

A.A.P.L. FORM 610 - 1989

MODEL FORM OPERATING AGREEMENT

OPERATING AGREEMENT

DATED

January 20 , 2012 ,
year

OPERATOR Burnett Oil Co., Inc.

CONTRACT AREA W/2, W/2 E/2 Sec. 12 & W/2 Sec. 13, All of Sec. 24

Township 17 South, Range 31 East N.M.P.M.

(less and except the well bore for the Hudson Oil Company of Texas – Knockabout

Federal #1 well located 1830' FSL & 1980' FWL of Section 12-T17S-R31E)

COUNTY OR PARISH OF Eddy , STATE OF New Mexico

Oil Conservation Division

Case No. 15404 + 15405

Exhibit No. 3

COPYRIGHT 1989 - ALL RIGHTS RESERVED
AMERICAN ASSOCIATION OF PETROLEUM
LANDMEN, 4100 FOSSIL CREEK BLVD.
FORT WORTH, TEXAS, 76137, APPROVED FORM.

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1 orders promulgated under such laws in reference to oil, gas and mineral operations, including the location, operation, or
2 production of wells, on tracts offsetting or adjacent to the Contract Area.

3 With respect to the operations hereunder, Non-Operators agree to release Operator from any and all losses, damages,
4 injuries, claims and causes of action arising out of, incident to or resulting directly or indirectly from Operator's interpretation
5 or application of rules, rulings, regulations or orders of the Department of Energy or Federal Energy Regulatory Commission
6 or predecessor or successor agencies to the extent such interpretation or application was made in good faith and does not
7 constitute gross negligence. Each Non-Operator further agrees to reimburse Operator for such Non-Operator's share of
8 production or any refund, fine, levy or other governmental sanction that Operator may be required to pay as a result of such
9 an incorrect interpretation or application, together with interest and penalties thereon owing by Operator as a result of such
10 incorrect interpretation or application.

11 **ARTICLE XV.**
12 **MISCELLANEOUS**

13 **A. Execution:**

14 This agreement shall be binding upon each Non-Operator when this agreement or a counterpart thereof has been
15 executed by such Non-Operator and Operator notwithstanding that this agreement is not then or thereafter executed by all of
16 the parties to which it is tendered or which are listed on Exhibit "A" as owning an interest in the Contract Area or which
17 own, in fact, an interest in the Contract Area. Operator may, however, by written notice to all Non-Operators who have
18 become bound by this agreement as aforesaid, given at any time prior to the actual spud date of the Initial Well but in no
19 event later than five days prior to the date specified in Article VI A. for commencement of the Initial Well, terminate this
20 agreement if Operator in its sole discretion determines that there is insufficient participation to justify commencement of
21 drilling operations. In the event of such a termination by Operator, all further obligations of the parties hereunder shall cease
22 as of such termination. In the event any Non-Operator has advanced or prepaid any share of drilling or other costs
23 hereunder, all sums so advanced shall be returned to such Non-Operator without interest. In the event Operator proceeds
24 with drilling operations for the Initial Well without the execution hereof by all persons listed on Exhibit "A" as having a
25 current working interest in such well, Operator shall indemnify Non-Operators with respect to all costs incurred for the
26 Initial Well which would have been charged to such person under this agreement if such person had executed the same and
27 Operator shall receive all revenues which would have been received by such person under this agreement if such person had
28 executed the same.

29 **B. Successors and Assigns:**

30 This agreement shall be binding upon and shall inure to the benefit of the parties hereto and their respective heirs,
31 devisees, legal representatives, successors and assigns, and the terms hereof shall be deemed to run with the Leases or
32 Interests included within the Contract Area.

33 **C. Counterparts:**

34 This instrument may be executed in any number of counterparts, each of which shall be considered an original for all
35 purposes.

36 **D. Severability:**

37 For the purposes of assuming or rejecting this agreement as an executory contract pursuant to federal bankruptcy laws,
38 this agreement shall not be severable, but rather must be assumed or rejected in its entirety, and the failure of any party to
39 this agreement to comply with all of its financial obligations provided herein shall be a material default.

40 **ARTICLE XVI.**
41 **OTHER PROVISIONS**

42
43 **A. Conflicts.** In the event of a conflict between any provision of this Article XVI and other provisions of
44 this agreement, this Article XVI shall control and prevail.

45
46 **B. Other Subsequent Operations:**

47 1. Proposals under Article VI.B to drill other wells (i.e., any well other than the Initial Well), or to
48 rework, sidetrack, deepen, recomplete or plug back an existing well not then capable of production in
49 paying quantities, may be:

- 50 a. By the Operator; or
51
52 b. By any non-operator with the approval of the Operator; or
53
54 c. By unanimous approval of all non-operators, without the approval of Operator.

