

**PAUL BACA PROFESSIONAL COURT REPORTERS**

**OIL CONSERVATION  
DIVISION**

**EXHIBIT**

**3**

UNIT OPERATING AGREEMENT  
WEST LOCO HILLS GRAYBURG NO. 4 SAND UNIT  
COUNTY OF EDDY  
STATE OF NEW MEXICO

Oil Conservation Division  
Case No. 3  
Exhibit No. 3

UNIT OPERATING AGREEMENT  
WEST LOCO HILLS GRAYBURG NO. 4 SAND UNIT  
COUNTY OF EDDY  
STATE OF NEW MEXICO

TABLE OF CONTENTS

<u>Section</u>	<u>Page</u>
Preliminary Recitations	1
ARTICLE 1 CONFIRMATION OF UNIT AGREEMENT	
	1
ARTICLE 2 EXHIBITS	
2.1 Exhibits	2
2.2 Revision of Exhibits	2
ARTICLE 3 SUPERVISION OF OPERATIONS BY WORKING INTEREST OWNERS	
3.1 Overall Supervision	2
3.2 Specific Authorities and Duties of Working Interest Owners	2
ARTICLE 4 MANNER OF EXERCISING SUPERVISION	
4.1 Designation of Representative and Appointment of Operating Committee	4
4.2 Meetings	5
4.3 Voting Procedure	5
ARTICLE 5 INDIVIDUAL RIGHTS OF WORKING INTEREST OWNERS	
5.1 Reservation of Rights	7
5.2 Specific Rights	7
5.3 Participating Interest	7
5.4 Apportionment of Cost and Benefit	8
ARTICLE 6 UNIT OPERATOR	
6.1 Initial Unit Operator	8
6.2 Resignation and Removal, and Successor	8
ARTICLE 7 AUTHORITIES AND DUTIES OF UNIT OPERATOR	
7.1 Exclusive Right to Operate Unit	8
7.2 Workmanlike Conduct	9
7.3 Liens and Encumbrances	9

<u>Section</u>	Cont'd.- ARTICLE 7	<u>Page</u>
7.4	Employees	9
7.5	Records	9
7.6	Reports to Working Interest Owners	9
7.7	Reports to Governmental Authorities	9
7.8	Engineering and Geological Information	9
7.9	Expenditures	9
7.10	Wells Drilled by Unit Operator	9
7.11	Water Supply	10
7.12	Fair Employment	10
7.13	Mathematical Errors	10
ARTICLE 8 TAXES		
8.1	Ad Valorem Taxes	10
8.2	Other Taxes	11
ARTICLE 9 INSURANCE		
		11
ARTICLE 10 ADJUSTMENT OF INVESTMENTS		
10.1	Personal Property Taken Over	11
10.2	Inventory and Evaluation of Personal Property	12
10.3	Initial Investment Adjustment	12
10.4	General Facilities	12
10.5	Ownership of Personal Property and Facilities	12
10.6	Investment Adjustment on Enlargement of Participating Area	13
ARTICLE 11 UNIT EXPENSE		
11.1	Basis of Charge to Working Interest Owners	13
11.2	Budgets	13
11.3	Advance Billings	13
11.4	Commingling of Funds	13
11.5	Lien of Unit Operator	13
11.6	Unpaid Unit Expenses	14
11.7	Royalties and Compensatory Royalties	14
11.8	Construction of Plants and Special Facilities	15
11.9	Gauge of Tanks	15
ARTICLE 12 NON-UNITIZED FORMATIONS AND NON-PARTICIPATING ACREAGE		
12.1	Right to Operate	15
12.2	Damage to Well Producing from Non-Unitized Formations	15
12.3	Wells Outside Participating Area	16

<u>Section</u>		<u>Page</u>
	ARTICLE 13 TITLES	
13.1	Warranty and Indemnity	18
13.2	Failure Because of Unit Operations	18
13.3	Rentals	18
	ARTICLE 14 LIABILITY, CLAIMS AND SUITS	
14.1	Individual Liability	19
14.2	Settlements	19
14.3	Force Majeure	19
14.4	Regulations	20
	ARTICLE 15 INTERNAL REVENUE PROVISION	20
	ARTICLE 16 NOTICES	21
	ARTICLE 17 WITHDRAWAL OF WORKING INTEREST OWNERS	21
	ARTICLE 18 ABANDONMENT OF WELLS	21
18.1	Rights of Former Owners	21
18.2	Plugging	22
	ARTICLE 19 EFFECTIVE DATE AND TERM	
19.1	Effective Date	22
19.2	Term	22
	ARTICLE 20 ABANDONMENT OF OPERATIONS	22
	ARTICLE 21 EXECUTION	
21.1	Original Counterpart, or Other Instrument	23
21.2	Execution	23
	ARTICLE 22 SUCCESSORS AND ASSIGNS	
22.1	Successors and Assigns	23
22.2	Creation of New Interest	24
	<u>EXHIBITS</u>	
	Exhibit C - Accounting Schedule	
	Exhibit D - Insurance Provisions	

UNIT OPERATING AGREEMENT  
WEST LOCO HILLS GRAYBURG NO. 4 SAND UNIT  
COUNTY OF EDDY  
STATE OF NEW MEXICO

THIS AGREEMENT, entered into as of the 17th day of September, 1962, (and as revised on April 25, 1963) by the parties who have signed the original of this instrument, a counterpart thereof, or other instrument agreeing to be bound by the provisions hereof;

W I T N E S S E T H:

WHEREAS, concurrently herewith, the parties hereto have entered into a certain Unit Agreement for the development and operation of the West Loco Hills Grayburg No. 4 Sand Unit Area, hereinafter referred to as the "Unit Agreement", which said agreement and this agreement embrace the area specified on the attached map, marked Exhibit "A", hereinafter referred to as the "Unit Area", containing 5,307.73 acres, more or less, situated in Eddy County, New Mexico; and,

WHEREAS, the parties hereto hereby make and enter into this agreement pursuant to Section 10 of said Unit Agreement;

NOW THEREFORE, in consideration of the mutual agreements herein set forth, it is agreed as follows:

ARTICLE 1

CONFIRMATION OF UNIT AGREEMENT

1.1 Confirmation of Unit Agreement. The Unit Agreement is hereby confirmed and by reference made a part of this agreement. The definitions in the Unit Agreement are adopted for all purposes of this agreement. If there is any conflict between the Unit Agreement and this agreement, the Unit Agreement shall govern; and further, the parties hereto recognize the existence of that certain Agreement dated April 1, 1958, between the Loco Hills Pressure Maintenance Association, Inc., as "Association", The Individual Stockholders of the Loco Hills Pressure Maintenance Association, Inc., as "Operators", and Valley Gas Corporation, as "Valley". The unitization of gas in the Loco Hills Grayburg No. 4 Sand under this Unit Operating Agreement and the Unit Agreement is subject to all of the rights and privileges held by Valley Gas Corporation under said Agreement of April 1, 1958.

## ARTICLE 2

### EXHIBITS

2.1 Exhibits. The Following exhibits are incorporated herein by reference:

2.1.1 Exhibits "A" and "B" of the Unit Agreement.

2.1.2 Exhibit "C", attached hereto, which is the Accounting Procedure applicable to Unit Operations. If there is any conflict between this agreement and Exhibit "C", this agreement shall govern.

