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February 1, 1995

TO: Janet Richardson
FROM: Dave Boneau *Dave Boneau*
SUBJECT: Proposed Avalon Delaware Unit

Attached is Exxon's response to the various proposals Yates has submitted in the past few months. The Exxon communication has the form of a letter to the Working Interest Owners that lays out changes to the original Exxon proposals that are agreeable to both Exxon and Yates. So the question is whether the position outlined in the letter is agreeable to Yates. You will see that I do not like the voting procedure devised by Exxon.

The main points are:

1. The participation formula for the life of the unit is:

- a) 25 Percent Remaining Primary Reserves
- b) 50 Percent Tract Waterflood Reserves
- c) 25 Percent Tract CO₂ Reserves.

The result gives 12.01 % to Yates and 73.92 % to Exxon (including Exxon's purchase of the Merit interests).

2. The overhead rate will be \$550 per producing well. The overhead rate will increase by 27% (to \$700 escalated) when a CO₂ project is approved by the owners and will decrease back to \$550 (escalated) when CO₂ injection ends. The agreement will allow AFE's to pay Exxon for CO₂ Project Studies.
3. Since Exxon will own over 70 percent, the voting procedure allows approval with the affirmative vote of Exxon plus owners of 2.6 percent additional.

The participation formula meets our needs. The voting procedure stinks, and the voting procedure is doubly important since it is linked to AFE's for Exxon CO₂ Project Studies. Last night I told Ron Mayhew of Exxon that I did not see how we could accept the voting procedure. I have told Exxon all along that the big minority owners should be able to veto an AFE if they all vote against it. Exxon feels that small owners will be bought out or will go non-consent or simply never return ballots so that Exxon will be

Janet Richardson

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pressed to get 2.6 percent without Yates and the few "major" people left. An alternative I have considered is that an Exxon AFE is approved unless we get 18 or 20 percent to vote negative.

So, the summary is that we have the voting procedure as a remaining major hurdle. I ask that you review the treatment of non-consents and investment equalization since they impact our discussion of the voting procedure. Exxon expects an immediate response from Yates so we will meet this week if possible.

DFB/cvg

Attachments

xc: Mike Slater
Randy Patterson
Pinson McWhorter
Bob Fant
Peyton Yates

Letterhead

DRAFT
Single Phase

Date

Avalon (Delaware) Field Unitization
Eddy Co., N. M.**Working Interest Owners:**

The last correspondence you received was my letter dated June 20, 1994, which summarized the June 17 Working Interest Owners (WIO) meeting. Several WIO's expressed a strong interest for a single phase formula. An action item of the meeting was for Yates Petroleum to develop an alternative participation formula from the one we proposed.

Letters that summarize the Yates formula and our suggested modifications are attached, dated September 6, October 10 and December 5, 1994. Our single phase proposal, along with modifications to the previously transmitted (April 1994) Unit and Unit Operating Agreements is described in Attachment II and resulting participation in Attachment III of this letter.

This single phase proposal is a significant concession of equity for Exxon compared to our original 2 phase proposal with a vote required for Phase 2. If the single phase proposal is not acceptable, we would prefer to return to a 2 phase formula similar to our original recommendation.

At this time we are requesting either 1.) your concurrence with provisions that are now acceptable to both Exxon and Yates Petroleum or 2.) your suggested changes (return Attachment I). Should you have questions feel free to call me at (915) 688 - 7841. We appreciate your continued support.

Sincerely,

Ronald E. Mayhew
Avalon Project Manager

Attachments I-III

Attachment I: Response to Exxon on Revised Unitization Proposal

Responses requested by February 24, 1995

Mail to: R. E. Mayhew, Avalon Response
Exxon USA
P.O. Box 1600
Midland, TX 79702-1600 or fax to (915) 688-6258

Please provide your response by checking one box and completing the information below:

Company Name (s): _____

We agree with the unitization proposal as described in this letter (Attachment II). Exxon should proceed with incorporating these modifications into revised Unit and Unit Operating Agreements.

By (typed or written): _____ Title: _____

Signature: _____ Phone: _____

We agree with the unitization proposal as described in this letter (Attachment II), but would like consideration of the issue(s) in our attached letter.

By (typed or written): _____ Title: _____

Signature: _____ Phone: _____

We disagree with the unitization proposal as described in this letter (Attachment II). Our proposal for changes along with our rationale is provided in the attached letter.