55 2. Any well or operation properly proposed under this article shall be subject to the subsequent
56 operation provisions of Article VI.B., above, including the non-consent election and penalties, except
57 that the penalty for an election not to participate in the drilling of the first well on a drilling or
58 spacing unit shall be the forfeiture of any non-consenting party's interest in the well and the drilling
59 or spacing unit for the well, limited to the depths covered by this agreement, to the participating
60 parties, in proportion to their interests.

61 **C. Priority of Proposals and Operations.** When the participating parties cannot agree on the sequence of
62 further operations in any well operated under this agreement as a result of conflicting or competing proposals
63 made in accordance with Article VI, the proposals shall be considered and the prevailing proposal determined
64 in the following priority:

- 65 1st additional logging, coring or testing;
66 2nd completion attempt at the objective Zone;
67 3rd plugging back and completion attempts at shallower depths, in order from the
68 deepest to the shallowest depths;
69 4th deepenings, in order from the shallowest to the deepest
70 depths;
71 5th sidetracking; and/or
72 6th plugging and abandonment.

73 If at any time when proposals of any of the above operations are being considered, the hole or
74 equipment is in such a condition that Operator recommends not to conduct one or more particular operations

1 because they might put the hole, equipment and/or objective formation in jeopardy or result in the loss of
2 either of them, such proposals shall be eliminated from the above order of priority. With regard to proposals
3 for additional logging, coring or testing, if any, but not all, of the parties entitled to make elections to the
4 proposals elect to pay the costs thereof they may do so, and the only penalty to any party that elects not to pay
5 such costs is that it shall not be entitled to the corresponding logs, cores or results of tests or any analyses of
6 them without the consent of all parties who participated in the additional logging, coring or testing.

7 **D. Commencement of Operations.** For the purposes of Articles VI.B.1 and VI.B.2, Operator may
8 commence activities preliminary to actual drilling operations including, without limitation, building location,
9 roads and pits, delivering materials and equipment to the well site, rigging up a drilling rig, and/or actual
10 drilling operations at any time either before or after giving the notice of proposed operations required by said
11 Articles. Notwithstanding the foregoing, the parties receiving notice of proposed operations pursuant to
12 Articles VI.B.1 and VI.B.2 shall have the full time allowed in which to make their election(s) and shall be
13 subject to the non-consent provisions thereof to the same extent and in the same manner as provided in Article
14 VI.B without reference to the time that such activities were commenced relative to giving notice.

15 **E. Ard Term Assignment:** COG Operating, LLC's ("COG") working interest in the Contract Area is
16 derived under a term assignment dated effective April 1, 2011, by and between the Ard Energy Group, LTD
17 and Ard Oil, LTD, as assignors, and COG, as assignee (the "Ard TA"). COG acknowledges that Operator is
18 under no obligation to drill wells on the Contract Area at any pace specified by the Ard TA's continuous
19 development provisions. Further, if the Ard TA shall expire with respect to any of Contract Area, the Parties
20 hereto agree that the subsequent treatment of the Ard working interest in the Contract Area shall be governed
21 by the following terms and agreements: (1) Such loss shall be the sole loss of COG but COG's interest will not
22 be reduced in any lands in which it has already earned an interest under the Ard TA at the time of such
23 termination; (2) The parties hereto, other than COG, will not attempt to obtain an assignment of Ard's
24 working interest in the Contract Area in which such interest has lapsed; (3) If and to the extent COG obtains a
25 new assignment on such lands, those lands will again be covered by the JOA; (4) If and to the extent COG has
26 not obtained a new assignment covering Ard's working interest in the Contract Area at the time the Operator
27 shall propose a well which includes any of such lapsed lands within its drilling or spacing unit, then the
28 Operator will initiate a compulsory pooling application with the New Mexico OCD with respect to such
29 interest and such well, and promptly after obtaining an order pooling such interest, and Ard's election not to
30 participate, offer such interest to all parties hereto that own a working interest in the well and its drilling or
31 spacing unit, in proportion to their interests. Each party receiving such offer shall have fifteen (15) days from
32 receipt thereof (48 hours, including Saturdays, Sundays and legal holidays, (if a drilling rig is on location) to
33 elect to take its prorata share of such interest. Failure of a party to timely respond shall be deemed as an
34 election by such party not to take its prorata share of such interest.