2.1.3 Exhibit "D", attached hereto, which contains insurance provisions applicable to Unit Operations.

2.2 Revision of Exhibits. Exhibit "B", or a revision thereof, shall not be conclusive as to the information therein except it may be used as showing the Participating Interests of the Working Interest Owners for the purpose of this agreement until it is shown to be in error or is revised as authorized by said Unit Agreement and by this agreement. Unit Operator shall also revise Exhibits "A" and "B" from time to time as may be required in the opinion of the Operator.

## ARTICLE 3

### SUPERVISION OF OPERATIONS BY WORKING INTEREST OWNERS

3.1 Overall Supervision. The Representatives as designated in 4.1 hereafter shall exercise overall supervision and control of all matters pertaining to Unit Operations, subject to such control given to Unit Operator as is elsewhere provided in this agreement and the Unit Agreement. The term "Unit Operations", as used herein, shall mean all operations conducted for Working Interest Owners by Unit Operator within the Unit Area pursuant to this agreement and the Unit Agreement for or on account of development and operations of the Unitized Formation for the production of Unitized Substances.

3.2 Specific Authorities and Duties of Working Interest Owners. The matters with respect to which the Working Interest Owners shall decide and take action shall include, but not be limited to, the following:

3.2.1 Method of Operation. The method of operation, including any type of pressure maintenance, secondary recovery, or other recovery program to be employed.

3.2.2 Drilling of Wells. Except where otherwise expressly provided herein, the drilling of any well, whether for production of Unitized Substances, for use as an injection well or for other purposes.

3.2.3 Well Recompletions or Abandonments. The recompletion or abandonment of any well in the Unit Area.

3.2.4 Expenditures. The making of any single expenditure in excess of Five Thousand Dollars (\$5,000.00); provided that, approval by Working Interest Owners of the drilling, reworking, deepening or plugging back of any well shall include approval of all necessary expenditures required therefor, and for completing, testing, and equipping the same, including necessary flow lines, separators and lease tankage.

3.2.5 Disposition of Unit Equipment. The selling or otherwise disposing of any major item of surplus Unit Equipment, if the current list price of new equipment similar thereto is Two Thousand Five Hundred Dollars (\$2,500.00) or more.

3.2.6 Appearance Before a Court or Regulatory Agency. The designating of a representative to appear before any court or regulatory agency in matters pertaining to Unit Operations; provided that, such designation shall not prevent any Working Interest Owner from appearing in person or from designating another representative in its own behalf.

3.2.7 Audits. The auditing of the accounts of Unit Operator pertaining to Unit Operations hereunder, provided that, the audits shall

- (a) not be conducted more than once each year except upon the resignation or removal of Unit Operator,
- (b) be made at the expense of all Working Interest Owners including the Working Interest Owner designated as Unit Operator, and

(c) be made upon not less than thirty (30) days' written notice to Unit Operator.

3.2.8 Inventories. The taking of periodic inventories under the terms of Exhibit "C".

3.2.9 Technical Services. The authorizing of charges to the joint account for services by consultants in excess of \$5,000.00 in any calendar year.

3.2.10 Assignments to Committees. The appointment of committees to study any problems in connection with Unit Operations.

3.2.11 The removal of Unit Operator and the selection of a successor as provided in the Unit Agreement.

3.2.12 The enlargement of the Unit Area or the Participating Area as provided in the Unit Agreement.

3.2.13 The adjustment and readjustment of investments.

3.2.14 The termination of the Unit Agreement.

3.2.15 Development Plan. The adoption or submission of any operating and development plan to the Supervisor or the Commissioner or to the Commission.

3.2.16 Subsequent Joinder. The subsequent joinder of any Working Interest or Royalty Interest Owner in the Unit Agreement or in this agreement and the determination and revision of the percentage participation to be assigned to any tract included within the Participating Area.

3.2.17 Revision of the Accounting Procedure. The revision or amendment of the overhead rates or any other provision in the Accounting Procedure attached hereto as Exhibit "C".

#### ARTICLE 4

##### MANNER OF EXERCISING SUPERVISION

4.1 Designation of Representative and Appointment of Operating Committee. Where the Working Interest Owner is other than an individual, such Working Interest Owner shall in writing keep informed the Unit Operator of the name and address of the person who is authorized to represent and bind such Working Interest Owner with respect to Unit Operations; and provided further, the Operator of each tract within the Unit

Area, as recognized prior to the approval of this Unit shall act as Representative for all the Working Interest Owners in each individual tract and by signature hereto, each Working Interest Owner, herein appoints the "Operator" of each tract under which he or it owns a working interest as his or its Representative with full authority to bind all the Working Interest Owners on all matters recited in Article 3 above, and such other matters as are herein specified, provided however, the appointment of "Operator" as herein provided may be revoked and rescinded at any time upon written notice to Unit Operator and thereafter, the Working Interest Owner who revokes this delegation of authority to his Operator shall act in his own behalf and shall be designated a "Representative" for purposes of this agreement.

After final approval of this Agreement by all the Working Interest Owners, the Representatives shall promptly name from their own group a permanent Operating Committee with membership composed of such Representatives as they select who will be able to meet with the Unit Operator from time to time to gather and analyze information so that the Representatives will be well informed and advised when exercising supervision of Unit activities. The Operating Committee shall be solely responsible to the Representatives who may from time to time delegate such power and authority as they deem appropriate to carry on the business of the Unit for the benefit of the Working Interest Owners. The Representatives will keep the Unit Operator advised in writing as to the names of the Representatives composing the Operating Committee. The membership of the Operating Committee may be changed by the Representatives from time to time as they may desire by a majority vote of the Representatives. Any such changes shall be brought to the attention of the Unit Operator by written notice.

**4.2 Meetings.** All meetings of Representatives of Working Interest Owners shall be called by Unit Operator upon its own motion or at the request of one or more Working Interest Owners having a total Participating Interest of not less than ten percent (10%). No meeting shall be called with less than seven (7) days' advance written notice to the designated Representatives of the Working Interest Owners with agenda for the meeting attached. Working Interest Owners who attend the meeting shall not be prevented from amending items included in the agenda or from deciding the amended item or other items presented at the meeting. The Representative of Unit Operator shall be chairman of each meeting.

**4.3 Voting Procedure.** Working Interest Owners through their Representatives shall decide all matters coming before them as follows:

**4.3.1 Voting Interest.** Each Working Interest Owner shall have a voting interest equal to its participating interest determined in accordance with Section 5.3 of this agreement, and each Representative shall have a voting interest equal to the aggregate of the participating interest of all the Working Interest Owners whom he represents.

4.3.2 Vote Required - Generally. Unless otherwise provided herein or in the Unit Agreement, all matters shall be decided by an affirmative vote of fifty per cent (50%) or more voting interest; provided that, should any one Working Interest Owner have more than fifty per cent (50%) voting interest its vote must be supported by the vote of two or more Working Interest Owners having a combined voting interest of at least ten per cent (10%).