By (typed or written): _____ Title: _____

Signature: _____ Phone: _____

Attachment II: Summary Description of Proposed Modifications to Avalon Field Unit and Unit Operating Agreements

Abbreviations The following abbreviations are used:

WI working interest
WIO working interest owners
AFE Authority For Expenditure

Equity The table below describes proposed revisions to equity participation in the Avalon (Delaware Field) Unit from what Exxon proposed in the previously provided Unit and Unit Operating Agreements.

Feature	Description
Phases	Participation will be in a single phase only; which was requested by several attendees at the June 94 WIO meeting.
Reserve Factors	Participation will be based on tract reserves with the following Reserve Factors: <ul style="list-style-type: none"> • 25 % Remaining Primary • 50 % Waterflood • 25 % CO₂ Note: These percentages are multiplied by each owners tract reserves percentage (by Primary, waterflood, and CO ₂), then summed to obtain a Unit Equity (percentage) as shown on Attachment III.
Rationale behind Reserve Factors	The rationale used in developing the reserve factors was based on several items listed below: <ul style="list-style-type: none"> • Primary reserves have a higher value/barrel by orders of magnitude (i.e. investments have been made and production is indicator of future potential) • the Unit is being put together to repressure the reservoir, implement a waterflood and gather data for evaluating CO₂ potential • CO₂ reserves are high, but have a relatively low value due to risks because of unknowns associated with the reservoir and of doing a CO₂ project • CO₂ reserves have substantially lower discounted profit per barrel Note: see Technical Report Vol. I, Exhibit H5 for more information
Why include CO ₂ reserves	About 2/3 of the CO ₂ reserves are within the area to be unitized for water injection. A CO ₂ flood would likely be initiated in this portion of the field and if successful expanded to the outer ring (tracts outside the waterflood area) that was not waterflooded. As potential operator we see some planning and development advantages of including the outside ring in the unit. This outer ring has no commercial primary and/or waterflood potential.
Owner participation	A summary of owner participation is provided in Attachment III.

Continued on next page

Attachment II: Summary Description of Proposed Modifications to Avalon Field Unit and Unit Operating Agreements, Continued

Capital Expenditures & Contributed Investments

All expenditures (capital and operating expense), along with existing investments of use to the Unit would be at the Single Phase participation percentage shown on Attachment III.

Examples:

- Capital Expenditure: \$13M waterflood and/or future AFEs/ballots: Each owner pays WI% times \$13M and/or ballot amounts
- Operating Expense: Each owner pays WI% times monthly operating cost
- Investment Equalization: If a well or portion of surface facility equipment can be utilized in waterflood or CO₂ operations each owner will be credited with the determined value. Then each owner will be debited with an amount equal to their WI% times (Sum of the values of all wells/equipment brought into the Unit).

Note: Under a single phase formula an owner cannot go non-consent on investment equalization and participate in the unit development or vice versa.

Overhead

Overhead rate will be charged as follows:

- initial overhead rate will be \$550/producing well
- overhead will increase 27% when a CO₂ project is approved by Unit Owners
- overhead will decrease 22% when CO₂ injection ceases

Exception: Exxon may submit AFE's prior to approval of a CO₂ Project to Working Interest Owners to conduct CO₂ Project studies that will be considered as an operating expense outside the overhead category. Approval must be voted in similar to other AFEs.

Examples: These studies could include computer modeling, injectivity test planning & analysis, cost/production estimates, etc.

Voting

Ballots submitted for approval to Working Interest Owners will be considered approved if either of the following conditions are met:

- 80% of the WIO participation approves the ballot
- If one owner has interest > 70%, that owners interest plus 10% of the remaining interest.

Approval = largest owner WI (if > 70%) + 0.10 (100% - Largest Owners WI)

> 2.5%
 2 beyond Yates, ANPC
 3 beyond Yates, ANPC, Hurd...

Attachment III: Avalon (Delaware) Participation (25,50,25)