35 **F. Hearing Costs:** Should it be necessary to conduct hearings before governmental agencies for the
36 securing of spacing or pooling orders or for certifying the classification of a well for any governmental purpose
37 or any other matters for the benefit of the Contract Area, the costs attributable to such hearings as well as fees
38 paid attorneys and witnesses, shall be borne by the Drilling Parties in the proportion that the interest of each
39 Drilling Party bears to the total interest of all Drilling Parties as such interests appear in Exhibit "A", and any
40 such pooled interest shall be owned by the Drilling Parties in such proportions.

41 **G. Proceeds Paid to Operator:** Operator shall arrange for the sale of all hydrocarbons produced, saved
42 and sold from the Contract Area to an unaffiliated third party purchaser in an "arms length" transaction and
43 the proceeds shall be paid to Operator by all purchasing companies purchasing such hydrocarbons and by the
44 execution of this Agreement, the Non-Operators covenant and agree to save all purchasing companies harmless
45 from any and all liability by reason of paying any such proceeds to Operator. Operator shall disburse such
46 proceeds to all parties entitled to share in such proceeds according to the New Mexico Oil and Gas Proceeds
47 Payment Act. Further, Non-Operators authorize and direct Operator to deduct from their proportionate share
48 of such proceeds for such expenses owed to Operator if such expenses owed to Operator become delinquent for
49 more than one hundred twenty (120) consecutive days and Operator shall remit the balance of the proceeds
50 from such sale to Non-Operators.

51 **H. Amendment of Operating Agreement.** Except as provided in Article XVI.E, this agreement may be
52 amended only by a written document that is specific in stating that it is an amendatory document to this
53 agreement and is executed by authorized representatives of each party hereto. All replacement pages to this
54 agreement which result from actions authorized under Article XVI.E, or an amendment as provided herein,
55 will be clearly marked as replacement pages and set forth the date of such amendment or replacement.

56 **I. Separate Measurement Facilities.** If any party hereto creates the necessity of separate measurement
57 facilities by reason of assignments or other mortgages or conveyances within the Contract Area, such party
58 shall alone bear the entire costs of purchasing, installing, and operating such separate measurement facility,
59 which facility may be constructed and operated by Operator, at Operator's election, for the account of said
60 party and shall be subject to all other provisions of this Operating Agreement including, without limitation,
61 those provisions relating to advances for costs and offsets for unpaid expenses.

62 **J. Bankruptcy.** If following the granting of relief under the Bankruptcy Code to any party hereto as
63 debtor thereunder, this agreement should be held to be an executory contract within the meaning of 11 U.S.C.
64 Section 365, then the Operator or, if the Operator is the debtor in bankruptcy, the other parties, shall be
65 entitled to a determination by the debtor or any trustee of the debtor within thirty (30) days from the date an
66 order for relief is entered under the Bankruptcy Code, as to the rejection or assumption of this agreement. In
67 the event of an assumption, Operator or the other parties shall be entitled to adequate assurances as to future
68 performance of debtor's obligations hereunder and the protection of the interests of all other parties.

69 **K. Security.** The lien and security interest granted by each Non-Operator to Operator, and by Operator
70 to the Non-Operators, under Article VII.B shall extend not only to such party's oil and gas rights in the
71 Contract Area (which for greater certainty shall include all of each party's leasehold interest and leasehold
72 estate in the Contract Area), the oil and/or gas when extracted, and equipment (as mentioned in said Article),
73 but also to all accounts, contract rights, inventory, and general intangibles constituting a part of, relating to, or
74 arising out of said oil and gas rights, extracted oil and gas, and said equipment or which are otherwise owned

1 or held by any such party in the Contract Area. Further, the lien and security interest of each of said parties
2 shall extend to all proceeds and products of all of the property and collateral described in this paragraph and
3 in Article VII.B as being subject to said lien and security interest.

4 **L. Interpretation.** This agreement shall never be construed for or against any party on the basis of which
5 party drafted this agreement or any particular provision herein, or which party supplied the form of
6 Operating Agreement. Each party agrees that this agreement has been purposefully drawn and correctly
7 reflects its understanding of the transaction that it contemplates.