4.3.3 Vote Required - Large Expenditures and Special Projects. A Project involving

- (a) an expenditure of more than Fifty Thousand Dollars (\$50,000.00), or
- (b) a revision of the Participating Interest necessitated by the enlargement of the Participating Area

shall be decided by the affirmative vote of seventy-five per cent (75%) or more voting interest; provided that, should any one Working Interest Owner have more than fifty per cent (50%) voting interest, its vote must be supported by two or more Working Interest Owners having a combined voting interest of at least ten per cent (10%).

4.3.4 Vote at Meeting in case of Nonattendance. Any Representative who is not represented at a meeting may vote by letter or telegram addressed to the Unit Operator if his vote is received prior to the vote on the item. Such vote shall not be counted with respect to any item on the agenda which is amended at the meeting.

4.3.5 Poll Votes. The Representatives of the Working Interest Owners may vote on and decide, by letter or telegram, any matter submitted in writing to them if no meeting is requested, as provided in Section 4.2 within seven (7) days after the proposal is sent to the Representatives of the Working Interest Owners by the Unit Operator. Unit Operator will give prompt notice of the results of the voting to all Representatives.

4.3.6 Proxy Voting. Each Representative may name in writing an alternate or proxy to attend any meeting and cast said Representative's vote on any matter coming before the meeting, or, said Representative may elect not to attend a meeting, but cast his vote in writing as provided in 4.3.5. Any such vote so cast by a Representative through his proxy or in writing shall constitute the vote of such Representative the same as though he were personally present at the meeting.

## ARTICLE 5

### INDIVIDUAL RIGHTS OF WORKING INTEREST OWNERS

5.1 Reservation of Rights. Working Interest Owners severally reserve to themselves all their rights, except as otherwise provided in this agreement and the Unit Agreement.

5.2 Specific Rights. Each Working Interest Owner shall have, among others, the following specific rights:

5.2.1 Access to Unit Area. Access to the Unit Area at reasonable times and at his own risk to inspect Unit Operations and all Unit Wells, and upon reasonable notice to Unit Operator, to inspect records and data pertaining to Unit Operations.

5.2.2 Reports. Working Interest Owners shall have the right to receive from Unit Operator, upon written request, copies of all reports to any governmental agency, reports of crude oil runs and stocks, inventory reports, and all other information pertaining to Unit Operations not covered in the Unit Operators monthly progress report. The cost of gathering and furnishing such information, however, shall be charged to the Working Interest Owner who requests the information.

5.2.3 Right to Take in Kind. Each Working Interest Owner shall have the right to take in kind or separately dispose of its share of the Unitized Substances, excluding that which has been used in Unit Operations or unavoidably lost. In the event any Working Interest Owner shall fail to take in kind or to separately dispose of its share of the Unitized Substances, then Unit Operator (or any Working Interest Owner if Unit Operator fails to exercise the right) shall have the right to sell or itself purchase the Unitized Substances on a day-to-day basis at the price which the Unit Operator receives for its share of such substances. Any cost incurred by Unit Operator in making any such sale shall be borne by the Working Interest Owner whose share is sold. Any such sale or purchase by Unit Operator or any Working Interest Owner, as the case may be, shall always be subject to the right of the owner of such Unitized Substances to exercise at any time the right to take in kind or to separately dispose of its share of production not previously delivered to a purchaser pursuant hereto. The Working Interest Owner who shall take in kind or separately dispose of its share of Unitized Substances shall bear the expense thereof.

5.3 Participating Interest. The "Participating Interest" of each Working Interest Owner hereunder is equal to the sum total of the Percentage Participation assigned to tracts in the Participating Area in which such Working Interest Owner owns an interest; provided that if the working interests in any such tract are owned in undivided interest by two

or more Working Interest Owners, the Percentage Participation assigned to such tract shall be divided among such owners in proportion to their undivided interests and provided, further, that if the working interests in any tract are divided with respect to separate parcels of such tract and owned severally by different parties, the Percentage Participation assigned to such tract shall, in the absence of a sufficient, recordable instrument executed by all such parties fixing the division of ownership, be divided among such parcels in proportion to the number of surface acres in each. The Percentage Participation and any revisions thereof, determined in accordance with the Unit Agreement, shall govern the Participating Interests of the Working Interest Owners hereunder.

5.4 Apportionment of Cost and Benefit. Except as herein otherwise expressly provided, the unit expense shall be borne by the Working Interest Owners in proportion to their respective Participating Interests at the time such unit expense is incurred, and all benefits accruing under said Unit Agreement and this agreement shall be owned by the Working Interest Owners in proportion to their respective Participating Interests at the time such benefits accrue. The phrase "Unit Expense", as used herein, shall mean all costs, expenses or liabilities accruing or resulting from exploration, development, operation and maintenance of the Unitized Lands within the Participating Area by Working Interest Owners or Unit Operator, or without the Participating Area but within the Unit Area by Unit Operator, pursuant to the Unit Agreement and this agreement.

## ARTICLE 6

### UNIT OPERATOR

6.1 Initial Unit Operator. Newmont Oil Company is hereby designated as Unit Operator.

6.2 Resignation and Removal, and Successor. The resignation or removal and selection of a successor Unit Operator shall be governed by the provisions of the Unit Agreement. For the purposes of removal of Unit Operator, or Successor Unit Operator, for default or failure in performance of its duties in accordance with Section 8 of the Unit Agreement, such default or failure shall be deemed to have been sufficiently proved when (75%) seventy-five per cent of the committed working interest owners, (on the basis of unit participation and exclusive of the interest of the working interest owner who is unit operator) give written notice to the Unit Operator of their desire to cause his removal pursuant to the provisions of the Unit Agreement.

## ARTICLE 7

### AUTHORITIES AND DUTIES OF UNIT OPERATOR

7.1 Exclusive Right to Operate Unit. Subject to the provisions of

this agreement and the Unit Agreement, and to instructions authorized hereunder from Working Interest Owners, Unit Operator shall have the exclusive right and duty to conduct Unit Operations for the production of Unitized Substances.

7.2 Workmanlike Conduct. Unit Operator shall conduct Unit Operations in a good and workmanlike manner as would a prudent operator under the same or similar circumstances. Unit Operator shall freely consult with Working Interest Owners and keep them informed of all matters which Unit Operator in the exercise of its best judgment, considers important. Unit Operator shall not be liable to Working Interest Owners for damages, unless such damages result from its gross negligence or willful misconduct.

7.3 Liens and Encumbrances. Unit Operator shall endeavor to keep the lands and leases in the Unit Area free from all liens and encumbrances occasioned by Unit Operations, except the lien of Unit Operator granted hereunder.

7.4 Employees. The number of employees used by Unit Operator in conducting Unit Operations, their selection, hours of labor and compensation shall be determined by Unit Operator. Such employees shall be the employees of Unit Operator.

7.5 Records. Unit Operator shall keep correct books, accounts and records of Unit Operations.

7.6 Reports to Working Interest Owners. Unit Operator shall furnish to each of the Working Interest Owners a monthly progress report of Operations on the unit area. Such report will summarize oil production, (including total oil runs from the Unit) water injection and well work accomplished during the preceding month.

7.7 Reports to Governmental Authorities. Unit Operator shall make all reports to governmental authorities that it has the duty to make as Unit Operator.

7.8 Engineering and Geological Information. Unit Operator shall furnish to any Representative designated in Article 4. above, at cost and upon written request, a copy of the log pertaining to wells drilled for Unit Operations.

