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June 5, 2008

Via fax

David K. Brooks
Oil Conservation Division
1220 South St. Francis Drive
Santa Fe, New Mexico 87505

Re: Case No. 14115/T.H. McElvain Oil & Gas Limited Partnership

Dear Mr. Brooks:

Enclosed is the proposed order of T.H. McElvain Oil & Gas Limited Partnership. The order is also being e-mailed to you.

Please note that, as discussed at the hearing, applicant has a City of Farmington permit that expires in a week, and applicant requests a prompt decision. If a final order cannot be entered in that time frame, applicant requests that an interim order be entered so that applicant can commence operations.

Very truly yours,

James Bruce

Attorney for T.H. McElvain Oil & Gas Limited Partnership

cc: W. Thomas Kellahin w/encl.

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

IN THE MATTER OF THE HEARING CALLED BY THE OIL CONSERVATION DIVISION FOR THE PURPOSE OF CONSIDERING:

CASE NO. 14115
ORDER NO. R-

APPLICATION OF T.H. MCELVAIN OIL & GAS LIMITED PARTNERSHIP FOR COMPULSORY POOLING, SAN JUAN COUNTY, NEW MEXICO.

APPLICANT'S PROPOSED ORDER OF THE DIVISION

BY THE DIVISION:

This case came on for hearing on May 1, 2008 at 8:15 a.m. at Santa Fe, New Mexico, before Examiners William R. Jones and David K. Brooks

NOW, on this _____ day of June, 2008, the Division Director, having considered the testimony, the record, and the recommendations of the Examiners,

FINDS THAT:

(1) Due public notice has been given, and the Division has jurisdiction of this case and of the subject matter.

(2) The applicant, T.H. McElvain Oil & Gas Limited Partnership ("applicant"), seeks an order pooling all uncommitted mineral interests from the surface to the base of the Fruitland Coal formation underlying Lots 1-4 and the S/2N/2 (the N/2) of Section 1, Township 29 North, Range 13 West, NMPM, San Juan County, New Mexico, to form a standard 319.40-acre spacing and proration unit for all formations and/or pools developed on 320 acre spacing within that vertical extent, including the Basin Fruitland Coal Gas Pool.

(3) The above-described unit (the "Unit") is to be dedicated to applicant's Hutchinson Well No. 2, which is to be drilled at an orthodox location in Lot 3 (Unit C) of Section 1.

(4) Two or more separately owned tracts are embraced within the Unit, and/or there are royalty interests and/or undivided interests in oil and gas minerals in one or more tracts included in the Unit that are separately owned.

(5) Applicant is an owner of an oil and gas working interest within the Unit. Applicant has the right to drill and proposes to drill its Hutchinson Well No. 2 at an orthodox well location.

(6) There are interest owners in the proposed Unit who have not agreed to pool their interests.

(7) ConocoPhillips Company ("ConocoPhillips), a working interest owner in the Unit, entered an appearance in this case and presented evidence.

(8) In this case, applicant incurred approximately $85,000 in abstract and title opinion costs. ConocoPhillips asserts that these costs are not well costs which should be included in an authorization for expenditure, and which may be recovered by an operator in a compulsory pooling case. ConocoPhillips does not otherwise object to the granting of the application.

(9) Applicant presented evidence which showed that:

(a) The N/2 of Section 1 is within the City of Farmington, and contains 48 separate mineral tracts.

(b) Applicant has a City of Farmington permit to drill the Hutchinson Well No. 2, which expires on June 12, 2008.

(c) Applicant first began preparations to drill this well in 2006. Applicant requested copies of prior opinions from ConocoPhillips, but ConocoPhillips refused this request. A title opinion was completed for applicant in early 2007, and applicant proposed the well to ConocoPhillips in July 2007.

(d) In August 2007 ConocoPhillips informed applicant that it desired to join in the well, and asked applicant for an invoice on the title opinion so that it could pay its proportionate share of those costs. After being notified of the opinion costs, it then asserted that they were not proper well costs.

