

P.O. DRAWER 3337
FARMINGTON, NM 87499

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COLEMAN OIL & GAS, INC.

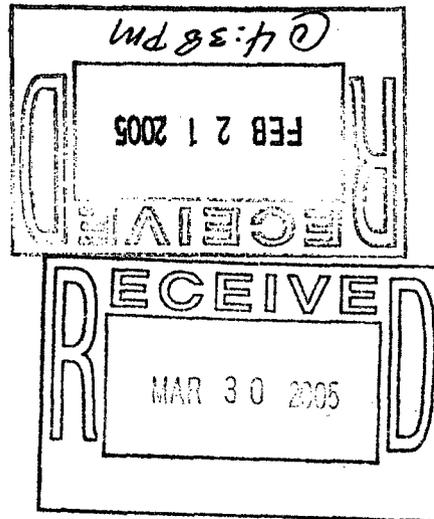
G. Chris Coleman
Vice President

VIA HAND DELIVERY

Thursday, February 17, 2005

Mr. Skip Fraker
Dugan Production Corporation
709 E Murray Drive
Farmington, NM 8701

RE: Township 24 North - Range 11 West
Section 12: NE/4
San Juan County, NM



Dear Mr. Fraker:

In reference to Coleman's recent proposal to operate our Juniper Com 32-12 well independently of Dugan's Kermit Com 90 well we believe it is in the best interest of each party to operate the well on their respective leases and within the spacing unit that would consist of the N/2 of the above referenced Section 12. Our 32-12 well fits in smoothly with our water disposal scheme, gathering facilities and overall operational logistics.

Coleman offers to reimburse Dugan for its costs of permitting the Kermit 90S well and for costs it may incur in attending the hearing at the NMOCD in this regard. If Dugan will agree to the proposed independent operation of each of the wells within the spacing unit, Coleman will agree to drill and complete its well within sixty (60) days of the change of operator. We would like to get this matter on the docket and February 22, 2005 is the day Bill Carr, with the NMOCD in Santa Fe, said will secure a near term hearing date for the matter. If Dugan will agree to the independent operation of each of our respective wells in the N/2 of said Section 12 please so indicate by signing in the space provided below and returning one original of this letter to me.

Mr. Carr stated that without positive agreement by both parties the NMOCD will not approve an arrangement in which wells can be independently operated. Short of Dugan bringing a force pooling action before the NMOCD, Coleman will not agree with the AFE's or Operating

BEFORE THE OIL CONSERVATION DIVISION
Santa Fe, New Mexico
Case No. 13460 Exhibit No. 3
Submitted by:
COLEMAN OIL & GAS INC.
Hearing Date: April 7, 2005

Mr. Skip Fraker
Thursday, February 17, 2005
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Agreement that were presented. Our partner in the acreage, EOG Resources, Inc. is in agreement with our management of this property, up to the point that they receive an offer to sell their acreage position for an amount they consider acceptable (latest market valuations are in the \$600 per acre range).

I think that the win win in this situation is for Dugan and Coleman to operate their own wells - it would make for good neighbors. Give me or Bryan Lewis a call if you want to discuss it further.

Sincerely,

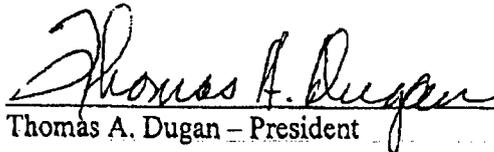


G. Chris Coleman
Vice President

GCC/bdl

YES, DUGAN PRODUCTION CORPORATION HEREBY CONSENTS TO THE INDEPENDENT OPERATION OF ITS KERMIT COM 90 WELL IN THE NW/4 BY DUGAN AND COLEMAN OIL & GAS, INC.'S JUNIPER COM 32-12 IN THE NE/4 BY COLEMAN, BEING A N/2 SPACING UNIT FOR THE FRUITLAND COAL FORMATION, ALL IN SECTION 12- TOWNSHIP 24 NORTH - RANGE 11 WEST, NMMPM, SAN JUAN COUNTY, NEW MEXICO.

DUGAN PRODUCTION CORPORATION


Thomas A. Dugan - President

Date: _____

FAXED

By: BLEWIS
Date: 02/21/05

COG-DV

@ 4:41 PM