7.9 Expenditures. Subject to the restrictions herein contained, Unit Operator is authorized to make any and all expenditures necessary for the development and operation of the Unit Area including, but not limited to, single expenditures not in excess of \$5,000.00. Prior approval of Representatives of the Working Interest Owners designated in Article 4. shall be necessary for any single expenditures in excess of \$5,000. If an emergency occurs, Unit Operator may immediately make or incur such expenditures as in its opinion are required to deal with the emergency. Unit Operator shall report to Working Interest Owners, as promptly as possible, the nature of the emergency and the action taken.

7.10 Wells Drilled by Unit Operator. All wells drilled by Unit Operator shall be at the usual rates prevailing in the area. Unit Operator may employ its own tools and equipment, but the charge therefor shall not exceed the prevailing rate in the area, and the work shall be performed by Unit Operator under the same terms and conditions as are usual in the area in contracts of independent contractors doing work of a similar nature.

7.11 Water Supply. Water shall be supplied to the Unit in accordance with the provisions of that certain Water Sales Contract between Newmont Oil Company as Operator of the Unit, and Yucca Water Company dated April 25, 1963, as approved by the sub-committee composed of Thomas A. Ford, Richard Ray, J, Cleo Thompson, Sr., and S. P. Yates selected at the special meeting of the Operators on January 9, 1963, and such contract is incorporated herein by reference. The Non-operating parties agree to assume, be liable for, and hold Newmont harmless from their proportionate several shares of all liabilities and obligations under such contract in the same several proportions as the Non-operating parties are to receive the uses and benefits thereof. The Unit Operator shall enforce this contract for the best use and benefit of all parties signatory to this Agreement. Should the Unit Operator for any reason fail to discharge this obligation, it may nevertheless be required to do so at the direction of the Owners of not less than fifty percent (50%) of the Working Interest in the Unit Area covered by this Agreement or at least fifty percent (50%) of the Working Interest Owners may elect to take any action that is necessary to enforce the contract as though they were parties thereto.

7.12 Fair Employment. In connection with the performance of work under this agreement, the Unit Operator agrees not to discriminate against any employee or applicant for employment because of race, religion, color or national origin. The aforesaid provision shall include, but not be limited to, the following: Employment, upgrading, demotion or transfer, recruitment or recruitment advertising, layoff or termination, rates of pay or other forms of compensation, and the selection for training, including apprenticeship. The Unit Operator agrees to post hereafter in conspicuous places, available for employees and applicants for employment, notice to be provided by the contracting officer, setting forth the provisions of this non-discrimination clause. The Unit Operator agrees to insert the foregoing provision in all sub-contracts hereunder, except subcontracts for standard commercial supplies or raw materials.

7.13 Mathematical Errors. It is hereby agreed by all parties to this agreement that Unit Operator is empowered to correct any mathematical errors which might exist in the pertinent exhibits to this agreement, with approval of the Commissioner and the Supervisor.

## ARTICLE 8

### TAXES

8.1 Ad Valorem Taxes. Unit Operator shall make and file all necessary ad valorem tax renditions and returns with the proper taxing authorities covering all real and personal property of each Working Interest Owner used or held by Unit Operator in Unit Operations. Unit Operator shall settle assessments arising therefrom. All such ad valorem taxes and the expense of reporting and paying same shall be paid by Unit Operator and charged to the joint account.

8.2 Other Taxes. Each Working Interest Owner shall pay or cause to be paid all production, severance, gathering and other taxes imposed upon or in respect of the production or handling of its share of Unitized Substances.

## ARTICLE 9

### INSURANCE

9.1 Insurance. Unit Operator, with respect to Unit Operations, and as a charge to the joint account shall:

9.1.1 Comply with the Workmen's Compensation Law of the State of New Mexico.

9.1.2 Carry Employer's Liability and other insurance as required by the laws of the State of New Mexico.

9.1.3 Carry other insurance as set forth in Exhibit "D".

## ARTICLE 10

### ADJUSTMENT OF INVESTMENTS

10.1 Personal Property Taken Over. Upon the Effective Date hereof, Working Interest Owners shall deliver to Unit Operator the following:

10.1.1 Wells and Casing. All wells completed in the Unitized Formation within the Participating Area, together with the casing therein.

10.1.2 Well and Lease Equipment. The tubing in each such well, the wellhead connections thereon, and all other lease and operating equipment that is used in the operation of such wells which Unit Operator determines is necessary or desirable for conducting Unit Operations.

10.1.3 Records. A copy of all production and well records that pertain to such wells.

10.1.4 Condition of Wells. Each 40 acre tract within the initial Participating Area shall be obligated to have, prior to being turned over to the Unit Operator, one usable well thereon completed in the Unitized Formation which shall be mechanically sound for production of Unitized Substances. A "usable well" shall be one which has a hole to the unitized zone and from which the casing has not been pulled and is not ruptured and in which there is no junk. In the event such well turned over to the Unit Operator is found to be mechanically unsound, Unit Operator may, at the sole cost, risk and expense of the Working Interest Owner of such well attempt to correct such mechanical conditions so as to cause such well to be acceptable hereunder. Should the expense of such remedial

work performed by the Unit Operator hereunder on any such required "usable well" exceed the sum of \$5,000.00, the amount in excess of such \$5,000.00 shall be borne by the Unit. Provided however, if Unit Operator does not object to any well, or the condition thereof, within three (3) months after the stage of the flood within which such well is located has been commenced, then such wells as are located on acreage covered by such stage shall be deemed to be "usable wells" and the Working Interest Owner thereof shall not be chargeable with the above mentioned \$5,000.00 expenditure. Provided further, all wells, regardless of the stage of the flood within which they are located, will be considered and deemed "usable wells" three (3) years after commencement of the first stage of the flood and the Unit Operator thereafter shall charge all remedial work to the Unit.

10.2 Inventory and Evaluation of Personal Property. Working Interest Owners shall at Unit Expense inventory and evaluate in accordance with the provisions of Exhibit "C" the personal property taken over.

10.3 Initial Investment Adjustment. Upon approval by Working Interest Owners of the inventory and evaluation, each Working Interest Owner shall be credited with the value of its interest in all personal property taken over under Section 10.1.2, and shall be charged with an amount equal to that obtained by multiplying the total value of all personal property taken over under Section 10.1.2 by such Working Interest Owner's Participating Interest. If the charge against any Working Interest Owner is greater than the amount credited to such Working Interest Owner, the resulting net charge shall be an item of Unit Expense chargeable against such Working Interest Owner and said Working Interest Owner shall forthwith pay to Unit Operator such net charge. If the credit to any Working Interest Owner is greater than the amount charged against such Working Interest Owner, the resulting net credit shall be paid to such Working Interest Owner by Unit Operator out of funds received by it in settlement of the net charges described above.

10.4 General Facilities. The acquisition of warehouses, warehouse stocks, lease houses, camps, facility systems and office buildings necessary for Unit Operations shall be by negotiations by the owners thereof and Unit Operator, subject to the approval of Working Interest Owners. There shall be no investment adjustment for lease roads or uncontrollable appurtenances thereto.

