

Powell No. 1  
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A.A.P.L. FORM 610 - 1989  
**MODEL FORM OPERATING AGREEMENT**

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**OPERATING AGREEMENT**

**DATED**

February 1, 19 97,

**OPERATOR** Merrion Oil & Gas Corporation

**CONTRACT AREA** Township 32 North, Range 13 West, NMPM

Section 22: All

As to the Fruitland Coal formation

**COUNTY OR PARISH OF** San Juan, **STATE OF** New Mexico

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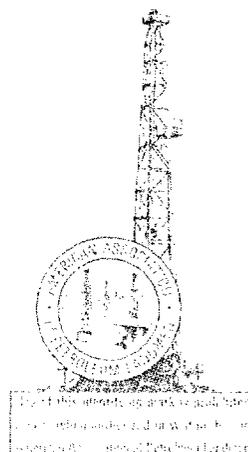
NMOCD Examiner Hearing  
May 1, 1997  
Docket No. 13-97  
Case No. 11766  
Exhibit No. 7

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OPERATING AGREEMENT

THIS AGREEMENT, entered into by and between Merrion Oil & Gas Corporation, hereinafter designated and referred to as "Operator," and the signatory party or parties other than Operator, sometimes hereinafter referred to individually as "Non-Operator," and collectively as "Non-Operators."

WITNESSETH:

WHEREAS, the parties to this agreement are owners of Oil and Gas Leases and/or Oil and Gas Interests in the land identified in Exhibit "A," and the parties hereto have reached an agreement to explore and develop these Leases and/or Oil and Gas Interests for the production of Oil and Gas to the extent and as hereinafter provided,

NOW, THEREFORE, it is agreed as follows:

ARTICLE I. DEFINITIONS

As used in this agreement, the following words and terms shall have the meanings here ascribed to them:

A. The term "AFE" shall mean an Authority for Expenditure prepared by a party to this agreement for the purpose of estimating the costs to be incurred in conducting an operation hereunder.

B. The term "Completion" or "Complete" shall mean a single operation intended to complete a well as a producer of Oil and Gas in one or more Zones, including, but not limited to, the setting of production casing, perforating, well stimulation and production testing conducted in such operation.

C. The term "Contract Area" shall mean all of the lands, Oil and Gas Leases and/or Oil and Gas Interests intended to be developed and operated for Oil and Gas purposes under this agreement. Such lands, Oil and Gas Leases and Oil and Gas Interests are described in Exhibit "A."

D. The term "Deepen" shall mean a single operation whereby a well is drilled to an objective Zone below the deepest Zone in which the well was previously drilled, or below the Deepest Zone proposed in the associated AFE, whichever is the lesser.

E. The terms "Drilling Party" and "Consenting Party" shall mean a party who agrees to join in and pay its share of the cost of any operation conducted under the provisions of this agreement.

F. The term "Drilling Unit" shall mean the area fixed for the drilling of one well by order or rule of any state or federal body having authority. If a Drilling Unit is not fixed by any such rule or order, a Drilling Unit shall be the drilling unit as established by the pattern of drilling in the Contract Area unless fixed by express agreement of the Drilling Parties.

G. The term "Drillsite" shall mean the Oil and Gas Lease or Oil and Gas Interest on which a proposed well is to be located.

H. The term "Initial Well" shall mean the well required to be drilled by the parties hereto as provided in Article VI.A.

I. The term "Non-Consent Well" shall mean a well in which less than all parties have conducted an operation as provided in Article VI.B.2.

J. The terms "Non-Drilling Party" and "Non-Consenting Party" shall mean a party who elects not to participate in a proposed operation.

K. The term "Oil and Gas" shall mean oil, gas, casinghead gas, gas condensate, and/or all other liquid or gaseous hydrocarbons and other marketable substances produced therewith, unless an intent to limit the inclusiveness of this term is specifically stated.

L. The term "Oil and Gas Interests" or "Interests" shall mean unleased fee and mineral interests in Oil and Gas in tracts of land lying within the Contract Area which are owned by parties to this agreement.

M. The terms "Oil and Gas Lease," "Lease" and "Leasehold" shall mean the oil and gas leases or interests therein covering tracts of land lying within the Contract Area which are owned by the parties to this agreement.

N. The term "Plug Back" shall mean a single operation whereby a deeper Zone is abandoned in order to attempt a Completion in a shallower Zone.

O. The term "Recompletion" or "Recomplete" shall mean an operation whereby a Completion in one Zone is abandoned in order to attempt a Completion in a different Zone within the existing wellbore.

P. The term "Rework" shall mean an operation conducted in the wellbore of a well after it is Completed to secure, restore, or improve production in a Zone which is currently open to production in the wellbore. Such operations include, but are not limited to, well stimulation operations but exclude any routine repair or maintenance work or drilling, Sidetracking, Deepening, Completing, Recompleting, or Plugging Back of a well.

Q. The term "Sidetrack" shall mean the directional control and intentional deviation of a well from vertical so as to change the bottom hole location unless done to straighten the hole or to drill around junk in the hole to overcome other mechanical difficulties.

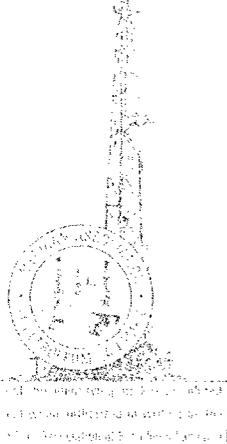
R. The term "Zone" shall mean a stratum of earth containing or thought to contain a common accumulation of Oil and Gas separately producible from any other common accumulation of Oil and Gas.

Unless the context otherwise clearly indicates, words used in the singular include the plural, the word "person" includes natural and artificial persons, the plural includes the singular, and any gender includes the masculine, feminine, and neuter.

ARTICLE II. EXHIBITS

The following exhibits, as indicated below and attached hereto, are incorporated in and made a part hereof:

- X A. Exhibit "A," shall include the following information: (1) Description of lands subject to this agreement, (2) Restrictions, if any, as to depths, formations, or substances, (3) Parties to agreement with addresses and telephone numbers for notice purposes, (4) Percentages or fractional interests of parties to this agreement, (5) Oil and Gas Leases and/or Oil and Gas Interests subject to this agreement, (6) Burdens on production.
B. Exhibit "B," Form of Lease.
X C. Exhibit "C," Accounting Procedure.
X D. Exhibit "D," Insurance.
X E. Exhibit "E," Gas Balancing Agreement.
X F. Exhibit "F," Non-Discrimination and Certification of Non-Segregated Facilities.
G. Exhibit "G," Tax Partnership.
H. Other:



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1 If any provision of any exhibit, except Exhibits "E," "F" and "G," is inconsistent with any provision contained in  
2 the body of this agreement, the provisions in the body of this agreement shall prevail.

## 3 ARTICLE III.

### 4 INTERESTS OF PARTIES

#### 5 A. Oil and Gas Interests:

6 ~~Every party to this Agreement~~  
7 ~~If any party owns an Oil and Gas Interest in the Contract Area, that Interest shall be treated for all purposes of this~~  
8 ~~agreement and during the term hereof as if it were covered by the form of Oil and Gas Lease attached hereto as Exhibit "B,"~~  
9 ~~and the owner thereof shall be deemed to own both royalty interest in such lease and the interest of the lessee thereunder.~~

#### 10 B. Interests of Parties in Costs and Production:

11 Unless changed by other provisions, all costs and liabilities incurred in operations under this agreement shall be borne  
12 and paid, and all equipment and materials acquired in operations on the Contract Area shall be owned, by the parties as their  
13 interests are set forth in Exhibit "A." In the same manner, the parties shall also own all production of Oil and Gas from the  
14 Contract Area subject, however, to the payment of royalties and other burdens on production as described hereafter.

15 ~~Regardless of which party has contributed any Oil and Gas Lease or Oil and Gas Interest on which royalty or other~~  
16 ~~burdens may be payable and except as otherwise expressly provided in this agreement, each party shall pay or deliver, or~~  
17 ~~cause to be paid or delivered, all burdens on its share of the production from the Contract Area up to, but not in excess of,~~  
18 ~~\_\_\_\_\_ and shall indemnify, defend and hold the other parties free from any liability therefor.~~

19 ~~Except as otherwise expressly provided in this agreement, if any party has contributed hereto any Lease or Interest which is~~  
20 ~~burdened with any royalty, overriding royalty, production payment or other burden on production in excess of the amounts~~  
21 ~~stipulated above, such party so burdened shall assume and alone bear all such excess obligations and shall indemnify, defend~~  
22 ~~and hold the other parties hereto harmless from any and all claims attributable to such excess burden. However, so long as~~  
23 ~~the Drilling Unit for the productive Zone(s) is identical with the Contract Area, each party shall pay or deliver, or cause to~~  
24 ~~be paid or delivered, all burdens on production from the Contract Area due under the terms of the Oil and Gas Lease(s)~~  
25 ~~which such party has contributed to this agreement, and shall indemnify, defend and hold the other parties free from any~~  
26 ~~liability therefor.~~

27 ~~No party shall ever be responsible, on a price basis higher than the price received by such party, to any other party's~~  
28 ~~lessor or royalty owner, and if such other party's lessor or royalty owner should demand and receive settlement on a higher~~  
29 ~~price basis, the party contributing the affected Lease shall bear the additional royalty burden attributable to such higher price.~~

30 Nothing contained in this Article III.B. shall be deemed an assignment or cross-assignment of interests covered hereby,  
31 and in the event two or more parties contribute to this agreement jointly owned Leases, the parties' undivided interests in  
32 said Leaseholds shall be deemed separate leasehold interests for the purposes of this agreement.

#### 33 C. Subsequently Created Interests:

34 If any party has contributed hereto a Lease or Interest that is burdened with an assignment of production given as security  
35 for the payment of money, or if, after the date of this agreement, any party creates an overriding royalty, production  
36 payment, net profits interest, assignment of production or other burden payable out of production attributable to its working  
37 interest hereunder, such burden shall be deemed a "Subsequently Created Interest." Further, if any party has contributed  
38 hereto a Lease or Interest burdened with an overriding royalty, production payment, net profits interest, or other burden  
39 payable out of production created prior to the date of this agreement, and such burden is not shown on Exhibit "A," such  
40 burden also shall be deemed a Subsequently Created Interest, ~~to the extent such burden causes the burdens on such party's~~  
41 ~~Lease or Interest to exceed the amount stipulated in Article III.B. above.~~

42 The party whose interest is burdened with the Subsequently Created Interest (the "Burdened Party") shall assume and  
43 alone bear, pay and discharge the Subsequently Created Interest and shall indemnify, defend and hold harmless the other  
44 parties from and against any liability therefor. Further, if the Burdened Party fails to pay, when due, its share of expenses  
45 chargeable hereunder, all provisions of Article VII.B. shall be enforceable against the Subsequently Created Interest in the  
46 same manner as they are enforceable against the working interest of the Burdened Party. If the Burdened Party is required  
47 under this agreement to assign or relinquish to any other party, or parties, all or a portion of its working interest and/or the  
48 production attributable thereto, said other party, or parties, shall receive said assignment and/or production free and clear of  
49 said Subsequently Created Interest, and the Burdened Party shall indemnify, defend and hold harmless said other party, or  
50 parties, from any and all claims and demands for payment asserted by owners of the Subsequently Created Interest.

## 51 ARTICLE IV.

### 52 TITLES

#### 53 A. Title Examination:

54 Title examination shall be made on the Drillsite of any proposed well prior to commencement of drilling operations and,  
55 if a majority in interest of the Drilling Parties so request or Operator so elects, title examination shall be made on the entire  
56 Drilling Unit, or maximum anticipated Drilling Unit, of the well. The opinion will include the ownership of the working  
57 interest, minerals, royalty, overriding royalty and production payments under the applicable Leases. Each party contributing  
58 Leases and/or Oil and Gas Interests to be included in the Drillsite or Drilling Unit, if appropriate, shall furnish to Operator  
59 all abstracts (including federal lease status reports), title opinions, title papers and curative material in its possession free of  
60 charge. All such information not in the possession of or made available to Operator by the parties, but necessary for the  
61 examination of the title, shall be obtained by Operator. Operator shall cause title to be examined by attorneys on its staff or  
62 by outside attorneys. Copies of all title opinions shall be furnished to each Drilling Party. Costs incurred by Operator in  
63 procuring abstracts, fees paid outside attorneys for title examination (including preliminary, supplemental, shut-in royalty  
64 opinions and division order title opinions) and other direct charges as provided in Exhibit "C" shall be borne by the Drilling  
65 Parties in the proportion that the interest of each Drilling Party bears to the total interest of all Drilling Parties as such  
66 interests appear in Exhibit "A." Operator shall make no charge for services rendered by its staff attorneys or other personnel  
67 in the performance of the above functions.

68 Each party shall be responsible for securing curative matter and pooling amendments or agreements required in  
69 connection with Leases or Oil and Gas Interests contributed by such party. Operator shall be responsible for the preparation  
70 and recording of pooling designations or declarations and communitization agreements as well as the conduct of hearings  
71 before governmental agencies for the securing of spacing or pooling orders or any other orders necessary or appropriate to  
72 the conduct of operations hereunder. This shall not prevent any party from appearing on its own behalf at such hearings.  
73 Costs incurred by Operator, including fees paid to outside attorneys, which are associated with hearings before governmental  
74 agencies, and which costs are necessary and proper for the activities contemplated under this agreement, shall be direct  
75 charges to the joint account and shall not be covered by the administrative overhead charges as provided in Exhibit "C."

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1 Operator shall make no charge for services rendered by its staff attorneys or other personnel in the performance of the above  
2 functions.

3 No well shall be drilled on the Contract Area until after (1) the title to the Drillsite or Drilling Unit, if appropriate, has  
4 been examined as above provided, and (2) the title has been approved by the examining attorney or title has been accepted by  
5 all of the Drilling Parties in such well.

6 **B. Loss or Failure of Title:**

7 ~~1. Failure of Title: Should any Oil and Gas Interest or Oil and Gas Lease be lost through failure of title, which results in a  
8 reduction of interest from that shown on Exhibit "A," the party credited with contributing the affected Lease or Interest  
9 (including, if applicable, a successor in interest to such party) shall have ninety (90) days from final determination of title  
10 failure to acquire a new lease or other instrument curing the entirety of the title failure, which acquisition will not be subject  
11 to Article VIII.B., and failing to do so, this agreement, nevertheless, shall continue in force as to all remaining Oil and Gas  
12 Leases and Interests; and,~~

13 (a) The party credited with contributing the Oil and Gas Lease or Interest affected by the title failure (including, if  
14 applicable, a successor in interest to such party) shall bear alone the entire loss and it shall not be entitled to recover from  
15 Operator or the other parties any development or operating costs which it may have previously paid or incurred, but there  
16 shall be no additional liability on its part to the other parties hereto by reason of such title failure;

17 (b) There shall be no retroactive adjustment of expenses incurred or revenues received from the operation of the  
18 Lease or Interest which has failed, but the interests of the parties contained on Exhibit "A" shall be revised on an acreage  
19 basis, as of the time it is determined finally that title failure has occurred, so that the interest of the party whose Lease or  
20 Interest is affected by the title failure will thereafter be reduced in the Contract Area by the amount of the Lease or Interest failed;

21 (c) If the proportionate interest of the other parties hereto in any producing well previously drilled on the Contract  
22 Area is increased by reason of the title failure, the party who bore the costs incurred in connection with such well attributable  
23 to the Lease or Interest which has failed shall receive the proceeds attributable to the increase in such interest (less costs and  
24 burdens attributable thereto) until it has been reimbursed for unrecovered costs paid by it in connection with such well  
25 attributable to such failed Lease or Interest;

26 (d) Should any person not a party to this agreement, who is determined to be the owner of any Lease or Interest  
27 which has failed, pay in any manner any part of the cost of operation, development, or equipment, such amount shall be paid  
28 to the party or parties who bore the costs which are so refunded;

29 (e) Any liability to account to a person not a party to this agreement for prior production of Oil and Gas which arises  
30 by reason of title failure shall be borne severally by each party (including a predecessor to a current party) who received  
31 production for which such accounting is required based on the amount of such production received, and each such party shall  
32 severally indemnify, defend and hold harmless all other parties hereto for any such liability to account;

33 (f) No charge shall be made to the joint account for legal expenses, fees or salaries in connection with the defense of  
34 the Lease or Interest claimed to have failed, but if the party contributing such Lease or Interest hereto elects to defend its title  
35 it shall bear all expenses in connection therewith; and

36 (g) If any party is given credit on Exhibit "A" to a Lease or Interest which is limited solely to ownership of an  
37 interest in the wellbore of any well or wells and the production therefrom, such party's absence of interest in the remainder  
38 of the Contract Area shall be considered a Failure of Title as to such remaining Contract Area unless that absence of interest  
39 is reflected on Exhibit "A."