(e) Applicant and ConocoPhillips have agreed on a form of joint operating agreement, which has not been executed due to the dispute over title opinion costs.

(f) It is industry-standard practice to include title opinion costs as part of well costs.

(g) Title opinion costs are normally recoverable under a joint operating agreement.

(h) A title opinion was required so that applicant knew the working interest owners and their ownership percentages in the proposed well. An operator must determine ownership in order to proceed with preparation of a joint operating

agreement, or with pooling under the compulsory pooling statute, NMSA 1978 §§70-2-17.C.

(i) Upon completing a well as a producer, the operator needs a title opinion to properly pay production proceeds to all interest owners in a well. An operator is required to pay interest owners under the Oil and Gas Proceeds Payment Act, NMSA 1978 §§70-10-1 *et seq.*

(j) An operator also needs to determine the ownership of the surface estate of the well site in order to comply with the Surface Owners Protection Act, NMSA 1978 §§70-12-1 *et seq.*

(10) Based upon the evidence, the Division finds that:

(a) Title opinion costs are well costs which are recoverable by an operator under a pooling order.

(b) Although ConocoPhillips presented some testimony at hearing as to the reasonableness of applicant's title opinion costs, ConocoPhillips did not raise this issue in its pre-hearing statement. Therefore, this issue should not be addressed until after the well is drilled, pursuant to Ordering Paragraph (9) below.

(11) To avoid the drilling of unnecessary wells, protect correlative rights, prevent waste, and afford to the owner of each interest in the Unit the opportunity to recover or receive without unnecessary expense its just and fair share of hydrocarbons, this application should be approved by pooling all uncommitted interests, whatever they may be, in the oil and gas within the Unit.

(12) McElvain Oil & Gas Properties, Inc. should be designated the operator of the subject well and of the Unit.

(13) Any pooled working interest owner who does not pay its share of estimated well costs should have withheld from production its share of reasonable well costs plus an additional 200% (pursuant to Rule 35.A) thereof as a reasonable charge for the risk involved in drilling the well.

(14) Reasonable charges for supervision (combined fixed rates) should be fixed at $5500.00 per month while drilling and $550.00 per month while producing, provided that these rates should be adjusted annually pursuant to Section III.1.A.3. of the COPAS form titled "*Accounting Procedure-Joint Operations.*"

IT IS THEREFORE ORDERED THAT:

(1) Pursuant to the application of T.H. McElvain Oil & Gas Limited Partnership, all uncommitted mineral interests in all formations from the surface to the base of the Fruitland Coal formation underlying Lots 1-4 and the S/2N/2 (the N/2) of Section 1, Township 29 North, Range 13 West, NMPM, San Juan County, New Mexico, are hereby pooled to form a standard 319.40-acre gas spacing and proration unit for all formations and/or pools developed on 320 acre spacing within that vertical extent. The above-described unit (the "Unit") is to be dedicated to applicant's Hutchinson Well No. 2, to be drilled at an orthodox location in Lot 3 (Unit C) of Section 1, to test any and all formations from the surface to the base of the Fruitland Coal formation.

(2) McElvain Oil & Gas Properties, Inc. is hereby designated the operator of the subject well and of the Unit.

(3) The operator of the Unit shall commence drilling the proposed well on or before October 1, 2008 and shall thereafter continue drilling the well with due diligence to test the Basin-Fruitland Coal Gas Pool.

(4) In the event the operator does not commence drilling the proposed well on or before October 1, 2008, Ordering Paragraph (1) shall be of no effect, unless the operator obtains a time extension from the Division Director for good cause.

(5) Should the subject well not be drilled and completed within 120 days after commencement thereof, Ordering Paragraph (1) shall be of no further effect, and the Unit created by this Order shall terminate unless the operator appears before the Division Director and obtains an extension of time to complete the well for good cause demonstrated by satisfactory evidence.