10.5 Ownership of Personal Property and Facilities. Each Working Interest Owner, individually, shall by virtue hereof own an undivided interest, equal to its Participating Interest, in all personal property and facilities taken over or otherwise acquired by Unit Operator pursuant to this agreement. Within the period of ninety (90) days after notice in writing from the Unit Operator that any personal property or facilities will not be retained for Unit Operations, the Working Interest Owner shall either remove such personal property or facilities from the Unit Area or shall locate such personal property and facilities within the Unit Area so that the same will not interfere with Unit Operations.

10.6 Investment Adjustment on Enlargement of Participating Area. On enlargement of the Participating Area as provided in this agreement and in the Unit Agreement, there shall be investment adjustments between the Working Interest Owners in the Participating Area as enlarged, who are parties hereto. The costs and investments within the enlarged Participating Area shall be paid for by the Working Interest Owners in the enlarged Participating Area in proportion to their respective Participating Interest in such enlarged Area in the manner set forth in Section 10.3 hereof, except that a book inventory of the Participating Area, prior to enlargement, may be used in the adjustment.

ARTICLE 11  
UNIT EXPENSE

11.1 Basis of Charge to Working Interest Owners. Unit Operator initially shall pay all Unit Expense. Each Working Interest Owner shall reimburse Unit Operator for its share of Unit Expense including Unit Operator's expenses incurred in organizing the Unit. Each Working Interest Owner's share shall be the same as its Participating Interest. All charges, credits and account for Unit Expense shall be in accordance with Exhibit "C".

11.2 Budgets. Before or as soon as practical after the effective date hereof, Unit Operator shall prepare a budget of estimated Unit Expense for the remainder of the calendar year, and, on or before the first day of each December thereafter, shall prepare such a budget for the ensuing calendar year. A budget shall set forth the estimated Unit Expense by quarterly periods. Budgets shall be estimates only, and may be adjusted or corrected by Unit Operator whenever an adjustment or correction is proper. A copy of each budget and adjusted budget shall promptly be furnished to each Working Interest Owner.

11.3 Advance Billings. Unit Operator shall have the right to require Working Interest Owners to advance their respective shares of estimated Unit Expense by submitting to the Representatives of the Working Interest Owners, on or before the 15th day of any month, an itemized estimate thereof for the succeeding month, with a request for payment in advance. Within fifteen (15) days thereafter, payment shall be made to the Unit Operator for each Working Interest Owner's share of such estimated cost. Adjustments between estimated and actual Unit Expense shall be made by Unit Operator at the close of each calendar month, and the accounts shall be adjusted accordingly.

11.4 Commingling of Funds. No funds received by Unit Operator under this agreement need be segregated or maintained by it as a separate fund, but may be commingled with its own funds.

11.5 Lien of Unit Operator. Each Working Interest Owner hereby grants to Unit Operator a lien upon its oil and gas rights in each tract, its share of Unitized Substances when produced, and its interest in all Unit Equipment, as security for payment of its share of Unit Expense,

together with interest thereon at the rate of six per cent (6%) per annum. Unit Operator shall have the right to bring suit to enforce collection of such indebtedness with or without seeking foreclosure of the lien. In addition, upon default by any Working Interest Owner in the payment of its share of Unit Expense, Unit Operator shall have the right to collect from the purchaser the proceeds from the sale of such Working Interest Owner's share of Unitized Substances until the amount owned by such Working Interest Owner, plus interest as aforesaid, has been paid. Each purchaser shall be entitled to rely upon Unit Operator's written statement concerning the amount of any default.

**11.6 Unpaid Unit Expenses.** If any Working Interest Owner fails to pay its share of Unit Expense within sixty (60) days after rendition of a statement therefor by Unit Operator, each Working Interest Owner agrees, upon request by Unit Operator, to pay its proportionate Participating Interest part of the unpaid share of Unit Expense of the defaulting Working Interest Owner. The Working Interest Owners that pay the share of Unit Expense of a defaulting Working Interest Owner shall be reimbursed by the Unit Operator for the amount so paid, plus any interest collected thereon, upon receipt by Unit Operator of any past due amount collected from the defaulting Working Interest Owner. Any Working Interest Owner so paying a defaulting Working Interest Owner's share of Unit Expenses shall be subrogated to the lien and rights herein granted Unit Operator.

**11.7 Royalties and Compensatory Royalties:** The Working Interest Owners shall be responsible severally for and shall pay all royalties which may become due and payable because of the production from, and allocation of Unitized Substances to, their respective leases committed to the Unit Agreement. If any of said leases are burdened with any overriding royalties, payments out of production or any other charges in addition to the usual royalty, the Working Interest Owners of any such lease shall bear and assume such burdens out of the Unitized Substances produced from or allocated thereto. In cases where the affected Working Interest Owners determine to pay compensatory royalty or damages in lieu of drilling a demanded offset well, such compensatory royalty shall be paid by Unit Operator and charged to the joint account to the affected Working Interest Owners. The expense of Compensatory royalty for drainage of lands within the Participating Area shall be apportioned to all the Working Interest Owners in proportion to their respective interests therein.

**11.7.1 Uncommitted Royalty.** Should an owner of a Royalty Interest in any Tract within the Participating Area fail to become a party to the Unit Agreement, and, as a result thereof, the actual Royalty Interest payments with respect to such Tract are more or less than the Royalty Interest payments computed on the basis of the Unitized Substances that are allocated to such Tract under the Unit Agreement, the difference shall be borne

by or inure to the benefit of the Working Interest Owner that has the Working Interest that is subject to such royalty.

11.8 Construction of Plants and Special Facilities. Unit Operator shall charge the joint account for overhead for the construction of Water or Gas Injection Plants, other special facilities, or additions thereto, at the rate of five per cent (5%) for the first Twenty Five Thousand Dollars (\$25,000.00) of investment costs and two per cent (2%) for all investment costs in excess thereof.

11.9 Gauge of Tanks. Unit Operator shall make a proper and timely gauge of all lease tanks within the Participating Area in order to ascertain the amount of merchantable Unitized Substances in such tanks as of 7:00 A.M. on the effective date hereof. All such Unitized Substances which have been produced legally shall remain the property of the Owners entitled thereto the same as if this Unit had not been formed; and such Owners shall promptly remove the Unitized Substances from the Unit Area. Any Unitized Substances not so removed shall be sold by Unit Operator for the account of such owners. If, however, as of the effective date hereof, any Tract within the Participating Area is overproduced with respect to the allowable of the well or wells located on such tract and the amount of such overproduction has been sold or otherwise disposed of, such overproduction shall be regarded and included as a part of the Unitized Substances produced after the effective date hereof and the amount thereof charged to such Tract as having been delivered to the persons entitled to Unitized Substances allocated to such Tract.

## ARTICLE 12

### NON-UNITIZED FORMATIONS AND NON-PARTICIPATING ACREAGE

12.1 Right to Operate. Any Working Interest Owner that has now or hereafter acquires the right to drill for and produce oil, gas or other minerals, from other than the Unitized Formation, shall have the right to do so notwithstanding this agreement or the Unit Agreement. In exercising the right, however, the Working Interest Owner shall exercise reasonable precaution to prevent unreasonable interference with Unit Operations. Unless expressly authorized by this agreement or by the Unit Agreement, no Working Interest Owner shall produce Unitized Substances through any well drilled or operated by it. If any Working Interest Owner drills any well into or through the Unitized Formation, the Unitized Formation shall be protected in a manner satisfactory to Unit Operator so that the production of Unitized Substances will not adversely be affected.