40 ~~2. Loss by Non-Payment or Erroneous Payment of Amount Due: If, through mistake or oversight, any rental, shut-in well  
41 payment, minimum royalty or royalty payment, or other payment necessary to maintain all or a portion of an Oil and Gas  
42 Lease or Interest is not paid or is erroneously paid, and as a result a Lease or Interest terminates, there shall be no monetary  
43 liability against the party who failed to make such payment. Unless the party who failed to make the required payment  
44 secures a new Lease or Interest covering the same interest within ninety (90) days from the discovery of the failure to make  
45 proper payment, which acquisition will not be subject to Article VIII.B., the interests of the parties reflected on Exhibit "A"  
46 shall be revised on an acreage basis, effective as of the date of termination of the Lease or Interest involved, and the party  
47 who failed to make proper payment will no longer be credited with an interest in the Contract Area on account of ownership  
48 of the Lease or Interest which has terminated. If the party who failed to make the required payment shall not have been fully  
49 reimbursed, at the time of the loss, from the proceeds of the sale of Oil and Gas attributable to the lost Lease or Interest,  
50 calculated on an acreage basis, for the development and operating costs previously paid on account of such Lease or Interest,  
51 it shall be reimbursed for unrecovered actual costs previously paid by it (but not for its share of the cost of any dry hole  
52 previously drilled or wells previously abandoned) from so much of the following as is necessary to effect reimbursement:~~

53 (a) Proceeds of Oil and Gas produced prior to termination of the Lease or Interest, less operating expenses and lease  
54 burdens chargeable hereunder to the person who failed to make payment, previously accrued to the credit of the lost Lease or  
55 Interest, on an acreage basis, up to the amount of unrecovered costs;

56 (b) Proceeds of Oil and Gas, less operating expenses and lease burdens chargeable hereunder to the person who failed  
57 to make payment, up to the amount of unrecovered costs attributable to that portion of Oil and Gas thereafter produced and  
58 marketed (excluding production from any wells thereafter drilled) which, in the absence of such Lease or Interest termination,  
59 would be attributable to the lost Lease or Interest on an acreage basis and which as a result of such Lease or Interest  
60 termination is credited to other parties, the proceeds of said portion of the Oil and Gas to be contributed by the other parties  
61 in proportion to their respective interests reflected on Exhibit "A"; and,

62 (c) Any monies, up to the amount of unrecovered costs, that may be paid by any party who is, or becomes, the owner  
63 of the Lease or Interest lost, for the privilege of participating in the Contract Area or becoming a party to this agreement.

64 ~~3. Other Losses: All losses of Leases or Interests committed to this agreement, other than those set forth in Articles  
65 IV.B.1. and IV.B.2. above, shall be joint losses and shall be borne by all parties in proportion to their interests shown on  
66 Exhibit "A." This shall include but not be limited to the loss of any Lease or Interest through failure to develop or because  
67 express or implied covenants have not been performed (other than performance which requires only the payment of money),  
68 and the loss of any Lease by expiration at the end of its primary term if it is not renewed or extended. There shall be no  
69 readjustment of interests in the remaining portion of the Contract Area on account of any joint loss.~~

70 ~~4. Curing Title: In the event of a Failure of Title under Article IV.B.1. or a loss of title under Article IV.B.2. above, any  
71 Lease or Interest acquired by any party hereto (other than the party whose interest has failed or was lost) during the ninety  
72 (90) day period provided by Article IV.B.1. and Article IV.B.2. above covering all or a portion of the interest that has failed  
73 or was lost shall be offered at cost to the party whose interest has failed or was lost, and the provisions of Article VIII.B.  
74 shall not apply to such acquisition.~~

ARTICLE V.  
OPERATOR

A. Designation and Responsibilities of Operator:

Merrion Oil & Gas Corporation shall be the Operator of the Contract Area, and shall conduct and direct and have full control of all operations on the Contract Area as permitted and required by, and within the limits of this agreement. In its performance of services hereunder for the Non-Operators, Operator shall be an independent contractor not subject to the control or direction of the Non-Operators except as to the type of operation to be undertaken in accordance with the election procedures contained in this agreement. Operator shall not be deemed, or hold itself out as, the agent of the Non-Operators with authority to bind them to any obligation or liability assumed or incurred by Operator as to any third party. Operator shall conduct its activities under this agreement as a reasonable prudent operator, in a good and workmanlike manner, with due diligence and dispatch, in accordance with good oilfield practice, and in compliance with applicable law and regulation, but in no event shall it have any liability as Operator to the other parties for losses sustained or liabilities incurred except such as may result from gross negligence or willful misconduct.

B. Resignation or Removal of Operator and Selection of Successor:

1. Resignation or Removal of Operator: Operator may resign at any time by giving written notice thereof to Non-Operators. If Operator terminates its legal existence, no longer owns an interest hereunder in the Contract Area, or is no longer capable of serving as Operator, Operator shall be deemed to have resigned without any action by Non-Operators, except the selection of a successor. Operator may be removed only for good cause by the affirmative vote of Non-Operators owning a majority interest based on ownership as shown on Exhibit "A" remaining after excluding the voting interest of Operator; such vote shall not be deemed effective until a written notice has been delivered to the Operator by a Non-Operator detailing the alleged default and Operator has failed to cure the default within thirty (30) days from its receipt of the notice or, if the default concerns an operation then being conducted, within forty-eight (48) hours of its receipt of the notice. For purposes hereof, "good cause" shall mean not only gross negligence or willful misconduct but also the material breach of or inability to meet the standards of operation contained in Article V.A. or material failure or inability to perform its obligations under this agreement.

Subject to Article VII.D.1., such resignation or removal shall not become effective until 7:00 o'clock A.M. on the first day of the calendar month following the expiration of ninety (90) days after the giving of notice of resignation by Operator or action by the Non-Operators to remove Operator, unless a successor Operator has been selected and assumes the duties of Operator at an earlier date. Operator, after effective date of resignation or removal, shall be bound by the terms hereof as a Non-Operator. A change of a corporate name or structure of Operator or transfer of Operator's interest to any single subsidiary, parent or successor corporation shall not be the basis for removal of Operator.

2. Selection of Successor Operator: Upon the resignation or removal of Operator under any provision of this agreement, a successor Operator shall be selected by the parties. The successor Operator shall be selected from the parties owning an interest in the Contract Area at the time such successor Operator is selected. The successor Operator shall be selected by the affirmative vote of two (2) or more parties owning a majority interest based on ownership as shown on Exhibit "A"; provided, however, if an Operator which has been removed or is deemed to have resigned fails to vote or votes only to succeed itself, the successor Operator shall be selected by the affirmative vote of the party or parties owning a majority interest based on ownership as shown on Exhibit "A" remaining after excluding the voting interest of the Operator that was removed or resigned. The former Operator shall promptly deliver to the successor Operator all records and data relating to the operations conducted by the former Operator to the extent such records and data are not already in the possession of the successor operator. Any cost of obtaining or copying the former Operator's records and data shall be charged to the joint account.

3. Effect of Bankruptcy: If Operator becomes insolvent, bankrupt or is placed in receivership, it shall be deemed to have resigned without any action by Non-Operators, except the selection of a successor. If a petition for relief under the federal bankruptcy laws is filed by or against Operator, and the removal of Operator is prevented by the federal bankruptcy court, all Non-Operators and Operator shall comprise an interim operating committee to serve until Operator has elected to reject or assume this agreement pursuant to the Bankruptcy Code, and an election to reject this agreement by Operator as a debtor in possession, or by a trustee in bankruptcy, shall be deemed a resignation as Operator without any action by Non-Operators, except the selection of a successor. During the period of time the operating committee controls operations, all actions shall require the approval of two (2) or more parties owning a majority interest based on ownership as shown on Exhibit "A." In the event there are only two (2) parties to this agreement, during the period of time the operating committee controls operations, a third party acceptable to Operator, Non-Operator and the federal bankruptcy court shall be selected as a member of the operating committee, and all actions shall require the approval of two (2) members of the operating committee without regard for their interest in the Contract Area based on Exhibit "A."

C. Employees and Contractors:

The number of employees or contractors used by Operator in conducting operations hereunder, their selection, and the hours of labor and the compensation for services performed shall be determined by Operator, and all such employees or contractors shall be the employees or contractors of Operator.

D. Rights and Duties of Operator:

1. Competitive Rates and Use of Affiliates: All wells drilled on the Contract Area shall be drilled on a competitive contract basis at the usual rates prevailing in the area. If it so desires, Operator may employ its own tools and equipment in the drilling of wells, but its charges therefor shall not exceed the prevailing rates in the area and the rate of such charges shall be agreed upon by the parties in writing before drilling operations are commenced, and such work shall be performed by Operator under the same terms and conditions as are customary and usual in the area in contracts of independent contractors who are doing work of a similar nature. All work performed or materials supplied by affiliates or related parties of Operator shall be performed or supplied at competitive rates, pursuant to written agreement, and in accordance with customs and standards prevailing in the industry.

2. Discharge of Joint Account Obligations: Except as herein otherwise specifically provided, Operator shall promptly pay and discharge expenses incurred in the development and operation of the Contract Area pursuant to this agreement and shall charge each of the parties hereto with their respective proportionate shares upon the expense basis provided in Exhibit "C." Operator shall keep an accurate record of the joint account hereunder, showing expenses incurred and charges and credits made and received.

3. Protection from Liens: Operator shall pay, or cause to be paid, as and when they become due and payable, all accounts of contractors and suppliers and wages and salaries for services rendered or performed, and for materials supplied on, to or in respect of the Contract Area or any operations for the joint account thereof, and shall keep the Contract Area free from

1 liens and encumbrances resulting therefrom except for those resulting from a bona fide dispute as to services rendered or  
2 materials supplied.

3 4. Custody of Funds: Operator shall hold for the account of the Non-Operators any funds of the Non-Operators advanced  
4 or paid to the Operator, either for the conduct of operations hereunder or as a result of the sale of production from the  
5 Contract Area, and such funds shall remain the funds of the Non-Operators on whose account they are advanced or paid until  
6 used for their intended purpose or otherwise delivered to the Non-Operators or applied toward the payment of debts as  
7 provided in Article VII.B. Nothing in this paragraph shall be construed to establish a fiduciary relationship between Operator  
8 and Non-Operators for any purpose other than to account for Non-Operator funds as herein specifically provided. Nothing in  
9 this paragraph shall require the maintenance by Operator of separate accounts for the funds of Non-Operators unless the  
10 parties otherwise specifically agree.

11 5. Access to Contract Area and Records: Operator shall, except as otherwise provided herein, permit each Non-Operator  
12 or its duly authorized representative, at the Non-Operator's sole risk and cost, full and free access at all reasonable times to  
13 all operations of every kind and character being conducted for the joint account on the Contract Area and to the records of  
14 operations conducted thereon or production therefrom, including Operator's books and records relating thereto. Such access  
15 rights shall not be exercised in a manner interfering with Operator's conduct of an operation hereunder and shall not obligate  
16 Operator to furnish any geologic or geophysical data of an interpretive nature unless the cost of preparation of such  
17 interpretive data was charged to the joint account. Operator will furnish to each Non-Operator upon request copies of any  
18 and all reports and information obtained by Operator in connection with production and related items, including, without  
19 limitation, meter and chart reports, production purchaser statements, run tickets and monthly gauge reports, but excluding  
20 purchase contracts and pricing information to the extent not applicable to the production of the Non-Operator seeking the  
21 information. Any audit of Operator's records relating to amounts expended and the appropriateness of such expenditures  
22 shall be conducted in accordance with the audit protocol specified in Exhibit "C."

23 6. Filing and Furnishing Governmental Reports: Operator will file, and upon written request promptly furnish copies to  
24 each requesting Non-Operator not in default of its payment obligations, all operational notices, reports or applications  
25 required to be filed by local, State, Federal or Indian agencies or authorities having jurisdiction over operations hereunder.  
26 Each Non-Operator shall provide to Operator on a timely basis all information necessary to Operator to make such filings.

27 7. Drilling and Testing Operations: The following provisions shall apply to each well drilled hereunder, including but not  
28 limited to the Initial Well:

29 (a) Operator will promptly advise Non-Operators of the date on which the well is spudded, or the date on which  
30 drilling operations are commenced.

31 (b) Operator will send to Non-Operators such reports, test results and notices regarding the progress of operations on the well  
32 as the Non-Operators shall reasonably request, including, but not limited to, daily drilling reports, completion reports, and well logs.

33 (c) Operator shall adequately test all Zones encountered which may reasonably be expected to be capable of producing  
34 Oil and Gas in paying quantities as a result of examination of the electric log or any other logs or cores or tests conducted  
35 hereunder.

36 8. Cost Estimates. Upon request of any Consenting Party, Operator shall furnish estimates of current and cumulative costs  
37 incurred for the joint account at reasonable intervals during the conduct of any operation pursuant to this agreement.  
38 Operator shall not be held liable for errors in such estimates so long as the estimates are made in good faith.

39 9. Insurance: At all times while operations are conducted hereunder, Operator shall comply with the workers  
40 compensation law of the state where the operations are being conducted; provided, however, that Operator may be a self-  
41 insurer for liability under said compensation laws in which event the only charge that shall be made to the joint account shall  
42 be as provided in Exhibit "C." Operator shall also carry or provide insurance for the benefit of the joint account of the parties  
43 as outlined in Exhibit "D" attached hereto and made a part hereof. Operator shall require all contractors engaged in work on  
44 or for the Contract Area to comply with the workers compensation law of the state where the operations are being conducted  
45 and to maintain such other insurance as Operator may require.

46 In the event automobile liability insurance is specified in said Exhibit "D," or subsequently receives the approval of the  
47 parties, no direct charge shall be made by Operator for premiums paid for such insurance for Operator's automotive  
48 equipment.

49 **ARTICLE VI.**  
50 **DRILLING AND DEVELOPMENT**

51 **A. Initial Well:**

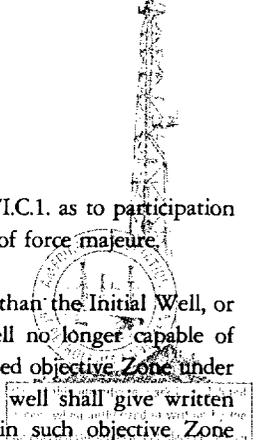
52 On or before the 31st day of December, 19 97, Operator shall commence the drilling of the Initial  
53 Well at the following location: (Havasu No. 1)  
54 790' FSL, 790' FEL  
55 SESE of Section 22, Township 32 North, Range 13 West, NMPM  
56  
57  
58  
59

60 and shall thereafter continue the drilling of the well with due diligence to test the Fruitland Coal formation.  
61  
62  
63  
64  
65  
66

67 The drilling of the Initial Well and the participation therein by all parties is obligatory, subject to Article VI.C.1. as to participation  
68 in Completion operations and Article VI.F. as to termination of operations and Article XI as to occurrence of force majeure.

69 **B. Subsequent Operations:**

70 1. Proposed Operations: If any party hereto should desire to drill any well on the Contract Area other than the Initial Well, or  
71 if any party should desire to Rework, Sidetrack, Deepen, Recomplete or Plug Back a dry hole or a well no longer capable of  
72 producing in paying quantities in which such party has not otherwise relinquished its interest in the proposed objective Zone under  
73 this agreement, the party desiring to drill, Rework, Sidetrack, Deepen, Recomplete or Plug Back such a well shall give written  
74 notice of the proposed operation to the parties who have not otherwise relinquished their interest in such objective Zone.