8
9 **M. Covenants Running with Land/ Effect of Transfer.** The terms, covenants, and conditions of this
10 agreement shall be covenants running with the lands covered hereby and leasehold estates therein and with
11 each transfer or assignment of said lands or leasehold estates. Any assignment, conveyance or other transfer of
12 an Oil and Gas Lease or Oil and Gas Interest that is subject to this agreement shall relieve the transferor from
13 liability for the cost and expense of operations attributable to the transferred interest which are conducted
14 after the effective date thereof; provided that, the transferor shall remain liable for and shall cause to be paid
15 its proportionate part of the cost and expense of all operations for which it was obligated to pay and were
16 commenced prior to the actual transfer, except costs and expenses arising out of or directly related to a specific
17 operation in which the transferor elected (or was deemed to have elected) not to participate pursuant to Article
18 VI. From and after the effective date of the said assignment, conveyance or other transfer, the transferee shall
19 be deemed to be a party to this agreement, subject to the performance of all obligations attributable to the
20 transferred interest for all periods from and after the effective date of transfer. The assumption of liability by a
21 transferee, pursuant to the foregoing, shall operate to terminate prospective liability of the transferring party
22 for all periods subsequent to the later of the actual date of transfer or the effective date of transfer, but shall in
23 no event limit, diminish, or affect the direct and continuing liability of the transferring party under this
24 agreement and applicable law for all periods prior to such date.

25 **N. Knockabout Federal No. 1:** The Hudson Oil Company of Texas – Knockabout Federal No. 1 Well
26 (the “Knockabout Well”) is a producing well located in Unit K of Section 12-T17S-R31E, which is operated
27 pursuant to a certain Operating Agreement dated October 1, 2004, between Hudson Oil Company of Texas, as
28 operator, and Marbob Energy Corporation, et al., as non-operators (the “Knockabout JOA”). The wellbore
29 for the Knockabout Well is specifically excluded from the Contract Area. The parties hereto agree that this
30 Operating Agreement dated January 20, 2012 shall supersede and replace the Knockabout JOA with respect
31 to the Glorieta/Yeso formations underlying all lands covered by the Knockabout JOA, save and except for the
32 Glorieta/Yeso formations in the wellbore of the Knockabout Federal No. 1 Well, and the Knockabout JOA
33 shall continue to govern operations with respect to the Knockabout Well and depths below the Glorieta/Yeso
34 formations in all lands covered by the Knockabout JOA.

35 **O. Burnett Oil Co., Inc. as Operator:** Burnett Oil Co., Inc., is a Texas corporation and is the Operator.
36 Burnett Oil Company is a Texas general partnership and is the owner of leasehold interests in the Contract
37 Area. If Burnett Oil Company shall cease to own a leasehold interest in the Contract Area, then Burnett Oil
38 Co., Inc. shall cease to be Operator without any action necessary by the remaining Parties, except for the
39 selection of a successor Unit Operator as provided for herein.

40 **P. Relationship of Parties.** Except as it relates to handling of funds as specified in Article V.D.4, the
41 parties shall not be considered fiduciaries or to have established a confidential relationship but rather the
42 parties shall be free to act on an arms-length basis in accordance with their own respective self-interests.

43 **Q. Severability.** In the event any provision contained herein should be deemed inconsistent with or
44 contrary to any Federal, State, or Municipal law, rule or regulation, said provision shall be deemed to be
45 modified to the extent required to comply with said law, rule or regulation and as so modified said provision in
46 this Agreement shall continue in full force and effect without affecting the enforceability of the remaining
47 provisions, duties, and liabilities set forth herein.
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1 IN WITNESS WHEREOF, this agreement shall be effective as of the 20th day of January
2 2012

3 _____ who has prepared and circulated this form for execution, represents and warrants
4 that the form was printed from and, with the exception(s) listed below, is identical to the A.A.P.L. Form 610-1989 Model Form
5 Operating Agreement, as published in computerized form by Forms On A Disk, Inc. No changes, alterations, or
6 modifications, other than those made by strikethrough and/or insertion and that are clearly recognizable as changes in
7 Articles _____, have been made to the form.

6 ATTEST OR WITNESS:

OPERATOR

7 _____
8 _____
9 _____

By Burnett Oil Co., Inc.
William D. Pollard
Type or print name

Title President

Date 1-19-2012

Tax ID or S.S. No. _____

15 NON-OPERATORS

16 _____
17 _____
18 _____

By Burnett Oil Company
Burnett Oil Co., Inc., Managing General Partner
William D. Pollard
Type or print name

Title President

Date 1-19-2012

Tax ID or S.S. No. _____

24 _____
25 _____
26 _____

By Jayclina Partners
E. Randall Hudson III
Type or print name

Title Managing General Partner

Date 1-19-2012

Tax ID or S.S. No. _____

31 _____
32 _____
33 _____

By Zorro Partners, Ltd.
E. Randall Hudson III
Type or print name

Title Attorney-In-Fact

Date 1-19-2012

Tax ID or S.S. No. _____