12.2 Damage to Well Producing from Non - Unitized Formations. The Unit shall be responsible for protecting from waterflood damage that one certain well known as the Bassett-Birney #5, located in the SENWNW of Section 2. T. 18 S - R. 29 E. that is producing from a different zone,

provided however, that any such damages shall not be caused by or contributed to through acts or negligence of the owners of said well.

### 12.3 Wells Outside Participating Area.

12.3.1 Responsibility for Development. The responsibility for reasonable development of each tract or portion thereof within the Unit Area but not within the Participating Area shall rest with the Working Interest Owners who contributed such tract to the Unit Area and all liability, if any, for nondevelopment of the portion of any such tract not within the Participating Area with reference to the Unitized Substances shall rest upon such Working Interest Owners. Such Working Interest Owners shall have the right, at their sole cost, risk and expense, to drill any well or wells thereon as may be necessary to reasonably develop such tract or portion thereof. Should any well so drilled by a party hereto be completed as a producer of Unitized Substances in paying quantities, then upon its completion, such parties shall offer such well to the Working Interest Owners in the Participating Area on the same basis of investment adjustment as wells located in the initial Participating Area were accepted and as to participation in accordance with Section 16 of the Unit Agreement. In the event of such acceptance the tract on which such well or wells is located shall be assigned a percentage of participation and shall be included in the Participating Area. In the event the tract is not so accepted and included within the Participating Area for any reason whatever, then all production from such well from the date of first production shall be owned by the parties entitled to share in the production from such tract.

12.3.2 Demanded Wells. For the purposes of this Agreement the term "demanded well" shall be deemed to mean and include any wells the drilling of which is demanded by the Department of the Interior, or, the Commissioner or Commission, either independently of any plan or development or as a substitution therefor or as an addition thereto. If the Working Interest Owners under the specific tract are unable to agree to drill such well, and if the Unit does not elect to drill such well pursuant to paragraph 12.3.4, then any one or more of the Working Interest Owners may elect to pay the cost of drilling a demanded well in proportion to their respective acreage interests in the Unit Area or as they may otherwise agree. If no Working Interest Owner is willing to pay such drilling costs, the parties hereto may determine by a vote taken pursuant to the provisions of this agreement whether to pay compensatory royalty, to contract the Unit Area, or to adopt any other measure satisfactory to the Department of the Interior, the Commissioner or Commission, whereby the obligation to drill such well may be avoided.

12.3.3 Dry Holes. If any well drilled in accordance with the foregoing provisions is completed as a dry hole, then the entire cost thereof shall be borne by the parties drilling the same, provided that at the request of the Unit Operator such well may be taken over by the Unit Operator for use as an injection well and to accomplish this the Operator is fully authorized and empowered to

negotiate, and with approval of the Representatives, enter into, execute and perform contracts with the drilling parties to acquire such well for its use as an injection well or for other purposes.

12.3.4 Non-Consent Development. In the event of failure of any Working Interest Owners to drill any well to the Unitized Formation within the Unit Area but without the Participating Area, deemed by the Working Interest Owners to be necessary for reasonable development, then the Unit Operator shall give written notice to the said Working Interest Owners so failing to drill of the request for the drilling of a well at a designated location and to the Unitized Formation. If, within thirty (30) days after receipt of such notice the notified Working Interest Owners fail to commence drilling operations at such location and fail to advise the Unit Operator of their agreement to drill such well, Unit Operator may proceed with the drilling of such well at the location specified and at Unit Expense. If such well is completed as a dry hole and the Tract upon which it is located is not included within the Participating Area, it shall be plugged and abandoned at Unit Expense, unless Unit Operator elects to use such well as an injection well for the benefit of the Unit. If such well is completed as a producer of Unitized Substances in paying quantities, the Participating Area shall be enlarged accordingly and the Tract on which the well was drilled shall be included among the Tracts within the Participating Area and such well shall be operated by Unit Operator for the joint account until the said account has received revenue from working interest Unitized Substances produced, saved and allocated to such Tract on account of such well over and above operating expenses equal to two times the cost of the drilling, completing and equipping such well for production including the control head or christmas tree. Thereafter the Working Interest Owners in the tract upon which such well was drilled shall be entitled to receive such portion of the Unitized Substances as were allocated to such Tract on account of such well. The basis of inclusion of such Tract and the percentage of participation allocable to such Tract shall be determined in the manner provided in Section 16 of the Unit Agreement.

12.3.5 Arbitration. In case of disagreement as to any of the matters under this Article, which cannot be settled amicably, then upon five (5) days' written notice given by one or more of the disagreeing parties to the parties taking a contrary position, the matter in dispute shall be submitted to a board of three arbitrators. The parties giving notice as provided herein agree to appoint one arbitrator and the parties receiving such notice agree to appoint one arbitrator. Such appointments shall be made within ten (10) days after the notice is given. Should either side in the dispute fail or refuse to appoint an arbitrator within the time specified, the side who has appointed an arbitrator, upon five (5) days' written notice to the side failing or refusing to appoint an arbitrator, may apply to the person who is the judge of any federal court having jurisdiction in the State of New Mexico

for the appointment of such second arbitrator, and in such case the person so appointed shall act as a second arbitrator. The third arbitrator shall be chosen promptly by the two so appointed. Any and all decisions rendered by a majority of the board of arbitrators shall be final and binding upon the parties hereto, and adjustment shall be made in conformity with their decision.

## ARTICLE 13

### TITLES

13.1 Warranty and Indemnity. Each Working Interest Owner represents and warrants that it is the owner of the respective working interests set forth opposite its name in Exhibit "B", and hereby agrees to indemnify and hold harmless the other Working Interest Owners from any loss due to failure, in whole or in part, of its title to any such interest, except failure of title arising out of Unit Operations; provided that, such indemnity shall be limited to an amount equal to the net value that has been received from the sale or receipt of Unitized Substances attributed to the interest as to which title failed. Each failure of title will be deemed to be effective, insofar as this agreement is concerned, as of the first day of the calendar month in which such failure is finally determined, and except as herein expressly provided for, there shall be no retroactive adjustment of Unit Expense, or retroactive allocation of Unitized Substances or the proceeds therefrom, as a result of title failure. Each Working Interest Owner will pay title opinion expenses required by the pipeline company in connection with the tracts under which such Working Interest Owners has interests.

13.2 Failure Because of Unit Operations. The failure of title to any Working Interest in any Tract by reason of Unit Operations, including non-production from such Tract, shall not change the Participating Interest of the Working Interest Owner whose title failed in relation to the Participating Interest Owners at the time of the title failure; provided such failure was not occasioned by the acts or neglect of the party whose title failed.