1 under this agreement and to all other parties in the case of a proposal for Sidetracking or Deepening, specifying the work to be  
 2 performed, the location, proposed depth, objective Zone and the estimated cost of the operation. The parties to whom such a  
 3 notice is delivered shall have thirty (30) days after receipt of the notice within which to notify the party proposing to do the work  
 4 whether they elect to participate in the cost of the proposed operation. If a drilling rig is on location, notice of a proposal to  
 5 Rework, Sidetrack, Recomplete, Plug Back or Deepen may be given by telephone and the response period shall be limited to forty-  
 6 eight (48) hours, exclusive of Saturday, Sunday and legal holidays. Failure of a party to whom such notice is delivered to reply  
 7 within the period above fixed shall constitute an election by that party not to participate in the cost of the proposed operation.  
 8 Any proposal by a party to conduct an operation conflicting with the operation initially proposed shall be delivered to all parties  
 9 within the time and in the manner provided in Article VI.B.6.

10 If all parties to whom such notice is delivered elect to participate in such a proposed operation, the parties shall be  
 11 contractually committed to participate therein provided such operations are commenced within the time period hereafter set  
 12 forth, and Operator shall, no later than ninety (90) days after expiration of the notice period of thirty (30) days (or as  
 13 promptly as practicable after the expiration of the forty-eight (48) hour period when a drilling rig is on location, as the case  
 14 may be), actually commence the proposed operation and thereafter complete it with due diligence at the risk and expense of  
 15 the parties participating therein; provided, however, said commencement date may be extended upon written notice of same  
 16 by Operator to the other parties, for a period of up to thirty (30) additional days if, in the sole opinion of Operator, such  
 17 additional time is reasonably necessary to obtain permits from governmental authorities, surface rights (including rights-of-  
 18 way) or appropriate drilling equipment, or to complete title examination or curative matter required for title approval or  
 19 acceptance. If the actual operation has not been commenced within the time provided (including any extension thereof as  
 20 specifically permitted herein or in the force majeure provisions of Article XI) and if any party hereto still desires to conduct  
 21 said operation, written notice proposing same must be resubmitted to the other parties in accordance herewith as if no prior  
 22 proposal had been made. Those parties that did not participate in the drilling of a well for which a proposal to Deepen or  
 23 Sidetrack is made hereunder shall, if such parties desire to participate in the proposed Deepening or Sidetracking operation,  
 24 reimburse the Drilling Parties in accordance with Article VI.B.4. in the event of a Deepening operation and in accordance  
 25 with Article VI.B.5. in the event of a Sidetracking operation.

26 **2. Operations by Less Than All Parties:**

27 (a) Determination of Participation. If any party to whom such notice is delivered as provided in Article VI.B.1. or  
 28 VI.C.1. (Option No. 2) elects not to participate in the proposed operation, then, in order to be entitled to the benefits of this  
 29 Article, the party or parties giving the notice and such other parties as shall elect to participate in the operation shall, no  
 30 later than ninety (90) days after the expiration of the notice period of thirty (30) days (or as promptly as practicable after the  
 31 expiration of the forty-eight (48) hour period when a drilling rig is on location, as the case may be) actually commence the  
 32 proposed operation and complete it with due diligence. Operator shall perform all work for the account of the Consenting  
 33 Parties; provided, however, if no drilling rig or other equipment is on location, and if Operator is a Non-Consenting Party,  
 34 the Consenting Parties shall either: (i) request Operator to perform the work required by such proposed operation for the  
 35 account of the Consenting Parties, or (ii) designate one of the Consenting Parties as Operator to perform such work. The  
 36 rights and duties granted to and imposed upon the Operator under this agreement are granted to and imposed upon the party  
 37 designated as Operator for an operation in which the original Operator is a Non-Consenting Party. Consenting Parties, when  
 38 conducting operations on the Contract Area pursuant to this Article VI.B.2., shall comply with all terms and conditions of this  
 39 agreement.

40 If less than all parties approve any proposed operation, the proposing party, immediately after the expiration of the  
 41 applicable notice period, shall advise all Parties of the total interest of the parties approving such operation and its  
 42 recommendation as to whether the Consenting Parties should proceed with the operation as proposed. Each Consenting Party,  
 43 within forty-eight (48) hours (exclusive of Saturday, Sunday and legal holidays) after delivery of such notice, shall advise the  
 44 proposing party of its desire to (i) limit participation to such party's interest as shown on Exhibit "A" or (ii) carry only its  
 45 proportionate part (determined by dividing such party's interest in the Contract Area by the interests of all Consenting Parties in  
 46 the Contract Area) of Non-Consenting Parties' interests, or (iii) carry its proportionate part (determined as provided in (ii)) of  
 47 Non-Consenting Parties' interests together with all or a portion of its proportionate part of any Non-Consenting Parties'  
 48 interests that any Consenting Party did not elect to take. Any interest of Non-Consenting Parties that is not carried by a  
 49 Consenting Party shall be deemed to be carried by the party proposing the operation if such party does not withdraw its  
 50 proposal. Failure to advise the proposing party within the time required shall be deemed an election under (i). In the event a  
 51 drilling rig is on location, notice may be given by telephone, and the time permitted for such a response shall not exceed a  
 52 total of forty-eight (48) hours (exclusive of Saturday, Sunday and legal holidays). The proposing party, at its election, may  
 53 withdraw such proposal if there is less than 100% participation and shall notify all parties of such decision within ten (10)  
 54 days, or within twenty-four (24) hours if a drilling rig is on location, following expiration of the applicable response period.  
 55 If 100% subscription to the proposed operation is obtained, the proposing party shall promptly notify the Consenting Parties  
 56 of their proportionate interests in the operation and the party serving as Operator shall commence such operation within the  
 57 period provided in Article VI.B.1., subject to the same extension right as provided therein.

58 (b) Relinquishment of Interest for Non-Participation. The entire cost and risk of conducting such operations shall be  
 59 borne by the Consenting Parties in the proportions they have elected to bear same under the terms of the preceding  
 60 paragraph. Consenting Parties shall keep the leasehold estates involved in such operations free and clear of all liens and  
 61 encumbrances of every kind created by or arising from the operations of the Consenting Parties. If such an operation results  
 62 in a dry hole, then subject to Articles VI.B.6. and VI.E.3., the Consenting Parties shall plug and abandon the well and restore  
 63 the surface location at their sole cost, risk and expense; provided, however, that those Non-Consenting Parties that  
 64 participated in the drilling, Deepening or Sidetracking of the well shall remain liable for, and shall pay, their proportionate  
 65 shares of the cost of plugging and abandoning the well and restoring the surface location insofar only as those costs were not  
 66 increased by the subsequent operations of the Consenting Parties. If any well drilled, Reworked, Sidetracked, Deepened,  
 67 Recompleted or Plugged Back under the provisions of this Article results in a well capable of producing Oil and/or Gas in  
 68 paying quantities, the Consenting Parties shall Complete and equip the well to produce at their sole cost and risk, and the  
 69 well shall then be turned over to Operator (if the Operator did not conduct the operation) and shall be operated by it at the  
 70 expense and for the account of the Consenting Parties. Upon commencement of operations for the drilling, Reworking,  
 71 Sidetracking, Recompleting, Deepening or Plugging Back of any such well by Consenting Parties in accordance with the  
 72 provisions of this Article, each Non-Consenting Party shall be deemed to have relinquished to Consenting Parties, and the  
 73 Consenting Parties shall own and be entitled to receive, in proportion to their respective interests, all of such Non-  
 74 Consenting Party's interest in the well and share of production therefrom or, in the case of a Reworking, Sidetracking,

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1 Deepening, Recompleting or Plugging Back, or a Completion pursuant to Article VI.C.1. Option No. 2, all of such Non-  
2 Consenting Party's interest in the production obtained from the operation in which the Non-Consenting Party did not elect  
3 to participate. Such relinquishment shall be effective until the proceeds of the sale of such share, calculated at the well, or  
4 market value thereof if such share is not sold (after deducting applicable ad valorem, production, severance, and excise taxes,  
5 royalty, overriding royalty and other interests not excepted by Article III.C. payable out of or measured by the production  
6 from such well accruing with respect to such interest until it reverts), shall equal the total of the following:

7 (i) 300 % of each such Non-Consenting Party's share of the cost of any newly acquired surface equipment  
8 beyond the wellhead connections (including but not limited to stock tanks, separators, treaters, pumping equipment and  
9 piping), plus 100% of each such Non-Consenting Party's share of the cost of operation of the well commencing with first  
10 production and continuing until each such Non-Consenting Party's relinquished interest shall revert to it under other  
11 provisions of this Article, it being agreed that each Non-Consenting Party's share of such costs and equipment will be that  
12 interest which would have been chargeable to such Non-Consenting Party had it participated in the well from the beginning  
13 of the operations; and

14 (ii) 300 % of (a) that portion of the costs and expenses of drilling, Reworking, Sidetracking, Deepening,  
15 Plugging Back, testing, Completing, and Recompleting, after deducting any cash contributions received under Article VIII.C.,  
16 and of (b) that portion of the cost of newly acquired equipment in the well (to and including the wellhead connections),  
17 which would have been chargeable to such Non-Consenting Party if it had participated therein.

18 Notwithstanding anything to the contrary in this Article VI.B., if the well does not reach the deepest objective Zone  
19 described in the notice proposing the well for reasons other than the encountering of granite or practically impenetrable  
20 substance or other condition in the hole rendering further operations impracticable, Operator shall give notice thereof to each  
21 Non-Consenting Party who submitted or voted for an alternative proposal under Article VI.B.6. to drill the well to a  
22 shallower Zone than the deepest objective Zone proposed in the notice under which the well was drilled, and each such Non-  
23 Consenting Party shall have the option to participate in the initial proposed Completion of the well by paying its share of the  
24 cost of drilling the well to its actual depth, calculated in the manner provided in Article VI.B.4. (a). If any such Non-  
25 Consenting Party does not elect to participate in the first Completion proposed for such well, the relinquishment provisions  
26 of this Article VI.B.2. (b) shall apply to such party's interest.

27 (c) Reworking, Recompleting or Plugging Back. An election not to participate in the drilling, Sidetracking or  
28 Deepening of a well shall be deemed an election not to participate in any Reworking or Plugging Back operation proposed in  
29 such a well, or portion thereof, to which the initial non-consent election applied that is conducted at any time prior to full  
30 recovery by the Consenting Parties of the Non-Consenting Party's recoupment amount. Similarly, an election not to  
31 participate in the Completing or Recompleting of a well shall be deemed an election not to participate in any Reworking  
32 operation proposed in such a well, or portion thereof, to which the initial non-consent election applied that is conducted at  
33 any time prior to full recovery by the Consenting Parties of the Non-Consenting Party's recoupment amount. Any such  
34 Reworking, Recompleting or Plugging Back operation conducted during the recoupment period shall be deemed part of the  
35 cost of operation of said well and there shall be added to the sums to be recouped by the Consenting Parties 300 % of  
36 that portion of the costs of the Reworking, Recompleting or Plugging Back operation which would have been chargeable to  
37 such Non-Consenting Party had it participated therein. If such a Reworking, Recompleting or Plugging Back operation is  
38 proposed during such recoupment period, the provisions of this Article VI.B. shall be applicable as between said Consenting  
39 Parties in said well.

40 (d) Recoupment Matters. During the period of time Consenting Parties are entitled to receive Non-Consenting Party's  
41 share of production, or the proceeds therefrom, Consenting Parties shall be responsible for the payment of all ad valorem,  
42 production, severance, excise, gathering and other taxes, and all royalty, overriding royalty and other burdens applicable to  
43 Non-Consenting Party's share of production not excepted by Article III.C.

44 In the case of any Reworking, Sidetracking, Plugging Back, Recompleting or Deepening operation, the Consenting  
45 Parties shall be permitted to use, free of cost, all casing, tubing and other equipment in the well, but the ownership of all  
46 such equipment shall remain unchanged; and upon abandonment of a well after such Reworking, Sidetracking, Plugging Back,  
47 Recompleting or Deepening, the Consenting Parties shall account for all such equipment to the owners thereof, with each  
48 party receiving its proportionate part in kind or in value, less cost of salvage.

49 Within ninety (90) days after the completion of any operation under this Article, the party conducting the operations  
50 for the Consenting Parties shall furnish each Non-Consenting Party with an inventory of the equipment in and connected to  
51 the well, and an itemized statement of the cost of drilling, Sidetracking, Deepening, Plugging Back, testing, Completing,  
52 Recompleting, and equipping the well for production; or, at its option, the operating party, in lieu of an itemized statement  
53 of such costs of operation, may submit a detailed statement of monthly billings. Each month thereafter, during the time the  
54 Consenting Parties are being reimbursed as provided above, the party conducting the operations for the Consenting Parties  
55 shall furnish the Non-Consenting Parties with an itemized statement of all costs and liabilities incurred in the operation of  
56 the well, together with a statement of the quantity of Oil and Gas produced from it and the amount of proceeds realized from  
57 the sale of the well's working interest production during the preceding month. In determining the quantity of Oil and Gas  
58 produced during any month, Consenting Parties shall use industry accepted methods such as but not limited to metering or  
59 periodic well tests. Any amount realized from the sale or other disposition of equipment newly acquired in connection with  
60 any such operation which would have been owned by a Non-Consenting Party had it participated therein shall be credited  
61 against the total unreturned costs of the work done and of the equipment purchased in determining when the interest of such  
62 Non-Consenting Party shall revert to it as above provided; and if there is a credit balance, it shall be paid to such Non-  
63 Consenting Party.

64 If and when the Consenting Parties recover from a Non-Consenting Party's relinquished interest the amounts provided  
65 for above, the relinquished interests of such Non-Consenting Party shall automatically revert to it as of 7:00 a.m. on the day  
66 following the day on which such recoupment occurs, and, from and after such reversion, such Non-Consenting Party shall  
67 own the same interest in such well, the material and equipment in or pertaining thereto, and the production therefrom as  
68 such Non-Consenting Party would have been entitled to had it participated in the drilling, Sidetracking, Reworking,  
69 Deepening, Recompleting or Plugging Back of said well. Thereafter, such Non-Consenting Party shall be charged with and  
70 shall pay its proportionate part of the further costs of the operation of said well in accordance with the terms of this  
71 agreement and Exhibit "C" attached hereto.

72 3. Stand-By Costs: When a well which has been drilled or Deepened has reached its authorized depth and all tests have  
73 been completed and the results thereof furnished to the parties, or when operations on the well have been otherwise  
74 terminated pursuant to Article VI.F., stand-by costs incurred pending response to a party's notice proposing a Reworking,

1 Sidetracking, Deepening, Recompleting, Plugging Back or Completing operation in such a well (including the period required  
 2 under Article VI.B.6. to resolve competing proposals) shall be charged and borne as part of the drilling or Deepening  
 3 operation just completed. Stand-by costs subsequent to all parties responding, or expiration of the response time permitted,  
 4 whichever first occurs, and prior to agreement as to the participating interests of all Consenting Parties pursuant to the terms  
 5 of the second grammatical paragraph of Article VI.B.2. (a), shall be charged to and borne as part of the proposed operation,  
 6 but if the proposal is subsequently withdrawn because of insufficient participation, such stand-by costs shall be allocated  
 7 between the Consenting Parties in the proportion each Consenting Party's interest as shown on Exhibit "A" bears to the total  
 8 interest as shown on Exhibit "A" of all Consenting Parties.

9 In the event that notice for a Sidetracking operation is given while the drilling rig to be utilized is on location, any party  
 10 may request and receive up to five (5) additional days after expiration of the forty-eight hour response period specified in  
 11 Article VI.B.1. within which to respond by paying for all stand-by costs and other costs incurred during such extended  
 12 response period; Operator may require such party to pay the estimated stand-by time in advance as a condition to extending  
 13 the response period. If more than one party elects to take such additional time to respond to the notice, standby costs shall be  
 14 allocated between the parties taking additional time to respond on a day-to-day basis in the proportion each electing party's  
 15 interest as shown on Exhibit "A" bears to the total interest as shown on Exhibit "A" of all the electing parties.