(6) Upon final plugging and abandonment of the subject well, the pooled Unit created by this Order shall terminate, unless this order has been amended to authorize further operations.

(7) After pooling, uncommitted working interest owners are referred to as pooled working interest owners. ("pooled working interest owners" are owners of working interests in the Unit, including unleased mineral interests, who are not parties to an operating agreement governing the Unit.) After the effective date of this order, the operator shall furnish the Division and each known pooled working interest owner in the Unit an itemized schedule of estimated costs of drilling, completing and equipping the subject well ("well costs").

(8) Within 30 days from the date the schedule of estimated well costs is furnished, any pooled working interest owner shall have the right to pay its share of estimated well costs to the operator in lieu of paying its share of reasonable well costs out of production as hereinafter provided, and any such owner who pays its share of estimated well costs as provided above shall

remain liable for operating costs but shall not be liable for risk charges. Pooled working interest owners who elect not to pay their share of estimated well costs as provided in this paragraph shall thereafter be referred to as "non-consenting working interest owners."

(9) The operator shall furnish the Division and each known pooled working interest owner (including non-consenting working interest owners) an itemized schedule of actual well costs within 90 days following completion of the proposed well. If no objection to the actual well costs is received by the Division, and the Division has not objected within 45 days following receipt of the schedule, the actual well costs shall be deemed to be the reasonable well costs. If there is an objection to actual well costs within the 45-day period, the Division will determine reasonable well costs after public notice and hearing. The issue of the reasonableness of applicant's title opinion costs is reserved until that time.

(10) Within 60 days following determination of reasonable well costs, any pooled working interest owner who has paid its share of estimated costs in advance as provided above shall pay to the operator its share of the amount that reasonable well costs exceed estimated well costs and shall receive from the operator the amount, if any, that the estimated well costs it has paid exceed its share of reasonable well costs.

(11) The operator is hereby authorized to withhold the following costs and charges from production:

(a) the proportionate share of reasonable well costs attributable to each non-consenting working interest owner; and

(b) as a charge for the risk involved in drilling the well, 200% of the above costs.

(12) The operator shall distribute the costs and charges withheld from production, proportionately, to the parties who advanced the well costs.

(13) Reasonable charges for supervision (combined fixed rates) are hereby fixed at $5500.00 per month while drilling and $550.00 per month while producing, provided that these rates shall be adjusted annually pursuant to Section III.1.A.3. of the COPAS form titled "*Accounting Procedure-Joint Operations.*" The operator is authorized to withhold from production the proportionate share of both the supervision charges and the actual expenditures required for operating the well, not in excess of what are reasonable, attributable to pooled working interest owners.

(14) Except as provided in Ordering Paragraphs (11) and (13) above, all proceeds from production from the well that are not disbursed for any reason shall be placed in escrow in San Juan County, New Mexico, to be paid to the true owner thereof upon demand and proof of

ownership. The operator shall notify the Division of the name and address of the escrow agent within 30 days from the date of first deposit with the escrow agent.

(15) Any unleased mineral interest shall be considered a seven-eighths (7/8) working interest and a one-eighth (1/8) royalty interest for the purpose of allocating costs and charges under this order. Any well costs or charges that are to be paid out of production shall be withheld only from the working interests' share of production, and no costs or charges shall be withheld from production attributable to royalty interests.

(16) Should all the parties to this compulsory pooling order reach voluntary agreement subsequent to entry of this order, this order shall thereafter be of no further effect.

(17) The operator of the well and the Unit shall notify the Division in writing of the subsequent voluntary agreement of all parties subject to the forced pooling provisions of this order.

(18) Jurisdiction of this case is retained for the entry of such further orders as the Commission may deem necessary.

DONE at Santa Fe, New Mexico, on the day and year hereinabove designated.

STATE OF NEW MEXICO
OIL CONSERVATION DIVISION

MARK E. FESMIRE, PE
Director

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