13.3 Rentals. The Working Interest Owners in each Tract shall pay rentals or minimum royalties due under the lease thereon and shall concurrently submit to the Unit Operator the evidence of such payments. Unit Operator shall reimburse the Working Interest Owner for all such payments and the cost thereof shall be a Unit Expense, unless such payment were made in connection with Non-participating Tracts, in which event such expense will be borne by the Working Interest Owners of such tracts. If the Working Interest Owners in any Tract determine not to pay any such rental or minimum royalty they shall notify Unit Operator at least sixty (60) days before the due date and they shall thereupon assign to Unit Operator as Trustee for all other Working Interest Owners, in proportion to their Participating Interest, all of their right, title and interest under said lease. In the event of failure of any Working Interest Owner to make proper payment of any such rental or minimum royalty through mistake or oversight where the same is required to continue the lease in force, there shall be no monetary liability on the part of Working Interest Owner failing to pay the same but such Working Interest

Owner shall make a bona fide effort to secure a new lease covering the same interest and commit such new lease to this agreement and to the Unit Agreement and in the event of failure to secure the new lease within a reasonable time, the Participating Interest of such Working Interest Owner shall be revised as required so that the Working Interest Owner failing to pay any such rentals shall not be credited with the ownership of such Tract on which the lease was lost. In the event of loss of title to a lease for failure to pay any rental or minimum royalty, all loss occasioned thereby shall be that of the Working Interest Owner who should have paid the same.

#### ARTICLE 14

##### LIABILITY, CLAIMS AND SUITS

14.1 Individual Liability. The duties, obligations and liabilities of Working Interest Owners shall be several and not joint or collective; and nothing herein contained shall ever be construed as creating a partnership of any kind, joint venture, association or trust among Working Interest Owners.

14.2 Settlements. Unit Operator may settle any single damage claim or suit involving Unit Operations but not involving an expenditure in excess of Two Thousand Dollars (\$2,000.00) provided the payment is in complete settlement of such claim or suit. If the amount required for settlement exceeds the above specified amount, Working Interest Owners shall assume and take over the further handling of the claim or suit unless such authority is expressly delegated to Unit Operator. All costs and expense of handling, settling or otherwise discharging such claim or suit shall be an item of Unit Expense. If a claim is made against any Working Interest Owner or if any Working Interest Owner is sued on account of any matter arising from Unit Operations and over which such Working Interest Owner individually has no control because of the rights given Working Interest Owners and Unit Operator by this agreement and the Unit Agreement, the Working Interest Owner shall immediately notify the Unit Operator, and the claim or suit shall be treated as any other claim or suit involving Unit Operations.

14.3 Force Majeure. Any obligation imposed upon the parties hereto by this agreement, other than the obligation to make payments due hereunder, shall be suspended while any party hereto (including the party designated as Unit Operator) is prevented from complying therewith by acts of God or the public enemy, governmental and/or judicial restraint, order or decree, war, fires, floods, storms, inability to secure materials, strikes, lockouts or other matters beyond such party's control whether similar or dissimilar, provided however, that the settlement of strikes and lockouts shall be entirely within the discretion of the party having the difficulty and no such party shall be required to settle any strike or

lockout when such course of action is deemed inadvisable by the party having such difficulty.

14.4 Regulations. Neither the Unit, nor the Unit Operator shall be under any liability, nor shall they be held responsible for any loss of title to any lease or portion thereof which is eliminated from the Unit Area pursuant to Section 5 of the Unit Agreement, or segregated into separate leases pursuant to Section 22 of the Unit Agreement.

## ARTICLE 15

### INTERNAL REVENUE PROVISION

15.1 Internal Revenue Provision. Notwithstanding any provisions herein that the rights and liabilities of the parties hereunder are several and not joint or collective, or that this agreement and the operations hereunder shall not constitute a partnership, if for Federal Income Tax purposes this agreement and the operations hereunder are regarded as a partnership, then each of the parties hereto hereby elects to be excluded from the application of all of the provisions of Subchapter K, Chapter 1, Subtitle A, of the Internal Revenue Code of 1954, as permitted and authorized by Section 761 of said Code and the regulation promulgated thereunder. Operator is hereby authorized and directed to execute on behalf of each of the parties hereto such evidence of this election as may be required by the Secretary of the Treasury of the United States or the Federal Internal Revenue Service, including specifically, but not by way of limitation, all of the returns, statements and the data required by Federal Regulations 1.761-1 (a). Should there be any requirement that each party hereto further evidence this election, each party hereto agrees to execute such documents and furnish such other evidence as may be required by the Federal Internal Revenue Service or as may be necessary to evidence this election. Each party hereto further agrees not to give any notices or take any other action inconsistent with the election made hereby. If any present or future income tax laws of the State or States in which the property covered by this agreement is located, or any future income tax law of the United States, contain, or shall hereafter contain, provisions similar to those contained in Subchapter K, Chapter 1, Subtitle A, of the Internal Revenue Code of 1954, under which an election similar to that provided by Section 761 of said Subchapter K is permitted, each of the parties hereto hereby makes such election or agrees to make such election as may be permitted by such laws. In making this election, each of the parties hereto hereby states that the income derived by him from the operations under this agreement can be adequately determined without the computation of partnership taxable income.

## ARTICLE 16

### NOTICES

16.1 Notices. All notices required hereunder shall be in writing and shall be deemed to have been properly served when sent by mail or telegram to the address of the representative of each Working Interest Owner as furnished to Unit Operator in accordance with Article 4.

## ARTICLE 17

### WITHDRAWAL OF WORKING INTEREST OWNER

17.1 Withdrawal. A Working Interest Owner may withdraw from this agreement by transferring, without warranty of title, either express or implied, to the other Working Interest Owners who do not desire to withdraw, all its Oil and Gas Rights together with its interest in all Unit Equipment and in all wells used in Unit Operations. Such transfer shall not relieve said Working Interest Owner from any such obligation or liability incurred prior to the date of the delivery of the transfer, which delivery may be made to Unit Operator as Agent for the transferees. The interest transferred shall be owned by the transferees in proportion to their respective Participating Interests. The transferees, in proportion to the respective interests so acquired, shall pay transferor, for its interest in Unit Equipment, the fair net salvage value thereof as estimated and fixed by Working Interest Owners. After the date of delivery of the transfer, the withdrawing Working Interest Owner shall be relieved from all further obligations and liability hereunder and under the Unit Agreement, and the rights of such Working Interest Owner hereunder and under the Unit Agreement shall cease insofar as they existed by virtue of the interest transferred. The phrase "Oil and Gas Rights" as used herein shall mean the right to explore, develop and operate lands within the Unit Area for the production of Unitized Substances and to share in the production so obtained or the proceeds thereof.

## ARTICLE 18

### ABANDONMENT OF WELLS

18.1 Rights of Former Owners. If Working Interest Owners decide to abandon permanently any well within the Unit Area prior to termination of the Unit Agreement, Unit Operator shall give written notice thereof to the Working Interest Owners of the Tract on which the well is located, and they shall have the option for a period of ninety (90) days after the sending of such notice to notify Unit Operator in writing of their election to take over and own the well. Within ten (10) days after

the Working Interest Owners of the Tract have notified Unit Operator of their election to take over the well, they shall pay Unit Operator for credit to the joint account, the amount estimated by Working Interest Owners to be the net salvage value of the casing and equipment in and on the well. The Working Interest Owners of the Tract, by taking over the well, agree to seal off effectively and protect the Unitized Formation, and upon abandonment to plug the well in compliance with applicable laws and regulations, and at their sole expense.