16 4. Deepening: If less than all the parties elect to participate in a drilling, Sidetracking, or Deepening operation proposed  
 17 pursuant to Article VI.B.1., the interest relinquished by the Non-Consenting Parties to the Consenting Parties under Article  
 18 VI.B.2. shall relate only and be limited to the lesser of (i) the total depth actually drilled or (ii) the objective depth or Zone  
 19 of which the parties were given notice under Article VI.B.1. ("Initial Objective"). Such well shall not be Deepened beyond the  
 20 Initial Objective without first complying with this Article to afford the Non-Consenting Parties the opportunity to participate  
 21 in the Deepening operation.

22 In the event any Consenting Party desires to drill or Deepen a Non-Consent Well to a depth below the Initial Objective,  
 23 such party shall give notice thereof, complying with the requirements of Article VI.B.1., to all parties (including Non-  
 24 Consenting Parties). Thereupon, Articles VI.B.1. and 2. shall apply and all parties receiving such notice shall have the right to  
 25 participate or not participate in the Deepening of such well pursuant to said Articles VI.B.1. and 2. If a Deepening operation  
 26 is approved pursuant to such provisions, and if any Non-Consenting Party elects to participate in the Deepening operation,  
 27 such Non-Consenting party shall pay or make reimbursement (as the case may be) of the following costs and expenses:

28 (a) If the proposal to Deepen is made prior to the Completion of such well as a well capable of producing in paying  
 29 quantities, such Non-Consenting Party shall pay (or reimburse Consenting Parties for, as the case may be) that share of costs  
 30 and expenses incurred in connection with the drilling of said well from the surface to the Initial Objective which Non-  
 31 Consenting Party would have paid had such Non-Consenting Party agreed to participate therein, plus the Non-Consenting  
 32 Party's share of the cost of Deepening and of participating in any further operations on the well in accordance with the other  
 33 provisions of this Agreement; provided, however, all costs for testing and Completion or attempted Completion of the well  
 34 incurred by Consenting Parties prior to the point of actual operations to Deepen beyond the Initial Objective shall be for the  
 35 sole account of Consenting Parties.

36 (b) If the proposal is made for a Non-Consent Well that has been previously Completed as a well capable of producing  
 37 in paying quantities, but is no longer capable of producing in paying quantities, such Non-Consenting Party shall pay (or  
 38 reimburse Consenting Parties for, as the case may be) its proportionate share of all costs of drilling, Completing, and  
 39 equipping said well from the surface to the Initial Objective, calculated in the manner provided in paragraph (a) above, less  
 40 those costs recouped by the Consenting Parties from the sale of production from the well. The Non-Consenting Party shall  
 41 also pay its proportionate share of all costs of re-entering said well. The Non-Consenting Parties' proportionate part (based  
 42 on the percentage of such well Non-Consenting Party would have owned had it previously participated in such Non-Consent  
 43 Well) of the costs of salvable materials and equipment remaining in the hole and salvable surface equipment used in  
 44 connection with such well shall be determined in accordance with Exhibit "C." If the Consenting Parties have recouped the  
 45 cost of drilling, Completing, and equipping the well at the time such Deepening operation is conducted, then a Non-  
 46 Consenting Party may participate in the Deepening of the well with no payment for costs incurred prior to re-entering the  
 47 well for Deepening.

48 The foregoing shall not imply a right of any Consenting Party to propose any Deepening for a Non-Consent Well prior  
 49 to the drilling of such well to its Initial Objective without the consent of the other Consenting Parties as provided in Article  
 50 VI.F.

51 5. Sidetracking: Any party having the right to participate in a proposed Sidetracking operation that does not own an  
 52 interest in the affected wellbore at the time of the notice shall, upon electing to participate, tender to the wellbore owners its  
 53 proportionate share (equal to its interest in the Sidetracking operation) of the value of that portion of the existing wellbore  
 54 to be utilized as follows:

55 (a) If the proposal is for Sidetracking an existing dry hole, reimbursement shall be on the basis of the actual costs  
 56 incurred in the initial drilling of the well down to the depth at which the Sidetracking operation is initiated.

57 (b) If the proposal is for Sidetracking a well which has previously produced, reimbursement shall be on the basis of  
 58 such party's proportionate share of drilling and equipping costs incurred in the initial drilling of the well down to the depth  
 59 at which the Sidetracking operation is conducted, calculated in the manner described in Article VI.B.4(b) above. Such party's  
 60 proportionate share of the cost of the well's salvable materials and equipment down to the depth at which the Sidetracking  
 61 operation is initiated shall be determined in accordance with the provisions of Exhibit "C."

62 6. Order of Preference of Operations. Except as otherwise specifically provided in this agreement, if any party desires to  
 63 propose the conduct of an operation that conflicts with a proposal that has been made by a party under this Article VI, such  
 64 party shall have fifteen (15) days from delivery of the initial proposal, in the case of a proposal to drill a well or to perform  
 65 an operation on a well where no drilling rig is on location, or twenty-four (24) hours, exclusive of Saturday, Sunday and legal  
 66 holidays, from delivery of the initial proposal, if a drilling rig is on location for the well on which such operation is to be  
 67 conducted, to deliver to all parties entitled to participate in the proposed operation such party's alternative proposal, such  
 68 alternate proposal to contain the same information required to be included in the initial proposal. Each party receiving such  
 69 proposals shall elect by delivery of notice to Operator within five (5) days after expiration of the proposal period, or within  
 70 twenty-four (24) hours (exclusive of Saturday, Sunday and legal holidays) if a drilling rig is on location for the well that is the  
 71 subject of the proposals, to participate in one of the competing proposals. Any party not electing within the time required  
 72 shall be deemed not to have voted. The proposal receiving the vote of parties owning the largest aggregate percentage  
 73 interest of the parties voting shall have priority over all other competing proposals; in the case of a tie vote, the

Accepted and authorized on behalf of the  
 by the  
 Secretary of the Association of Petroleum Engineers

1 initial proposal shall prevail. Operator shall deliver notice of such result to all parties entitled to participate in the operation  
 2 within five (5) days after expiration of the election period (or within twenty-four (24) hours, exclusive of Saturday, Sunday  
 3 and legal holidays, if a drilling rig is on location). Each party shall then have two (2) days (or twenty-four (24) hours if a rig  
 4 is on location) from receipt of such notice to elect by delivery of notice to Operator to participate in such operation or to  
 5 relinquish interest in the affected well pursuant to the provisions of Article VI.B.2.; failure by a party to deliver notice within  
 6 such period shall be deemed an election not to participate in the prevailing proposal.

7 7. Conformity to Spacing Pattern. Notwithstanding the provisions of this Article VI.B.2., it is agreed that no wells shall be  
 8 proposed to be drilled to or Completed in or produced from a Zone from which a well located elsewhere on the Contract  
 9 Area is producing, unless such well conforms to the then-existing well spacing pattern for such Zone.

10 8. Paying Wells. No party shall conduct any Reworking, Deepening, Plugging Back, Completion, Recompletion, or  
 11 Sidetracking operation under this agreement with respect to any well then capable of producing in paying quantities except  
 12 with the consent of all parties that have not relinquished interests in the well at the time of such operation.

13 **C. Completion of Wells; Reworking and Plugging Back:**

14 1. Completion: Without the consent of all parties, no well shall be drilled, Deepened or Sidetracked, except any well  
 15 drilled, Deepened or Sidetracked pursuant to the provisions of Article VI.B.2. of this agreement. Consent to the drilling,  
 16 Deepening or Sidetracking shall include:

17  Option No. 1: All necessary expenditures for the drilling, Deepening or Sidetracking, testing, Completing and  
 18 equipping of the well, including necessary tankage and/or surface facilities.

19  ~~Option No. 2: All necessary expenditures for the drilling, Deepening or Sidetracking and testing of the well. When~~  
 20 ~~such well has reached its authorized depth, and all logs, cores and other tests have been completed, and the results~~  
 21 ~~thereof furnished to the parties, Operator shall give immediate notice to the Non-Operators having the right to~~  
 22 ~~participate in a Completion attempt whether or not Operator recommends attempting to Complete the well,~~  
 23 ~~together with Operator's AFE for Completion costs if not previously provided. The parties receiving such notice~~  
 24 ~~shall have forty-eight (48) hours (exclusive of Saturday, Sunday and legal holidays) in which to elect by delivery of~~  
 25 ~~notice to Operator to participate in a recommended Completion attempt or to make a Completion proposal with an~~  
 26 ~~accompanying AFE. Operator shall deliver any such Completion proposal, or any Completion proposal conflicting~~  
 27 ~~with Operator's proposal, to the other parties entitled to participate in such Completion in accordance with the~~  
 28 ~~procedures specified in Article VI.B.6. Election to participate in a Completion attempt shall include consent to all~~  
 29 ~~necessary expenditures for the Completing and equipping of such well, including necessary tankage and/or surface~~  
 30 ~~facilities but excluding any stimulation operation not contained on the Completion AFE. Failure of any party~~  
 31 ~~receiving such notice to reply within the period above fixed shall constitute an election by that party not to~~  
 32 ~~participate in the cost of the Completion attempt; provided, that Article VI.B.6. shall control in the case of~~  
 33 ~~conflicting Completion proposals. If one or more, but less than all of the parties, elect to attempt a Completion, the~~  
 34 ~~provisions of Article VI.B.2. hereof (the phrase "Reworking, Sidetracking, Deepening, Recompleting or Plugging~~  
 35 ~~Back" as contained in Article VI.B.2. shall be deemed to include "Completing") shall apply to the operations~~  
 36 ~~thereafter conducted by less than all parties; provided, however, that Article VI.B.2 shall apply separately to each~~  
 37 ~~separate Completion or Recompletion attempt undertaken hereunder, and an election to become a Non-Consenting~~  
 38 ~~Party as to one Completion or Recompletion attempt shall not prevent a party from becoming a Consenting Party~~  
 39 ~~in subsequent Completion or Recompletion attempts regardless whether the Consenting Parties as to earlier~~  
 40 ~~Completions or Recompletions have recouped their costs pursuant to Article VI.B.2.; provided further, that any~~  
 41 ~~recoupment of costs by a Consenting Party shall be made solely from the production attributable to the Zone in~~  
 42 ~~which the Completion attempt is made. Election by a previous Non-Consenting Party to participate in a subsequent~~  
 43 ~~Completion or Recompletion attempt shall require such party to pay its proportionate share of the cost of salvable~~  
 44 ~~materials and equipment installed in the well pursuant to the previous Completion or Recompletion attempt,~~  
 45 ~~insofar and only insofar as such materials and equipment benefit the Zone in which such party participates in a~~  
 46 ~~Completion attempt.~~

47 2. Rework, Recomplete or Plug Back: No well shall be Reworked, Recompleted or Plugged Back except a well Reworked,  
 48 Recompleted, or Plugged Back pursuant to the provisions of Article VI.B.2. of this agreement. Consent to the Reworking,  
 49 Recompleting or Plugging Back of a well shall include all necessary expenditures in conducting such operations and  
 50 Completing and equipping of said well, including necessary tankage and/or surface facilities.

51 **D. Other Operations:**

52 Operator shall not undertake any single project reasonably estimated to require an expenditure in excess of \_\_\_\_\_  
 53 Twenty Thousand----- Dollars (\$ 20,000 ) except in connection with the  
 54 drilling, Sidetracking, Reworking, Deepening, Completing, Recompleting or Plugging Back of a well that has been previously  
 55 authorized by or pursuant to this agreement; provided, however, that, in case of explosion, fire, flood or other sudden  
 56 emergency, whether of the same or different nature, Operator may take such steps and incur such expenses as in its opinion  
 57 are required to deal with the emergency to safeguard life and property but Operator, as promptly as possible, shall report the  
 58 emergency to the other parties. If Operator prepares an AFE for its own use, Operator shall furnish any Non-Operator so  
 59 requesting an information copy thereof for any single project costing in excess of Twenty Thousand----- Dollars  
 60 ( \$ 20,000 ). Any party who has not relinquished its interest in a well shall have the right to propose that  
 61 Operator perform repair work or undertake the installation of artificial lift equipment or ancillary production facilities such as  
 62 salt water disposal wells or to conduct additional work with respect to a well drilled hereunder or other similar project (but  
 63 not including the installation of gathering lines or other transportation or marketing facilities, the installation of which shall  
 64 be governed by separate agreement between the parties) reasonably estimated to require an expenditure in excess of the  
 65 amount first set forth above in this Article VI.D. (except in connection with an operation required to be proposed under  
 66 Articles VI.B.1. or VI.C.1. Option No. 2, which shall be governed exclusively by those Articles). Operator shall deliver such  
 67 proposal to all parties entitled to participate therein. If within thirty (30) days thereof Operator secures the written consent  
 68 of any party or parties owning at least 65 % of the interests of the parties entitled to participate in such operation,  
 69 each party having the right to participate in such project shall be bound by the terms of such proposal and shall be obligated  
 70 to pay its proportionate share of the costs of the proposed project as if it had consented to such project pursuant to the terms  
 71 of the proposal.

72 **E. Abandonment of Wells:**

73 1. Abandonment of Dry Holes: Except for any well drilled or Deepened pursuant to Article VI.B.2., any well which has  
 74 been drilled or Deepened under the terms of this agreement and is proposed to be completed as a dry hole shall not be

1 plugged and abandoned without the consent of all parties. Should Operator, after diligent effort, be unable to contact any  
 2 party, or should any party fail to reply within forty-eight (48) hours (exclusive of Saturday, Sunday and legal holidays) after  
 3 delivery of notice of the proposal to plug and abandon such well, such party shall be deemed to have consented to the  
 4 proposed abandonment. All such wells shall be plugged and abandoned in accordance with applicable regulations and at the  
 5 cost, risk and expense of the parties who participated in the cost of drilling or Deepening such well. Any party who objects to  
 6 plugging and abandoning such well by notice delivered to Operator within forty-eight (48) hours (exclusive of Saturday,  
 7 Sunday and legal holidays) after delivery of notice of the proposed plugging shall take over the well as of the end of such  
 8 forty-eight (48) hour notice period and conduct further operations in search of Oil and/or Gas subject to the provisions of  
 9 Article VI.B.; failure of such party to provide proof reasonably satisfactory to Operator of its financial capability to conduct  
 10 such operations or to take over the well within such period or thereafter to conduct operations on such well or plug and  
 11 abandon such well shall entitle Operator to retain or take possession of the well and plug and abandon the well. The party  
 12 taking over the well shall indemnify Operator (if Operator is an abandoning party) and the other abandoning parties against  
 13 liability for any further operations conducted on such well except for the costs of plugging and abandoning the well and  
 14 restoring the surface, for which the abandoning parties shall remain proportionately liable.

15 2. Abandonment of Wells That Have Produced: Except for any well in which a Non-Consent operation has been  
 16 conducted hereunder for which the Consenting Parties have not been fully reimbursed as herein provided, any well which has  
 17 been completed as a producer shall not be plugged and abandoned without the consent of all parties. If all parties consent to  
 18 such abandonment, the well shall be plugged and abandoned in accordance with applicable regulations and at the cost, risk  
 19 and expense of all the parties hereto. Failure of a party to reply within sixty (60) days of delivery of notice of proposed  
 20 abandonment shall be deemed an election to consent to the proposal. If, within sixty (60) days after delivery of notice of the  
 21 proposed abandonment of any well, all parties do not agree to the abandonment of such well, those wishing to continue its  
 22 operation from the Zone then open to production shall be obligated to take over the well as of the expiration of the  
 23 applicable notice period and shall indemnify Operator (if Operator is an abandoning party) and the other abandoning parties  
 24 against liability for any further operations on the well conducted by such parties. Failure of such party or parties to provide  
 25 proof reasonably satisfactory to Operator of their financial capability to conduct such operations or to take over the well  
 26 within the required period or thereafter to conduct operations on such well shall entitle Operator to retain or take possession  
 27 of such well and plug and abandon the well.

