____


Joanna Prukop, Secretary

NEW MEXICO OIL CONSERVATION DIVISION

By: _____


Lori Wrotenbery, Director

NEW MEXICO OIL CONSERVATION DIVISION

By: Chris Williams
Chris Williams, District 1 Supervisor

APPROVED

By: David K. Brooks
David K. Brooks,
Special Assistant Attorney General

CONTROLLED RECOVERY INC.

By: Ken Marsh
Ken Marsh, President