	G-24 1/1/93 Ram Primary	G-24 Tract Waterflood Reserves	G-24 Tract CO2 Reserves	Single Phase Formula Participation: 25% Primary, 50% Waterflood, and 25% CO2 flood
Abco Petroleum Corporation	0.6731%	1.3313%	1.1936%	1.1323%
American National Pet. Corp.	2.3177%	5.5317%	4.7210%	4.6505%
Art, Mary H.	0.8259%	1.6336%	1.3331%	1.3566%
Bello, Ernie	0.0046%	0.0088%	0.0075%	0.0074%
Bunn, Mrs. Francis B.	0.0046%	0.0088%	0.0075%	0.0074%
Chevron PBC, Inc.	0.4236%	0.6857%	1.3238%	1.3566%
Claremont Corporation	0.1549%	0.3063%	0.2500%	0.2544%
Devon Energy Corporation (NV)	0.0691%	0.1367%	0.1117%	0.1117%
Devon Energy Partners L.P.	0.3916%	0.7746%	0.6331%	0.6331%
Exxon Corporation	85.0939%	70.7355%	67.9026%	73.6419%
Fox, Fred A. & D. Marjorie Living Trust	0.0005%	0.0000%	0.0038%	0.0011%
Gendron Family Revocable Trust	0.0069%	0.0132%	0.0112%	0.0111%
Goodnow, David	0.0046%	0.0088%	0.0075%	0.0074%
Hayes Partners I	0.0000%	0.0000%	0.0412%	0.0103%
Hodge, Joseph R.	0.0008%	0.0015%	0.0012%	0.0013%
Hodge, Sanford J. III	0.0008%	0.0015%	0.0012%	0.0013%
Holden, E. G. Testamentary Tr	0.0023%	0.0044%	0.0037%	0.0037%
Hudson, Edward R. Jr.	0.8259%	1.6336%	1.3331%	1.3566%
Hudson, William A. II	0.8259%	1.6336%	1.3331%	1.3566%
Kawasaki, Isaac A.	0.0046%	0.0088%	0.0075%	0.0074%
Keller, Betsy H.	0.0023%	0.0044%	0.0037%	0.0037%
Kerr-McGee Corporation	0.1493%	0.2953%	0.2410%	0.2452%
LJ Corporation	0.0010%	0.0000%	0.0073%	0.0021%
Los Chicos	0.0000%	0.0000%	0.0100%	0.0025%
Marin, James L. Jr., Trust	0.0005%	0.0000%	0.0038%	0.0011%
Marin, Williams, & Jackson	0.3456%	0.6125%	0.7825%	0.7825%
McCall, Jack O Estate of	0.0000%	0.0000%	0.0003%	0.0001%
Merit Energy Partners, II, L.P.	0.0000%	0.0000%	0.3713%	0.0928%
Merit Energy Partners, III, L.P.	0.0000%	0.0000%	0.3713%	0.0928%
Merit Energy Partners, L.P.	0.0000%	0.0000%	0.3713%	0.0928%
Moore, Charles Cline	0.0115%	0.0219%	0.0189%	0.0186%
Munroe, Vernon	0.0046%	0.0088%	0.0075%	0.0074%
Myco Industries, Inc.	2.0241%	3.9938%	3.4210%	3.3582%
Napco	0.0000%	0.0000%	0.0719%	0.0180%
Oliver, Angus Cluete Tr	0.0046%	0.0088%	0.0075%	0.0074%
Oliver, William B Tr	0.0046%	0.0088%	0.0075%	0.0074%
Oxy U.S.A., Inc.	0.0000%	0.0000%	0.5361%	0.1340%
Pemier Oil & Gas, Inc.	0.0000%	0.0000%	4.0769%	4.0769%
Redfern, John J. III, Indep Exec of Est of	0.0725%	0.1433%	0.1170%	0.1190%
Redfern, Rosalind	0.0725%	0.1433%	0.1170%	0.1190%
Schlagel, John L.	0.0005%	0.0000%	0.0032%	0.0009%
Mrd, Adair P Schuman Tr	0.0046%	0.0088%	0.0075%	0.0074%
Seventy-Seven Corporation	0.0000%	0.0000%	0.0080%	1.0020%
Sigmar, Inc.	0.0015%	0.0000%	0.0111%	0.0032%
Space Building Corp.	0.0115%	0.0219%	0.0189%	0.0186%
Tipperary Oil Corporation	0.3199%	0.5561%	0.4468%	0.4468%
TR Oil Corporation	0.0000%	0.0000%	0.0042%	0.0011%
Van Vranken, J. F. Jr.	0.0046%	0.0088%	0.0075%	0.0074%
Whiting Petroleum Corporation	0.3199%	0.5561%	0.4468%	0.4468%
Yates Drilling Company	2.0192%	3.9938%	3.3864%	3.3483%
Yates Petroleum Corporation	2.4800%	4.9051%	4.3094%	4.1495%
Yates, John A.	0.0049%	0.0000%	0.0446%	0.0124%
Yates, S. P.	0.0049%	0.0000%	0.0446%	0.0099%
	100.0000%	100.0000%	100.0000%	100.0000%
YPC Et al	7.2062%	14.2340%	12.3996%	12.0135%
Exxon with Merit	85.0939%	70.7355%	69.0165%	73.9204%

1.3566

0.9049

0.1136
0.6435

0.5893 INVESTMENT = GAIN

1.0192

0.5197

0.5197