28 Parties taking over a well as provided herein shall tender to each of the other parties its proportionate share of the value of  
 29 the well's salvable material and equipment, determined in accordance with the provisions of Exhibit "C," less the estimated cost  
 30 of salvaging and the estimated cost of plugging and abandoning and restoring the surface; provided, however, that in the event  
 31 the estimated plugging and abandoning and surface restoration costs and the estimated cost of salvaging are higher than the  
 32 value of the well's salvable material and equipment, each of the abandoning parties shall tender to the parties continuing  
 33 operations their proportionate shares of the estimated excess cost. Each abandoning party shall assign to the non-abandoning  
 34 parties, without warranty, express or implied, as to title or as to quantity, or fitness for use of the equipment and material, all  
 35 of its interest in the wellbore of the well and related equipment, together with its interest in the Leasehold insofar and only  
 36 insofar as such Leasehold covers the right to obtain production from that wellbore in the Zone then open to production. If the  
 37 interest of the abandoning party is or includes an Oil and Gas Interest, such party shall execute and deliver to the non-  
 38 abandoning party or parties an oil and gas lease, limited to the wellbore and the Zone then open to production, for a term of  
 39 one (1) year and so long thereafter as Oil and/or Gas is produced from the Zone covered thereby, such lease to be on the form  
 40 attached as Exhibit "B." The assignments or leases so limited shall encompass the Drilling Unit upon which the well is located.  
 41 The payments by, and the assignments or leases to, the assignees shall be in a ratio based upon the relationship of their  
 42 respective percentage of participation in the Contract Area to the aggregate of the percentages of participation in the Contract  
 43 Area of all assignees. There shall be no readjustment of interests in the remaining portions of the Contract Area.

44 Thereafter, abandoning parties shall have no further responsibility, liability, or interest in the operation of or production  
 45 from the well in the Zone then open other than the royalties retained in any lease made under the terms of this Article. Upon  
 46 request, Operator shall continue to operate the assigned well for the account of the non-abandoning parties at the rates and  
 47 charges contemplated by this agreement, plus any additional cost and charges which may arise as the result of the separate  
 48 ownership of the assigned well. Upon proposed abandonment of the producing Zone assigned or leased, the assignor or lessor  
 49 shall then have the option to repurchase its prior interest in the well (using the same valuation formula) and participate in  
 50 further operations therein subject to the provisions hereof.

51 3. Abandonment of Non-Consent Operations: The provisions of Article VI.E.1. or VI.E.2. above shall be applicable as  
 52 between Consenting Parties in the event of the proposed abandonment of any well excepted from said Articles; provided,  
 53 however, no well shall be permanently plugged and abandoned unless and until all parties having the right to conduct further  
 54 operations therein have been notified of the proposed abandonment and afforded the opportunity to elect to take over the well  
 55 in accordance with the provisions of this Article VI.E.; and provided further, that Non-Consenting Parties who own an interest  
 56 in a portion of the well shall pay their proportionate shares of abandonment and surface restoration costs for such well as  
 57 provided in Article VI.B.2.(b).

58 **F. Termination of Operations:**

59 Upon the commencement of an operation for the drilling, Reworking, Sidetracking, Plugging Back, Deepening, testing,  
 60 Completion or plugging of a well, including but not limited to the Initial Well, such operation shall not be terminated without  
 61 consent of parties bearing 65 % of the costs of such operation; provided, however, that in the event granite or other  
 62 practically impenetrable substance or condition in the hole is encountered which renders further operations impractical,  
 63 Operator may discontinue operations and give notice of such condition in the manner provided in Article VI.B.1, and the  
 64 provisions of Article VI.B. or VI.E. shall thereafter apply to such operation, as appropriate.

65 **G. Taking Production in Kind:**

66  Option No. 1: Gas Balancing Agreement Attached

67 Each party shall take in kind or separately dispose of its proportionate share of all Oil and Gas produced from the  
 68 Contract Area, exclusive of production which may be used in development and producing operations and in preparing and  
 69 treating Oil and Gas for marketing purposes and production unavoidably lost. Any extra expenditure incurred in the taking  
 70 in kind or separate disposition by any party of its proportionate share of the production shall be borne by such party. Any  
 71 party taking its share of production in kind shall be required to pay for only its proportionate share of such part of  
 72 Operator's surface facilities which it uses.

73 Each party shall execute such division orders and contracts as may be necessary for the sale of its interest in  
 74 production from the Contract Area, and, except as provided in Article VII.B., shall be entitled to receive payment

1 directly from the purchaser thereof for its share of all production.

2 If any party fails to make the arrangements necessary to take in kind or separately dispose of its proportionate  
3 share of the Oil produced from the Contract Area, Operator shall have the right, subject to the revocation at will by  
4 the party owning it, but not the obligation, to purchase such Oil or sell it to others at any time and from time to  
5 time, for the account of the non-taking party. Any such purchase or sale by Operator may be terminated by  
6 Operator upon at least ten (10) days written notice to the owner of said production and shall be subject always to  
7 the right of the owner of the production upon at least ten (10) days written notice to Operator to exercise at any  
8 time its right to take in kind, or separately dispose of, its share of all Oil not previously delivered to a purchaser.  
9 Any purchase or sale by Operator of any other party's share of Oil shall be only for such reasonable periods of time  
10 as are consistent with the minimum needs of the industry under the particular circumstances, but in no event for a  
11 period in excess of one (1) year.

12 Any such sale by Operator shall be in a manner commercially reasonable under the circumstances but Operator  
13 shall have no duty to share any existing market or to obtain a price equal to that received under any existing  
14 market. The sale or delivery by Operator of a non-taking party's share of Oil under the terms of any existing  
15 contract of Operator shall not give the non-taking party any interest in or make the non-taking party a party to said  
16 contract. No purchase shall be made by Operator without first giving the non-taking party at least ten (10) days  
17 written notice of such intended purchase and the price to be paid or the pricing basis to be used.

18 All parties shall give timely written notice to Operator of their Gas marketing arrangements for the following  
19 month, excluding price, and shall notify Operator immediately in the event of a change in such arrangements.  
20 Operator shall maintain records of all marketing arrangements, and of volumes actually sold or transported, which  
21 records shall be made available to Non-Operators upon reasonable request.

22 In the event one or more parties' separate disposition of its share of the Gas causes split-stream deliveries to separate  
23 pipelines and/or deliveries which on a day-to-day basis for any reason are not exactly equal to a party's respective proportion-  
24 ate share of total Gas sales to be allocated to it, the balancing or accounting between the parties shall be in accordance with  
25 any Gas balancing agreement between the parties hereto, whether such an agreement is attached as Exhibit "E" or is a  
26 separate agreement. Operator shall give notice to all parties of the first sales of Gas from any well under this agreement.

27  ~~Option No. 2: No Gas Balancing Agreement:~~

28 ~~Each party shall take in kind or separately dispose of its proportionate share of all Oil and Gas produced from  
29 the Contract Area, exclusive of production which may be used in development and producing operations and in  
30 preparing and treating Oil and Gas for marketing purposes and production unavoidably lost. Any extra expenditure  
31 incurred in the taking in kind or separate disposition by any party of its proportionate share of the production shall  
32 be borne by such party. Any party taking its share of production in kind shall be required to pay for only its  
33 proportionate share of such part of Operator's surface facilities which it uses.~~

34 ~~Each party shall execute such division orders and contracts as may be necessary for the sale of its interest in  
35 production from the Contract Area, and, except as provided in Article VII.B., shall be entitled to receive payment  
36 directly from the purchaser thereof for its share of all production.~~

37 ~~If any party fails to make the arrangements necessary to take in kind or separately dispose of its proportionate  
38 share of the Oil and/or Gas produced from the Contract Area, Operator shall have the right, subject to the  
39 revocation at will by the party owning it, but not the obligation, to purchase such Oil and/or Gas or sell it to others  
40 at any time and from time to time, for the account of the non-taking party. Any such purchase or sale by Operator  
41 may be terminated by Operator upon at least ten (10) days written notice to the owner of said production and shall  
42 be subject always to the right of the owner of the production upon at least ten (10) days written notice to Operator  
43 to exercise its right to take in kind, or separately dispose of, its share of all Oil and/or Gas not previously delivered  
44 to a purchaser; provided, however, that the effective date of any such revocation may be deferred at Operator's  
45 election for a period not to exceed ninety (90) days if Operator has committed such production to a purchase  
46 contract having a term extending beyond such ten (10) -day period. Any purchase or sale by Operator of any other  
47 party's share of Oil and/or Gas shall be only for such reasonable periods of time as are consistent with the  
48 minimum needs of the industry under the particular circumstances, but in no event for a period in excess of one (1)  
49 year.~~

50 ~~Any such sale by Operator shall be in a manner commercially reasonable under the circumstances, but Operator  
51 shall have no duty to share any existing market or transportation arrangement or to obtain a price or transportation  
52 fee equal to that received under any existing market or transportation arrangement. The sale or delivery by  
53 Operator of a non-taking party's share of production under the terms of any existing contract of Operator shall not  
54 give the non-taking party any interest in or make the non-taking party a party to said contract. No purchase of Oil  
55 and Gas and no sale of Gas shall be made by Operator without first giving the non-taking party ten days written  
56 notice of such intended purchase or sale and the price to be paid or the pricing basis to be used. Operator shall give  
57 notice to all parties of the first sale of Gas from any well under this Agreement.~~

58 ~~All parties shall give timely written notice to Operator of their Gas marketing arrangements for the following  
59 month, excluding price, and shall notify Operator immediately in the event of a change in such arrangements.  
60 Operator shall maintain records of all marketing arrangements, and of volumes actually sold or transported, which  
61 records shall be made available to Non-Operators upon reasonable request.~~

62 **ARTICLE VII.**

63 **EXPENDITURES AND LIABILITY OF PARTIES**

64 **A. Liability of Parties:**

65 The liability of the parties shall be several, not joint or collective. Each party shall be responsible only for its obligations,  
66 and shall be liable only for its proportionate share of the costs of developing and operating the Contract Area. Accordingly, the  
67 liens granted among the parties in Article VII.B. are given to secure only the debts of each severally, and no party shall have  
68 any liability to third parties hereunder to satisfy the default of any other party in the payment of any expense or obligation  
69 hereunder. It is not the intention of the parties to create, nor shall this agreement be construed as creating, a mining or other  
70 partnership, joint venture, agency relationship or association, or to render the parties liable as partners, co-venturers, or  
71 principals. In their relations with each other under this agreement, the parties shall not be considered fiduciaries or to have  
72 established a confidential relationship but rather shall be free to act on an arm's-length basis in accordance with their own  
73 respective self-interest, subject, however, to the obligation of the parties to act in good faith in their dealings with each other  
74 with respect to activities hereunder.

1 **B. Liens and Security Interests:**

2 Each party grants to the other parties hereto a lien upon any interest it now owns or hereafter acquires in Oil and Gas  
3 Leases and Oil and Gas Interests in the Contract Area, and a security interest and/or purchase money security interest in any  
4 interest it now owns or hereafter acquires in the personal property and fixtures on or used or obtained for use in connection  
5 therewith, to secure performance of all of its obligations under this agreement including but not limited to payment of expense,  
6 interest and fees, the proper disbursement of all monies paid hereunder, the assignment or relinquishment of interest in Oil  
7 and Gas Leases as required hereunder, and the proper performance of operations hereunder. Such lien and security interest  
8 granted by each party hereto shall include such party's leasehold interests, working interests, operating rights, and royalty and  
9 overriding royalty interests in the Contract Area now owned or hereafter acquired and in lands pooled or unitized therewith or  
10 otherwise becoming subject to this agreement, the Oil and Gas when extracted therefrom and equipment situated thereon or  
11 used or obtained for use in connection therewith (including, without limitation, all wells, tools, and tubular goods), and accounts  
12 (including, without limitation, accounts arising from gas imbalances or from the sale of Oil and/or Gas at the wellhead),  
13 contract rights, inventory and general intangibles relating thereto or arising therefrom, and all proceeds and products of the  
14 foregoing.

15 To perfect the lien and security agreement provided herein, each party hereto shall execute and acknowledge the recording  
16 supplement and/or any financing statement prepared and submitted by any party hereto in conjunction herewith or at any time  
17 following execution hereof, and Operator is authorized to file this agreement or the recording supplement executed herewith as  
18 a lien or mortgage in the applicable real estate records and as a financing statement with the proper officer under the Uniform  
19 Commercial Code in the state in which the Contract Area is situated and such other states as Operator shall deem appropriate  
20 to perfect the security interest granted hereunder. Any party may file this agreement, the recording supplement executed  
21 herewith, or such other documents as it deems necessary as a lien or mortgage in the applicable real estate records and/or a  
22 financing statement with the proper officer under the Uniform Commercial Code.

23 Each party represents and warrants to the other parties hereto that the lien and security interest granted by such party to  
24 the other parties shall be a first and prior lien, and each party hereby agrees to maintain the priority of said lien and security  
25 interest against all persons acquiring an interest in Oil and Gas Leases and Interests covered by this agreement by, through or  
26 under such party. All parties acquiring an interest in Oil and Gas Leases and Oil and Gas Interests covered by this agreement,  
27 whether by assignment, merger, mortgage, operation of law, or otherwise, shall be deemed to have taken subject  
28 to the lien and security interest granted by this Article VII.B. as to all obligations attributable to such interest hereunder  
29 whether or not such obligations arise before or after such interest is acquired.

30 To the extent that parties have a security interest under the Uniform Commercial Code of the state in which the  
31 Contract Area is situated, they shall be entitled to exercise the rights and remedies of a secured party under the Code.  
32 The bringing of a suit and the obtaining of judgment by a party for the secured indebtedness shall not be deemed an  
33 election of remedies or otherwise affect the lien rights or security interest as security for the payment thereof. In  
34 addition, upon default by any party in the payment of its share of expenses, interests or fees, or upon the improper use  
35 of funds by the Operator, the other parties shall have the right, without prejudice to other rights or remedies, to collect  
36 from the purchaser the proceeds from the sale of such defaulting party's share of Oil and Gas until the amount owed by  
37 such party, plus interest as provided in "Exhibit C," has been received, and shall have the right to offset the amount  
38 owed against the proceeds from the sale of such defaulting party's share of Oil and Gas. All purchasers of production  
39 may rely on a notification of default from the non-defaulting party or parties stating the amount due as a result of the  
40 default, and all parties waive any recourse available against purchasers for releasing production proceeds as provided in  
41 this paragraph.

42 If any party fails to pay its share of cost within one hundred twenty (120) days after rendition of a statement therefor by  
43 Operator, the non-defaulting parties, including Operator, shall, upon request by Operator, pay the unpaid amount in the  
44 proportion that the interest of each such party bears to the interest of all such parties. The amount paid by each party so  
45 paying its share of the unpaid amount shall be secured by the liens and security rights described in Article VII.B., and each  
46 paying party may independently pursue any remedy available hereunder or otherwise.

47 If any party does not perform all of its obligations hereunder, and the failure to perform subjects such party to foreclosure  
48 or execution proceedings pursuant to the provisions of this agreement, to the extent allowed by governing law, the defaulting  
49 party waives any available right of redemption from and after the date of judgment, any required valuation or appraisal  
50 of the mortgaged or secured property prior to sale, any available right to stay execution or to require a marshalling of assets  
51 and any required bond in the event a receiver is appointed. In addition, to the extent permitted by applicable law, each party  
52 hereby grants to the other parties a power of sale as to any property that is subject to the lien and security rights granted  
53 hereunder, such power to be exercised in the manner provided by applicable law or otherwise in a commercially reasonable  
54 manner and upon reasonable notice.

55 Each party agrees that the other parties shall be entitled to utilize the provisions of Oil and Gas lien law or other lien  
56 law of any state in which the Contract Area is situated to enforce the obligations of each party hereunder. Without limiting  
57 the generality of the foregoing, to the extent permitted by applicable law, Non-Operators agree that Operator may invoke or  
58 utilize the mechanics' or materialmen's lien law of the state in which the Contract Area is situated in order to secure the  
59 payment to Operator of any sum due hereunder for services performed or materials supplied by Operator.