18.2 Plugging. If the Working Interest Owners of a Tract do not elect to take over a well located thereon which is proposed for abandonment, Unit Operator shall plug and abandon the well in compliance with applicable laws and regulations, and at Unit expense.

## ARTICLE 19

### EFFECTIVE DATE AND TERM

19.1 Effective Date. This agreement shall become effective on the date and at the time that the Unit Agreement becomes effective.

19.2 Term. This agreement shall continue in effect so long as the Unit Agreement remains in effect, and thereafter until (a) all unit wells have been abandoned and plugged or turned over to Working Interest Owners in accordance with Article 20, (b) all Unit Equipment and real property acquired for the joint account have been disposed of by Unit Operator in accordance with instructions of Working Interest Owners, and (c) there has been a final accounting.

## ARTICLE 20

### ABANDONMENT OF OPERATIONS

20.1 Termination. Upon termination of the Unit Agreement, the following will occur:

20.1.1 Oil and Gas Rights. Oil and Gas Rights in and to each separate Tract shall no longer be affected by this agreement, and thereafter the parties shall be governed by the terms and provisions of the leases, contracts and other instruments affecting the separate Tracts.

20.1.2 Right to Operate. Working Interest Owners of any Tract that desire to take over and continue to operate wells located thereon may do so by paying Unit Operator, for credit to the joint account, the net salvage value of the casing and equipment in and on the wells taken over, as

estimated by Working Interest Owners, and by agreeing to plug properly each well at such time as it is abandoned.

20.1.3 Salvaging Wells. Unit Operator shall salvage as much of the casing and equipment in or on wells not taken over by Working Interest Owners of Separate Tracts as can economically and reasonably be salvaged, and shall cause the wells to be plugged and abandoned properly.

20.1.4 Cost of Salvaging. Working Interest Owners shall share the cost of salvaging, liquidation or other distribution of assets and properties used in Unit Operation in proportion to their respective Participating Interests.

## ARTICLE 21

### EXECUTION

21.1 Original Counterpart, or Other Instrument. A party may become a party to this agreement by signing the original of this instrument, a counterpart thereof, or other instrument agreeing to be bound by the provisions hereof. The signing of any such instrument shall have the same effect as if all the parties had signed the same instrument.

21.2 Execution. Unit Operator shall, prior to submission of the Unit Agreement for final approval to the Director and the Commissioner, furnish the Working Interest Owners with a report as to the number and percentage in interest of the Working Interest and Royalty Owners who have executed the Unit Agreement. The Working Interest Owners shall then determine whether or not submission of the Unit Agreement is justified. If a seventy-five per cent (75%) voting interest is in favor of such submission, then the Unit Agreement shall be submitted for final approval and all parties who have joined herein shall be bound hereby and shall remain a party hereto regardless of the joinder or nonjoinder of any other party who might be entitled to join herein, but in the event at least a seventy-five per cent (75%) voting interest is not in favor of such submission, no party hereto shall be construed to be bound by the terms of either this agreement or the Unit Agreement.

## ARTICLE 22

### SUCCESSORS AND ASSIGNS

22.1 Successors and Assigns. The provisions hereof shall be covenants running with the lands, leases and interests covered hereby, and shall be binding upon and inure to the benefit of the respective heirs, devisees, legal representatives, successors and assigns of the parties hereto.

22.2 Creation of New Interest. If any Working Interest Owner shall after executing this agreement, create any overriding royalty, production payment, or other similar interest, hereinafter referred to as "New Interest", out of its interest subject to this agreement, such New Interest shall be subject to all the terms and provisions of this agreement. In the event the Working Interest Owner, owning the interest from which the New Interest was created, withdraws from this agreement under the terms of Section 17., or fails to pay any expenses and costs chargeable to it under this agreement and the production to the credit of such Working Interest Owner is insufficient for that purpose, the owner of the New Interest will be liable for the pro rata portion of all costs and expenses which the original Working Interest Owner, creating such New Interest, would have been liable by virtue of his ownership of the New Interest had the same not been transferred. In this event, the lien provided in Section 11.5 may be enforced against such New Interest. If the owner of the New Interest bears a portion of the costs and expenses or the same is enforced against such New Interest, the owner of the New Interest will be subrogated to the rights of the Unit Operator with respect to the interest primarily chargeable with such costs and expenses.

IN WITNESS WHEREOF, The parties hereto have executed this agreement on the dates opposite their respective signatures.

Attest, if a Corporation,  
Witness, if an Individual

Name



Richard Warren  
Assistant Secretary

Date  
Signed

5-29-63

NEWMONT OIL COMPANY

By Charles B. Hayden  
Vice-President

UNIT OPERATOR AND WORKING  
INTEREST OWNER  
1-2A,-2B-2C-21A-21B-22-30-35

WORKING INTEREST OWNERS

BRIGHT & LARUE CORPORATION  
Company

By Sam Bright  
President  
23-43

Attest:

Ruth Chapman  
Secretary

5-13-63

Attest:

Marvin G. Welton  
Secretary-Treasurer

5-13-63

FAIR OIL COMPANY  
Company

By James W. Fair  
President  
17A-17B-24-31-33-35

Signature Page to: Unit Operating Agreement, West Loco Hills Grayburg  
No. 4 Sand Unit, Eddy County, New Mexico

Attest:

*W. J. Barry*  
Assistant Secretary

Yates Petroleum Corporation  
Company

By: *S. P. Yates*  
President

Attest:

\_\_\_\_\_

\_\_\_\_\_  
Company  
By: \_\_\_\_\_  
President

Attest:

\_\_\_\_\_

Dixon - Yates Oil Co.  
14-15

Gladys Dixon & Mary D. Duggan, Individually  
4A-4B-6-7A-7B-13A-13B

DIXON & YATES OIL COMPANY, a p  
Yates Brothers, a partnersh

By *Gladys Dixon*  
Gladys Dixon, Individually and  
partner in Dixon & Yates Oil Co

Yates Brothers  
4A-4B

Harvey E. Yates, Individually  
6-7A-7B-9-10B-10C-11A-11B-13A-13B

*Mary D. Duggan*  
Mary D. Duggan (Mary Dorot  
Individually & as a partner in Dixon  
YATES BROTHERS, a partnership  
Harvey E. Yates, John

Martin Yates, III, Individually  
4A-4B-6-7A-7B-9-10B-10C-11A-11B-13A-13B-40

By *Harvey E. Yates*  
Harvey E. Yates, Individua  
a partner in Yates Brother

S. P. Yates, Individually  
6-7A-7B-9-10A-10B-10C-10D-11A-11B-13A-13B

By *Martin Yates III*  
Martin Yates, III, Indivic  
as a partner in Dixon & Yates Oil Co.,  
and a partner in Yates Brothers

John A. Yates, Individually  
6-7A-7B-9-10B-10C-10D-11A-11B-13A-13B

By *S. P. Yates*  
S. P. Yates, Individually and as a  
partner in Yates Brothers

Yates Petroleum Corporation  
6-7A-7B-11A-11B-13A-13B-16-39-40

*Estelle H. Yates*  
Estelle H. Yates, his wife

By *John A. Yates*  
John A. Yates, Individually and as  
a partner in Yates Brothers

*Peggy A. Yates*  
Peggy A. Yates, his wife