60 **C. Advances:**

61 Operator, at its election, shall have the right from time to time to demand and receive from one or more of the other  
62 parties payment in advance of their respective shares of the estimated amount of the expense to be incurred in operations  
63 hereunder during the next succeeding month, which right may be exercised only by submission to each such party of an  
64 itemized statement of such estimated expense, together with an invoice for its share thereof. Each such statement and invoice  
65 for the payment in advance of estimated expense shall be submitted on or before the 20th day of the next preceding month.  
66 Each party shall pay to Operator its proportionate share of such estimate within fifteen (15) days after such estimate and  
67 invoice is received. If any party fails to pay its share of said estimate within said time, the amount due shall bear interest as  
68 provided in Exhibit "C" until paid. Proper adjustment shall be made monthly between advances and actual expense to the end  
69 that each party shall bear and pay its proportionate share of actual expenses incurred, and no more.

70 **D. Defaults and Remedies:**

71 If any party fails to discharge any financial obligation under this agreement, including without limitation the failure to  
72 make any advance under the preceding Article VII.C. or any other provision of this agreement, within the period required for  
73 such payment hereunder, then in addition to the remedies provided in Article VII.B. or elsewhere in this agreement, the  
74 remedies specified below shall be applicable. For purposes of this Article VII.D., all notices and elections shall be delivered

1 only by Operator, except that Operator shall deliver any such notice and election requested by a non-defaulting Non-Operator,  
2 and when Operator is the party in default, the applicable notices and elections can be delivered by any Non-Operator.  
3 Election of any one or more of the following remedies shall not preclude the subsequent use of any other remedy specified  
4 below or otherwise available to a non-defaulting party.

5 1. Suspension of Rights: Any party may deliver to the party in default a Notice of Default, which shall specify the default,  
6 specify the action to be taken to cure the default, and specify that failure to take such action will result in the exercise of one  
7 or more of the remedies provided in this Article. If the default is not cured within thirty (30) days of the delivery of such  
8 Notice of Default, all of the rights of the defaulting party granted by this agreement may upon notice be suspended until the  
9 default is cured, without prejudice to the right of the non-defaulting party or parties to continue to enforce the obligations of  
10 the defaulting party previously accrued or thereafter accruing under this agreement. If Operator is the party in default, the  
11 Non-Operators shall have in addition the right, by vote of Non-Operators owning a majority in interest in the Contract Area  
12 after excluding the voting interest of Operator, to appoint a new Operator effective immediately. The rights of a defaulting  
13 party that may be suspended hereunder at the election of the non-defaulting parties shall include, without limitation, the right  
14 to receive information as to any operation conducted hereunder during the period of such default, the right to elect to  
15 participate in an operation proposed under Article VI.B. of this agreement, the right to participate in an operation being  
16 conducted under this agreement even if the party has previously elected to participate in such operation, and the right to  
17 receive proceeds of production from any well subject to this agreement.

18 2. Suit for Damages: Non-defaulting parties or Operator for the benefit of non-defaulting parties may sue (at joint  
19 account expense) to collect the amounts in default, plus interest accruing on the amounts recovered from the date of default  
20 until the date of collection at the rate specified in Exhibit "C" attached hereto. Nothing herein shall prevent any party from  
21 suing any defaulting party to collect consequential damages accruing to such party as a result of the default.

22 3. Deemed Non-Consent: The non-defaulting party may deliver a written Notice of Non-Consent Election to the  
23 defaulting party at any time after the expiration of the thirty-day cure period following delivery of the Notice of Default, in  
24 which event if the billing is for the drilling of a new well or the Plugging Back, Sidetracking, Reworking or Deepening of a  
25 well which is to be or has been plugged as a dry hole, or for the Completion or Recompletion of any well, the defaulting  
26 party will be conclusively deemed to have elected not to participate in the operation and to be a Non-Consenting Party with  
27 respect thereto under Article VI.B. or VI.C., as the case may be, to the extent of the costs unpaid by such party,  
28 notwithstanding any election to participate theretofore made. If election is made to proceed under this provision, then the  
29 non-defaulting parties may not elect to sue for the unpaid amount pursuant to Article VII.D.2.

30 Until the delivery of such Notice of Non-Consent Election to the defaulting party, such party shall have the right to cure  
31 its default by paying its unpaid share of costs plus interest at the rate set forth in Exhibit "C," provided, however, such  
32 payment shall not prejudice the rights of the non-defaulting parties to pursue remedies for damages incurred by the non-  
33 defaulting parties as a result of the default. Any interest relinquished pursuant to this Article VII.D.3. shall be offered to the  
34 non-defaulting parties in proportion to their interests, and the non-defaulting parties electing to participate in the ownership  
35 of such interest shall be required to contribute their shares of the defaulted amount upon their election to participate therein.

36 4. Advance Payment: If a default is not cured within thirty (30) days of the delivery of a Notice of Default, Operator, or  
37 Non-Operators if Operator is the defaulting party, may thereafter require advance payment from the defaulting  
38 party of such defaulting party's anticipated share of any item of expense for which Operator, or Non-Operators, as the case may  
39 be, would be entitled to reimbursement under any provision of this agreement, whether or not such expense was the subject of  
40 the previous default. Such right includes, but is not limited to, the right to require advance payment for the estimated costs of  
41 drilling a well or Completion of a well as to which an election to participate in drilling or Completion has been made. If the  
42 defaulting party fails to pay the required advance payment, the non-defaulting parties may pursue any of the remedies provided  
43 in this Article VII.D. or any other default remedy provided elsewhere in this agreement. Any excess of funds advanced remaining  
44 when the operation is completed and all costs have been paid shall be promptly returned to the advancing party.

45 5. Costs and Attorneys' Fees. In the event any party is required to bring legal proceedings to enforce any financial  
46 obligation of a party hereunder, the prevailing party in such action shall be entitled to recover all court costs, costs of  
47 collection, and a reasonable attorney's fee, which the lien provided for herein shall also secure.

48 **E. Rentals, Shut-in Well Payments and Minimum Royalties:**

49 Rentals, shut-in well payments and minimum royalties which may be required under the terms of any lease shall be paid  
50 by the party or parties who subjected such lease to this agreement at its or their expense. In the event two or more parties  
51 own and have contributed interests in the same lease to this agreement, such parties may designate one of such parties to  
52 make said payments for and on behalf of all such parties. Any party may request, and shall be entitled to receive, proper  
53 evidence of all such payments. In the event of failure to make proper payment of any rental, shut-in well payment or  
54 minimum royalty through mistake or oversight where such payment is required to continue the lease in force, any loss which  
55 results from such non-payment shall be borne in accordance with the provisions of Article IV.B.2.

56 Operator shall notify Non-Operators of the anticipated completion of a shut-in well, or the shutting in or return to  
57 production of a producing well, at least five (5) days (excluding Saturday, Sunday and legal holidays) prior to taking such  
58 action, or at the earliest opportunity permitted by circumstances, but assumes no liability for failure to do so. In the event of  
59 failure by Operator to so notify Non-Operators, the loss of any lease contributed hereto by Non-Operators for failure to make  
60 timely payments of any shut-in well payment shall be borne jointly by the parties hereto under the provisions of Article  
61 IV.B.3.

62 **F. Taxes:**

63 Beginning with the first calendar year after the effective date hereof, Operator shall render for ad valorem taxation all  
64 property subject to this agreement which by law should be rendered for such taxes, and it shall pay all such taxes assessed  
65 thereon before they become delinquent. Prior to the rendition date, each Non-Operator shall furnish Operator information as  
66 to burdens (to include, but not be limited to, royalties, overriding royalties and production payments) on Leases and Oil and  
67 Gas Interests contributed by such Non-Operator. If the assessed valuation of any Lease is reduced by reason of its being  
68 subject to outstanding excess royalties, overriding royalties or production payments, the reduction in ad valorem taxes  
69 resulting therefrom shall inure to the benefit of the owner or owners of such Lease, and Operator shall adjust the charge to  
70 such owner or owners so as to reflect the benefit of such reduction. If the ad valorem taxes are based in whole or in part  
71 upon separate valuations of each party's working interest, then notwithstanding anything to the contrary herein, charges to  
72 the joint account shall be made and paid by the parties hereto in accordance with the tax value generated by each party's  
73 working interest. Operator shall bill the other parties for their proportionate shares of all tax payments in the manner  
74 provided in Exhibit "C."

1 If Operator considers any tax assessment improper, Operator may, at its discretion, protest within the time and manner  
2 prescribed by law, and prosecute the protest to a final determination, unless all parties agree to abandon the protest prior to final  
3 determination. During the pendency of administrative or judicial proceedings, Operator may elect to pay, under protest, all such taxes  
4 and any interest and penalty. When any such protested assessment shall have been finally determined, Operator shall pay the tax for  
5 the joint account, together with any interest and penalty accrued, and the total cost shall then be assessed against the parties, and be  
6 paid by them, as provided in Exhibit "C."

7 Each party shall pay or cause to be paid all production, severance, excise, gathering and other taxes imposed upon or with respect  
8 to the production or handling of such party's share of Oil and Gas produced under the terms of this agreement.

9 **ARTICLE VIII.**

10 **ACQUISITION, MAINTENANCE OR TRANSFER OF INTEREST**

11 **A. Surrender of Leases:**

12 The Leases covered by this agreement, insofar as they embrace acreage in the Contract Area, shall not be surrendered in whole  
13 or in part unless all parties consent thereto.

14 However, should any party desire to surrender its interest in any Lease or in any portion thereof, such party shall give written  
15 notice of the proposed surrender to all parties, and the parties to whom such notice is delivered shall have thirty (30) days after  
16 delivery of the notice within which to notify the party proposing the surrender whether they elect to consent thereto. Failure of a  
17 party to whom such notice is delivered to reply within said 30-day period shall constitute a consent to the surrender of the Leases  
18 described in the notice. If all parties do not agree or consent thereto, the party desiring to surrender shall assign, without express or  
19 implied warranty of title, all of its interest in such Lease, or portion thereof, and any well, material and equipment which may be  
20 located thereon and any rights in production thereafter secured, to the parties not consenting to such surrender. If the interest of the  
21 assigning party is or includes an Oil and Gas Interest, the assigning party shall execute and deliver to the party or parties not  
22 consenting to such surrender an oil and gas lease covering such Oil and Gas Interest for a term of one (1) year and so long  
23 thereafter as Oil and/or Gas is produced from the land covered thereby, such lease to be on the form attached hereto as Exhibit "B."  
24 Upon such assignment or lease, the assigning party shall be relieved from all obligations thereafter accruing, but not theretofore  
25 accrued, with respect to the interest assigned or leased and the operation of any well attributable thereto, and the assigning party  
26 shall have no further interest in the assigned or leased premises and its equipment and production other than the royalties retained  
27 in any lease made under the terms of this Article. The party assignee or lessee shall pay to the party assignor or lessor the  
28 reasonable salvage value of the latter's interest in any well's salvable materials and equipment attributable to the assigned or leased  
29 acreage. The value of all salvable materials and equipment shall be determined in accordance with the provisions of Exhibit "C," less  
30 the estimated cost of salvaging and the estimated cost of plugging and abandoning and restoring the surface. If such value is less  
31 than such costs, then the party assignor or lessor shall pay to the party assignee or lessee the amount of such deficit. If the  
32 assignment or lease is in favor of more than one party, the interest shall be shared by such parties in the proportions that the  
33 interest of each bears to the total interest of all such parties. If the interest of the parties to whom the assignment is to be made  
34 varies according to depth, then the interest assigned shall similarly reflect such variances.

35 Any assignment, lease or surrender made under this provision shall not reduce or change the assignor's, lessor's or surrendering  
36 party's interest as it was immediately before the assignment, lease or surrender in the balance of the Contract Area; and the acreage  
37 assigned, leased or surrendered, and subsequent operations thereon, shall not thereafter be subject to the terms and provisions of this  
38 agreement but shall be deemed subject to an Operating Agreement in the form of this agreement.

39 **B. Renewal or Extension of Leases:**

40 If any party secures a renewal or replacement of an Oil and Gas Lease or Interest subject to this agreement, then all other parties  
41 shall be notified promptly upon such acquisition or, in the case of a replacement Lease taken before expiration of an existing Lease,  
42 promptly upon expiration of the existing Lease. The parties notified shall have the right for a period of thirty (30) days following  
43 delivery of such notice in which to elect to participate in the ownership of the renewal or replacement Lease, insofar as such Lease  
44 affects lands within the Contract Area, by paying to the party who acquired it their proportionate shares of the acquisition cost  
45 allocated to that part of such Lease within the Contract Area, which shall be in proportion to the interests held at that time by the  
46 parties in the Contract Area. Each party who participates in the purchase of a renewal or replacement Lease shall be given an  
47 assignment of its proportionate interest therein by the acquiring party.

48 If some, but less than all, of the parties elect to participate in the purchase of a renewal or replacement Lease, it shall be owned  
49 by the parties who elect to participate therein, in a ratio based upon the relationship of their respective percentage of participation in  
50 the Contract Area to the aggregate of the percentages of participation in the Contract Area of all parties participating in the  
51 purchase of such renewal or replacement Lease. The acquisition of a renewal or replacement Lease by any or all of the parties hereto  
52 shall not cause a readjustment of the interests of the parties stated in Exhibit "A," but any renewal or replacement Lease in which  
53 less than all parties elect to participate shall not be subject to this agreement but shall be deemed subject to a separate Operating  
54 Agreement in the form of this agreement.

55 If the interests of the parties in the Contract Area vary according to depth, then their right to participate proportionately in  
56 renewal or replacement Leases and their right to receive an assignment of interest shall also reflect such depth variances.

57 The provisions of this Article shall apply to renewal or replacement Leases whether they are for the entire interest covered by  
58 the expiring Lease or cover only a portion of its area or an interest therein. Any renewal or replacement Lease taken before the  
59 expiration of its predecessor Lease, or taken or contracted for or becoming effective within six (6) months after the expiration of the  
60 existing Lease, shall be subject to this provision so long as this agreement is in effect at the time of such acquisition or at the time  
61 the renewal or replacement Lease becomes effective; but any Lease taken or contracted for more than six (6) months after the  
62 expiration of an existing Lease shall not be deemed a renewal or replacement Lease and shall not be subject to the provisions of this  
63 agreement.

64 The provisions in this Article shall also be applicable to extensions of Oil and Gas Leases.

65 **C. Acreage or Cash Contributions:**

66 While this agreement is in force, if any party contracts for a contribution of cash towards the drilling of a well or any other  
67 operation on the Contract Area, such contribution shall be paid to the party who conducted the drilling or other operation and shall  
68 be applied by it against the cost of such drilling or other operation. If the contribution be in the form of acreage, the party to whom  
69 the contribution is made shall promptly tender an assignment of the acreage, without warranty of title, to the Drilling Parties in the  
70 proportions said Drilling Parties shared the cost of drilling the well. Such acreage shall become a separate Contract Area and, to the  
71 extent possible, be governed by provisions identical to this agreement. Each party shall promptly notify all other parties of any  
72 acreage or cash contributions it may obtain in support of any well or any other operation on the Contract Area. The above  
73 provisions shall also be applicable to optional rights to earn acreage outside the Contract Area which are in support of well drilled  
74 inside the Contract Area.

1 If any party contracts for any consideration relating to disposition of such party's share of substances produced hereunder,  
2 such consideration shall not be deemed a contribution as contemplated in this Article VIII.C.

3 **D. Assignment; Maintenance of Uniform Interest:**

4 For the purpose of maintaining uniformity of ownership in the Contract Area in the Oil and Gas Leases, Oil and Gas  
5 Interests, wells, equipment and production covered by this agreement no party shall sell, encumber, transfer or make other  
6 disposition of its interest in the Oil and Gas Leases and Oil and Gas Interests embraced within the Contract Area or in wells,  
7 equipment and production unless such disposition covers either:

- 8 1. the entire interest of the party in all Oil and Gas Leases, Oil and Gas Interests, wells, equipment and production; or
- 9 2. an equal undivided percent of the party's present interest in all Oil and Gas Leases, Oil and Gas Interests, wells,  
10 equipment and production in the Contract Area.

11 Every sale, encumbrance, transfer or other disposition made by any party shall be made expressly subject to this agreement  
12 and shall be made without prejudice to the right of the other parties, and any transferee of an ownership interest in any Oil and  
13 Gas Lease or Interest shall be deemed a party to this agreement as to the interest conveyed from and after the effective date of  
14 the transfer of ownership; provided, however, that the other parties shall not be required to recognize any such sale,  
15 encumbrance, transfer or other disposition for any purpose hereunder until thirty (30) days after they have received a copy of the  
16 instrument of transfer or other satisfactory evidence thereof in writing from the transferor or transferee. No assignment or other  
17 disposition of interest by a party shall relieve such party of obligations previously incurred by such party hereunder with respect  
18 to the interest transferred, including without limitation the obligation of a party to pay all costs attributable to an operation  
19 conducted hereunder in which such party has agreed to participate prior to making such assignment, and the lien and security  
20 interest granted by Article VII.B. shall continue to burden the interest transferred to secure payment of any such obligations.

21 If, at any time the interest of any party is divided among and owned by four or more co-owners, Operator, at its discretion,  
22 may require such co-owners to appoint a single trustee or agent with full authority to receive notices, approve expenditures,  
23 receive billings for and approve and pay such party's share of the joint expenses, and to deal generally with, and with power to  
24 bind, the co-owners of such party's interest within the scope of the operations embraced in this agreement; however, all such co-  
25 owners shall have the right to enter into and execute all contracts or agreements for the disposition of their respective shares of  
26 the Oil and Gas produced from the Contract Area and they shall have the right to receive, separately, payment of the sale  
27 proceeds thereof.

28 **E. Waiver of Rights to Partition:**

29 If permitted by the laws of the state or states in which the property covered hereby is located, each party hereto owning an  
30 undivided interest in the Contract Area waives any and all rights it may have to partition and have set aside to it in severalty its  
31 undivided interest therein.

32 ~~**F. Preferential Right to Purchase:**~~

33  (Optional; Check if applicable.)

34 ~~Should any party desire to sell all or any part of its interests under this agreement, or its rights and interests in the Contract  
35 Area, it shall promptly give written notice to the other parties, with full information concerning its proposed disposition, which  
36 shall include the name and address of the prospective transferee (who must be ready, willing and able to purchase), the purchase  
37 price, a legal description sufficient to identify the property, and all other terms of the offer. The other parties shall then have an  
38 optional prior right, for a period of ten (10) days after the notice is delivered, to purchase for the stated consideration on the  
39 same terms and conditions the interest which the other party proposes to sell; and, if this optional right is exercised, the  
40 purchasing parties shall share the purchased interest in the proportions that the interest of each bears to the total interest of all  
41 purchasing parties. However, there shall be no preferential right to purchase in those cases where any party wishes to mortgage  
42 its interests, or to transfer title to its interests to its mortgagee in lieu of or pursuant to foreclosure of a mortgage of its interests,  
43 or to dispose of its interests by merger, reorganization, consolidation, or by sale of all or substantially all of its Oil and Gas assets  
44 to any party, or by transfer of its interests to a subsidiary or parent company or to a subsidiary of a parent company, or to any  
45 company in which such party owns a majority of the stock.~~

46 **ARTICLE IX.**  
47 **INTERNAL REVENUE CODE ELECTION**

48 If, for federal income tax purposes, this agreement and the operations hereunder are regarded as a partnership, and if the  
49 parties have not otherwise agreed to form a tax partnership pursuant to Exhibit "G" or other agreement between them, each  
50 party thereby affected elects to be excluded from the application of all of the provisions of Subchapter "K," Chapter 1, Subtitle  
51 "A," of the Internal Revenue Code of 1986, as amended ("Code"), as permitted and authorized by Section 761 of the Code and  
52 the regulations promulgated thereunder. Operator is authorized and directed to execute on behalf of each party hereby affected  
53 such evidence of this election as may be required by the Secretary of the Treasury of the United States or the Federal Internal  
54 Revenue Service, including specifically, but not by way of limitation, all of the returns, statements, and the data required by  
55 Treasury Regulations §1.761. Should there be any requirement that each party hereby affected give further evidence of this  
56 election, each such party shall execute such documents and furnish such other evidence as may be required by the Federal Internal  
57 Revenue Service or as may be necessary to evidence this election. No such party shall give any notices or take any other action  
58 inconsistent with the election made hereby. If any present or future income tax laws of the state or states in which the Contract  
59 Area is located or any future income tax laws of the United States contain provisions similar to those in Subchapter "K," Chapter  
60 1, Subtitle "A," of the Code, under which an election similar to that provided by Section 761 of the Code is permitted, each party  
61 hereby affected shall make such election as may be permitted or required by such laws. In making the foregoing election, each  
62 such party states that the income derived by such party from operations hereunder can be adequately determined without the  
63 computation of partnership taxable income.

64 **ARTICLE X.**  
65 **CLAIMS AND LAWSUITS**

66 Operator may settle any single uninsured third party damage claim or suit arising from operations hereunder if the expenditure  
67 does not exceed Twenty-five Thousand Dollars (\$ 25,000 ) and if the payment is in complete settlement  
68 of such claim or suit. If the amount required for settlement exceeds the above amount, the parties hereto shall assume and take over  
69 the further handling of the claim or suit, unless such authority is delegated to Operator. All costs and expenses of handling, settling,  
70 or otherwise discharging such claim or suit shall be at the joint expense of the parties participating in the operation from which the  
71 claim or suit arises. If a claim is made against any party or if any party is sued on account of any matter arising from operations  
72 hereunder over which such individual has no control because of the rights given Operator by this agreement, such party shall  
73 immediately notify all other parties, and the claim or suite shall be treated as any other claim or suit involving operations hereunder.

ARTICLE XI.  
FORCE MAJEURE

If any party is rendered unable, wholly or in part, by force majeure to carry out its obligations under this agreement, other than the obligation to indemnify or make money payments or furnish security, that party shall give to all other parties prompt written notice of the force majeure with reasonably full particulars concerning it; thereupon, the obligations of the party giving the notice, so far as they are affected by the force majeure, shall be suspended during, but no longer than, the continuance of the force majeure. The term "force majeure," as here employed, shall mean an act of God, strike, lockout, or other industrial disturbance, act of the public enemy, war, blockade, public riot, lightning, fire, storm, flood or other act of nature, explosion, governmental action, governmental delay, restraint or inaction, unavailability of equipment, and any other cause, whether of the kind specifically enumerated above or otherwise, which is not reasonably within the control of the party claiming suspension.

The affected party shall use all reasonable diligence to remove the force majeure situation as quickly as practicable. The requirement that any force majeure shall be remedied with all reasonable dispatch shall not require the settlement of strikes, lockouts, or other labor difficulty by the party involved, contrary to its wishes; how all such difficulties shall be handled shall be entirely within the discretion of the party concerned.

ARTICLE XII.  
NOTICES

All notices authorized or required between the parties by any of the provisions of this agreement, unless otherwise specifically provided, shall be in writing and delivered in person or by United States mail, courier service, telegram, telex, telecopier or any other form of facsimile, postage or charges prepaid, and addressed to such parties at the addresses listed on Exhibit "A." All telephone or oral notices permitted by this agreement shall be confirmed immediately thereafter by written notice. The originating notice given under any provision hereof shall be deemed delivered only when received by the party to whom such notice is directed, and the time for such party to deliver any notice in response thereto shall run from the date the originating notice is received. "Receipt" for purposes of this agreement with respect to written notice delivered hereunder shall be actual delivery of the notice to the address of the party to be notified specified in accordance with this agreement, or to the telecopy, facsimile or telex machine of such party. The second or any responsive notice shall be deemed delivered when deposited in the United States mail or at the office of the courier or telegraph service, or upon transmittal by telex, telecopy or facsimile, or when personally delivered to the party to be notified, provided, that when response is required within 24 or 48 hours, such response shall be given orally or by telephone, telex, telecopy or other facsimile within such period. Each party shall have the right to change its address at any time, and from time to time, by giving written notice thereof to all other parties. If a party is not available to receive notice orally or by telephone when a party attempts to deliver a notice required to be delivered within 24 or 48 hours, the notice may be delivered in writing by any other method specified herein and shall be deemed delivered in the same manner provided above for any responsive notice.

ARTICLE XIII.  
TERM OF AGREEMENT

This agreement shall remain in full force and effect as to the Oil and Gas Leases and/or Oil and Gas Interests subject hereto for the period of time selected below; provided, however, no party hereto shall ever be construed as having any right, title or interest in or to any Lease or Oil and Gas Interest contributed by any other party beyond the term of this agreement.

Option No. 1: So long as any of the Oil and Gas Leases subject to this agreement remain or are continued in force as to any part of the Contract Area, whether by production, extension, renewal or otherwise.

~~Option No. 2: In the event the well described in Article VI.A., or any subsequent well drilled under any provision of this agreement, results in the Completion of a well as a well capable of production of Oil and/or Gas in paying quantities, this agreement shall continue in force so long as any such well is capable of production, and for an additional period of \_\_\_\_\_ days thereafter; provided, however, if, prior to the expiration of such additional period, one or more of the parties hereto are engaged in drilling, Reworking, Deepening, Sidetracking, Plugging Back, testing or attempting to Complete or Re-complete a well or wells hereunder, this agreement shall continue in force until such operations have been completed and if production results therefrom, this agreement shall continue in force as provided herein. In the event the well described in Article VI.A., or any subsequent well drilled hereunder, results in a dry hole, and no other well is capable of producing Oil and/or Gas from the Contract Area, this agreement shall terminate unless drilling, Deepening, Sidetracking, Completing, Re-completing, Plugging Back or Reworking operations are commenced within \_\_\_\_\_ days from the date of abandonment of said well. "Abandonment" for such purposes shall mean either (i) a decision by all parties not to conduct any further operations on the well or (ii) the elapse of 180 days from the conduct of any operations on the well, whichever first occurs.~~

The termination of this agreement shall not relieve any party hereto from any expense, liability or other obligation or any remedy therefor which has accrued or attached prior to the date of such termination.

Upon termination of this agreement and the satisfaction of all obligations hereunder, in the event a memorandum of this Operating Agreement has been filed of record, Operator is authorized to file of record in all necessary recording offices a notice of termination, and each party hereto agrees to execute such a notice of termination as to Operator's interest, upon request of Operator, if Operator has satisfied all its financial obligations.

ARTICLE XIV.  
COMPLIANCE WITH LAWS AND REGULATIONS

A. Laws, Regulations and Orders:

This agreement shall be subject to the applicable laws of the state in which the Contract Area is located, to the valid rules, regulations, and orders of any duly constituted regulatory body of said state; and to all other applicable federal, state, and local laws, ordinances, rules, regulations and orders.

B. Governing Law:

This agreement and all matters pertaining hereto, including but not limited to matters of performance, non-performance, breach, remedies, procedures, rights, duties, and interpretation or construction, shall be governed and determined by the law of the state in which the Contract Area is located. If the Contract Area is in two or more states, the law of the state of New Mexico shall govern.

C. Regulatory Agencies:

Nothing herein contained shall grant, or be construed to grant, Operator the right or authority to waive or release any rights, privileges, or obligations which Non-Operators may have under federal or state laws or under rules, regulations or

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

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

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

13 **A. Execution:**

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

29 **B. Successors and Assigns:**

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

33 **C. Counterparts:**

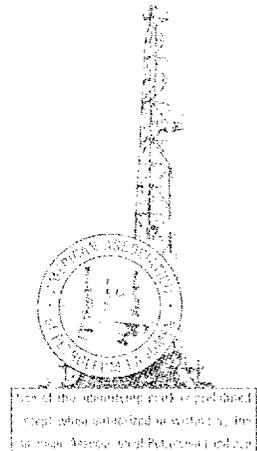
34 This instrument may be executed in any number of counterparts, each of which shall be considered an original for all  
35 purposes.

36 **D. Severability:**

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

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

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A.A.P.L. FORM 610 - MODEL FORM OPERATING AGREEMENT - 1989

1 IN WITNESS WHEREOF, this agreement shall be effective as of the 1st day of February,  
2 19 97.

3 ATTEST OR WITNESS:

OPERATOR

4  
5 *Michael K. Merrion*  
6 Michael K. Merrion, Secretary  
7

MERRION OIL & GAS CORPORATION  
By *T. Greg Merrion*  
T. Greg Merrion  
Type or print name

8 Title President

9 Date 4/28/97

10 Tax ID or S.S. No. 85-0232430

12 NON-OPERATORS

14 BURLINGTON RESOURCES, INC.

15 \_\_\_\_\_ By \_\_\_\_\_  
16 \_\_\_\_\_  
17 Type or print name

18 Title \_\_\_\_\_

19 Date \_\_\_\_\_

20 Tax ID or S.S. No. \_\_\_\_\_

22 ESTATE OF HAROLD FIELDS

23 \_\_\_\_\_ By \_\_\_\_\_  
24 \_\_\_\_\_  
25 Type or print name

26 Title \_\_\_\_\_

27 Date \_\_\_\_\_

28 Tax ID or S.S. No. \_\_\_\_\_

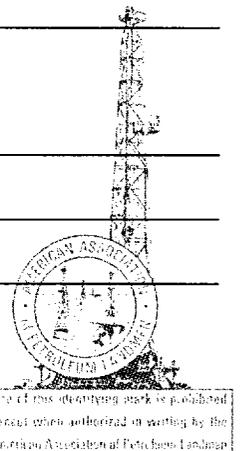
29 EAON WAYMEN-PALMER

30 \_\_\_\_\_ By \_\_\_\_\_  
31 \_\_\_\_\_  
32 Type or print name

33 Title \_\_\_\_\_

34 Date \_\_\_\_\_

35 Tax ID or S.S. No. \_\_\_\_\_



ACKNOWLEDGMENTS

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Note: The following forms of acknowledgment are the short forms approved by the Uniform Law on Notarial Acts. The validity and effect of these forms in any state will depend upon the statutes of that state.

Individual acknowledgment:

State of NEW MEXICO )

) ss.

County of SAN JUAN )

This instrument was acknowledged before me on

\_\_\_\_\_ by Eaon Waymen-Palmer

(Seal, if any) \_\_\_\_\_

Title (and Rank) \_\_\_\_\_

My commission expires: \_\_\_\_\_

Acknowledgment in representative capacity:

State of NEW MEXICO )

) ss.

County of SAN JUAN )

This instrument was acknowledged before me on

April 28, 97

\_\_\_\_\_ by T. Greg Merrion as

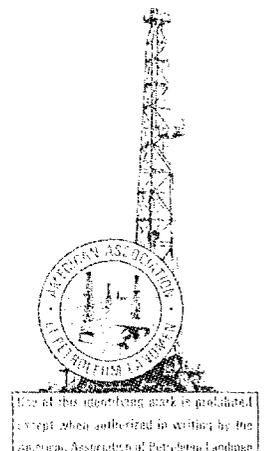
President of Merrion Oil & Gas Corporation

(Seal, if any) \_\_\_\_\_

*Cynthia Williams*

Title (and Rank) Notary Public

My commission expires: June 27, 1998



ACKNOWLEDGMENTS

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Note: The following forms of acknowledgment are the short forms approved by the Uniform Law on Notarial Acts. The validity and effect of these forms in any state will depend upon the statutes of that state.

Individual acknowledgment:

State of \_\_\_\_\_ )

\_\_\_\_\_ ) ss.

County of \_\_\_\_\_ )

This instrument was acknowledged before me on

\_\_\_\_\_ by \_\_\_\_\_

(Seal, if any)

\_\_\_\_\_ Title (and Rank)

My commission expires: \_\_\_\_\_

Acknowledgment in representative capacity:

State of NEW MEXICO )

\_\_\_\_\_ ) ss.

County of SAN JUAN )

This instrument was acknowledged before me on

\_\_\_\_\_ by \_\_\_\_\_ as

\_\_\_\_\_ of Burlington Resources, Inc.

(Seal, if any)

\_\_\_\_\_ Title (and Rank)

My commission expires: \_\_\_\_\_



**EXHIBIT "A"**

Attached to and made a part of that certain Operating Agreement  
by and between Merrion Oil & Gas Corporation, as Operator, and Non-Operators

**LANDS AND LEASE SUBJECT TO THIS AGREEMENT**

1. Lessor: Estate of Edward Truett Helms, Jr.  
and Holly A. Helms  
Lessee: Merrion Oil & Gas Corporation  
Date: February 23, 1996  
Recording Data: Book 1216, Page 725
2. Lessor: Estate of Edward Truett Helms, Jr.  
and Jennifer M. Helms  
Lessee: Merrion Oil & Gas Corporation  
Date: February 23, 1997  
Recording Data: Book 1216, Page 726
3. Lessor: Estate of Arthur Lyon, deceased  
Lessee: Merrion Oil & Gas Corporation  
Date: August 12, 1996  
Recording Data: Book 1228, Page 190
4. Lessor: George D. Fehr  
Lessee: Merrion Oil & Gas Corporation  
Date: June 1, 1996  
Recording Data: Book 1226, Page 277
5. Lessor: Harry B. Heutel  
Lessee: Merrion Oil & Gas Corporation  
Date: April 1, 1996  
Recording Data: Book 1220, Page 189
6. Lessor: Ronald D. Catterson  
Lessee: Merrion Oil & Gas Corporation  
Date: February 23, 1996  
Recording Data: Book 1217, Page 646
7. Lessor: David P. Catterson  
Lessee: Merrion Oil & Gas Corporation  
Date: February 23, 1996  
Recording Data: Book 1217, Page 648
8. Lessor: Shelly A. Catterson  
Lessee: Merrion Oil & Gas Corporation  
Date: February 23, 1996  
Recording Data: Book 1217, Page 647
9. Lessor: James M. Shaffer and Marion Rocelle Shaffer  
Lessee: Merrion Oil & Gas Corporation  
Date: February 23, 1996  
Recording Data: Book 1217, Page 645
10. Lessor: Darla Y. Dickerson  
Lessee: Merrion Oil & Gas Corporation  
Date: February 23, 1996  
Recording Data: Book 1219, Page 42

11. Lessor: Marilyn J. Bader and Ernest A. Bader, H&W  
Lessee: Merrion Oil & Gas Corporation  
Date: February 23, 1996  
Recording Data: Book 1217, Page 642
12. Lessor: Meredyth J. Verhoeff and Elton E. Verhoeff, H&W  
Lessee: Merrion Oil & Gas Corporation  
Date: February 23, 1996  
Recording Data: Book 1217, Page 644
13. Lessor: Phyllis C. Jones and William T. Jones, H&W  
Lessee: Merrion Oil & Gas Corporation  
Date: February 23, 1996  
Recording Data: Book 1215, Page 749
14. Lessor: Clarence C. Carroll and Donna Carroll, H&W  
Lessee: Merrion Oil & Gas Corporation  
Date: March 25, 1996  
Recording Data: Book 1217, Page 643
15. Lessor: Terry Dean Lester and Dennise M. Walker  
Lessee: Merrion Oil & Gas Corporation  
Date: March 25, 1996  
Recording Data: Book 1219, Page 815
16. Lessor: Georgia M. Moore and Robert Moore, H&W  
Lessee: Merrion Oil & Gas Corporation  
Date: April 1, 1996  
Recording Data: Book 1219, Page 43
17. Lessor: John Larry McLaws and Sonja L. McLaws, H&W  
Lessee: Merrion Oil & Gas Corporation  
Date: February 23, 1996  
Recording Data: Book 1220, Page 639
18. Lessor: Monte B. and Emily C. McLaws Revocable Trust  
Lessee: Merrion Oil & Gas Corporation  
Date: February 23, 1996  
Recording Data: Book 1216, Page 727
19. Lessor: Lyndella Bryant and Ian L. Bryant, H&W  
Lessee: Merrion Oil & Gas Corporation  
Date: February 23, 1996  
Recording Data: Book 1216, Page 724
20. Lessor: Don Hyrum Rothlisberger  
Lessee: Merrion Oil & Gas Corporation  
Date: May 16, 1996  
Recording Data: Book 1221, Page 597
21. Lessor: Kathleen Hicks  
Lessee: Merrion Oil & Gas Corporation  
Date: May 16, 1996  
Recording Data: Book 1223, Page 962
22. Lessor: Fred N. Rothlisberger  
Lessee: Merrion Oil & Gas Corporation  
Date: May 16, 1996  
Recording Data: Book 1220, Page 638

- 23. Lessor: John Alcid Rothlisberger  
 Lessee: Merrion Oil & Gas Corporation  
 Date: May 16, 1996  
 Recording Data: Book 1221, Page 366
- 24. Lessor: Alethea Rothlisberger  
 Lessee: Merrion Oil & Gas Corporation  
 Date: May 16, 1996  
 Recording Data: Book 1221, Page 364
- 25. Lessor: Celeste Williams  
 Lessee: Merrion Oil & Gas Corporation  
 Date: May 16, 1996  
 Recording Data: Book 1221, Page 367
- 26. Lessor: Ernest C. Rothlisberger  
 Lessee: Merrion Oil & Gas Corporation  
 Date: May 16, 1996  
 Recording Data: Book 1221, Page 365
- 27. Lessor: Marinus Lynn Rothlisberger  
 Lessee: Merrion Oil & Gas Corporation  
 Date: May 16, 1996  
 Recording Data: Book 1221, Page 234
- 28. Lessor: Elva T. Mackay  
 Lessee: Merrion Oil & Gas Corporation  
 Date: January 2, 1996  
 Recording Data: Book 1220, Page 108
- 29. Lessor: San Juan Coal Company  
 Lessee: Merrion Oil & Gas Corporation  
 Date: June 1, 1996  
 Recording Data: Book 1221, Page 596
- 30. Lessor: Elizabeth C. Thomas  
 Lessee: Merrion Oil & Gas Corporation  
 Date: October 15, 1996  
 Recording Data: Book 1228, Page 920

OWNERSHIP:

Merrion Oil & Gas Corporation 100%

- 30. Lessor: United States of America (SF-078818)  
 Lessee:  
 Date: November 1, 1951  
 Recording Data:

OWNERSHIP:

Burlington Resources, Inc. 100%

UNLEASED

- 31. Lessor: Estate of Harold Fields  
 Lessee: Estate of Harold Fields  
 Date: N/A  
 Recording Data: N/A

OWNERSHIP:

Estate of Harold Fields 100%

32. Lessor: Eاون Waymen-Palmer  
Lessee: Eاون Waymen-Palmer  
Date: N/A  
Recording Data: N/A

OWNERSHIP:  
Eاون Waymen-Palmer 100%

ADDRESSES OF PARTIES SUBJECT TO THIS AGREEMENT

Operator:

Merrion Oil & Gas Corporation  
610 Reilly Avenue  
Farmington, NM 87401

Non-Operators:

Burlington Resources, Inc.  
P.O. Box 4289  
Farmington, NM 87401

Estate of Harold Fields  
Medreth D. Fields, Personal Rep.  
c/o Lakeside Manor  
7020 S. 12th, #2901  
Tacoma, WA 98465

Eاون Waymen-Palmer  
P.O. Box 239  
La Plata, NM 87418

**EXHIBIT "B"**

Not applicable.

EXHIBIT " C "

Attached to and made a part of that certain Operating Agreement dated 2/1/97 between Merrion Oil & Gas Corporation, as Operator and Non-Operators.

ACCOUNTING PROCEDURE  
JOINT OPERATIONS

I. GENERAL PROVISIONS

1. Definitions

"Joint Property" shall mean the real and personal property subject to the agreement to which this Accounting Procedure is attached.

"Joint Operations" shall mean all operations necessary or proper for the development, operation, protection and maintenance of the Joint Property.

"Joint Account" shall mean the account showing the charges paid and credits received in the conduct of the Joint Operations and which are to be shared by the Parties.

"Operator" shall mean the party designated to conduct the Joint Operations.

"Non-Operators" shall mean the Parties to this agreement other than the Operator.

"Parties" shall mean Operator and Non-Operators.

"First Level Supervisors" shall mean those employees whose primary function in Joint Operations is the direct supervision of other employees and/or contract labor directly employed on the Joint Property in a field operating capacity.

"Technical Employees" shall mean those employees having special and specific engineering, geological or other professional skills, and whose primary function in Joint Operations is the handling of specific operating conditions and problems for the benefit of the Joint Property.

"Personal Expenses" shall mean travel and other reasonable reimbursable expenses of Operator's employees.

"Material" shall mean personal property, equipment or supplies acquired or held for use on the Joint Property.

"Controllable Material" shall mean Material which at the time is so classified in the Material Classification Manual as most recently recommended by the Council of Petroleum Accountants Societies.

2. Statement and Billings

Operator shall bill Non-Operators on or before the last day of each month for their proportionate share of the Joint Account for the preceding month. Such bills will be accompanied by statements which identify the authority for expenditure, lease or facility, and all charges and credits summarized by appropriate classifications of investment and expense except that items of Controllable Material and unusual charges and credits shall be separately identified and fully described in detail.

3. Advances and Payments by Non-Operators

A. Unless otherwise provided for in the agreement, the Operator may require the Non-Operators to advance their share of estimated cash outlay for the succeeding month's operation within fifteen (15) days after receipt of the billing or by the first day of the month for which the advance is required, whichever is later. Operator shall adjust each monthly billing to reflect advances received from the Non-Operators.

B. Each Non-Operator shall pay its proportion of all bills within fifteen (15) days after receipt. If payment is not made within such time, the unpaid balance shall bear interest monthly at the prime rate in effect at The Chase Manhattan Bank on the first day of the month in which delinquency occurs plus 1% or the maximum contract rate permitted by the applicable usury laws in the state in which the Joint Property is located, whichever is the lesser, plus attorney's fees, court costs, and other costs in connection with the collection of unpaid amounts.

4. Adjustments

Payment of any such bills shall not prejudice the right of any Non-Operator to protest or question the correctness thereof; provided, however, all bills and statements rendered to Non-Operators by Operator during any calendar year shall conclusively be presumed to be true and correct after twenty-four (24) months following the end of any such calendar year, unless within the said twenty-four (24) month period a Non-Operator takes written exception thereto and makes claim on Operator for adjustment. No adjustment favorable to Operator shall be made unless it is made within the same prescribed period. The provisions of this paragraph shall not prevent adjustments resulting from a physical inventory of Controllable Material as provided for in Section V.

1 5. Audits

2  
3 A. A Non-Operator, upon notice in writing to Operator and all other Non-Operators, shall have the right to audit  
4 Operator's accounts and records relating to the Joint Account for any calendar year within the twenty-four  
5 (24) month period following the end of such calendar year; provided, however, the making of an audit shall not  
6 extend the time for the taking of written exception to and the adjustments of accounts as provided for in  
7 Paragraph 4 of this Section I. Where there are two or more Non-Operators, the Non-Operators shall make  
8 every reasonable effort to conduct a joint audit in a manner which will result in a minimum of inconvenience  
9 to the Operator. Operator shall bear no portion of the Non-Operators' audit cost incurred under this  
10 paragraph unless agreed to by the Operator. The audits shall not be conducted more than once each year  
11 without prior approval of Operator, except upon the resignation or removal of the Operator, and shall be made  
12 at the expense of those Non-Operators approving such audit.

13  
14 B. The Operator shall reply in writing to an audit report within 180 days after receipt of such report.

15  
16 6. Approval By Non-Operators

17  
18 Where an approval or other agreement of the Parties or Non-Operators is expressly required under other sections of  
19 this Accounting Procedure and if the agreement to which this Accounting Procedure is attached contains no  
20 contrary provisions in regard thereto, Operator shall notify all Non-Operators of the Operator's proposal, and the  
21 agreement or approval of a majority in interest of the Non-Operators shall be controlling on all Non-Operators.

22  
23  
24 II. DIRECT CHARGES

25  
26 Operator shall charge the Joint Account with the following items:

27  
28 1. Ecological and Environmental

29  
30 Costs incurred for the benefit of the Joint Property as a result of governmental or regulatory requirements to satisfy  
31 environmental considerations applicable to the Joint Operations. Such costs may include surveys of an ecological or  
32 archaeological nature and pollution control procedures as required by applicable laws and regulations.

33  
34 2. Rentals and Royalties

35  
36 Lease rentals and royalties paid by Operator for the Joint Operations.

37  
38 3. Labor

39  
40 A. (1) Salaries and wages of Operator's field employees directly employed on the Joint Property in the conduct of  
41 Joint Operations.

42  
43 (2) Salaries of First Level Supervisors in the field.

44  
45 (3) Salaries and wages of Technical Employees directly employed on the Joint Property if such charges are  
46 excluded from the overhead rates.

47  
48 (4) Salaries and wages of Technical Employees either temporarily or permanently assigned to and directly  
49 employed in the operation of the Joint Property if such charges are excluded from the overhead rates.

50  
51 B. Operator's cost of holiday, vacation, sickness and disability benefits and other customary allowances paid to  
52 employees whose salaries and wages are chargeable to the Joint Account under Paragraph 3A of this Section II.  
53 Such costs under this Paragraph 3B may be charged on a "when and as paid basis" or by "percentage assessment"  
54 on the amount of salaries and wages chargeable to the Joint Account under Paragraph 3A of this Section II. If  
55 percentage assessment is used, the rate shall be based on the Operator's cost experience.

56  
57 C. Expenditures or contributions made pursuant to assessments imposed by governmental authority which are  
58 applicable to Operator's costs chargeable to the Joint Account under Paragraphs 3A and 3B of this Section II.

59  
60 D. Personal Expenses of those employees whose salaries and wages are chargeable to the Joint Account under  
61 Paragraph 3A of this Section II.

62  
63 4. Employee Benefits

64  
65 Operator's current costs of established plans for employees' group life insurance, hospitalization, pension, retirement,  
66 stock purchase, thrift, bonus, and other benefit plans of a like nature, applicable to Operator's labor cost chargeable to the  
67 Joint Account under Paragraphs 3A and 3B of this Section II shall be Operator's actual cost not to exceed the percent  
68 most recently recommended by the Council of Petroleum Accountants Societies.

1 **5. Material**

2  
3 Material purchased or furnished by Operator for use on the Joint Property as provided under Section IV. Only such  
4 Material shall be purchased for or transferred to the Joint Property as may be required for immediate use and is  
5 reasonably practical and consistent with efficient and economical operations. The accumulation of surplus stocks shall be  
6 avoided.

7  
8 **6. Transportation**

9  
10 Transportation of employees and Material necessary for the Joint Operations but subject to the following limitations:

- 11  
12 A. If Material is moved to the Joint Property from the Operator's warehouse or other properties, no charge shall be  
13 made to the Joint Account for a distance greater than the distance from the nearest reliable supply store where like  
14 material is normally available or railway receiving point nearest the Joint Property unless agreed to by the Parties.  
15  
16 B. If surplus Material is moved to Operator's warehouse or other storage point, no charge shall be made to the Joint  
17 Account for a distance greater than the distance to the nearest reliable supply store where like material is normally  
18 available, or railway receiving point nearest the Joint Property unless agreed to by the Parties. No charge shall be  
19 made to the Joint Account for moving Material to other properties belonging to Operator, unless agreed to by the  
20 Parties.  
21  
22 C. In the application of subparagraphs A and B above, the option to equalize or charge actual trucking cost is  
23 available when the actual charge is \$400 or less excluding accessorial charges. The \$400 will be adjusted to the  
24 amount most recently recommended by the Council of Petroleum Accountants Societies.  
25

26 **7. Services**

27  
28 The cost of contract services, equipment and utilities provided by outside sources, except services excluded by Paragraph  
29 10 of Section II and Paragraph i, ii, and iii, of Section III. The cost of professional consultant services and contract  
30 services of technical personnel directly engaged on the Joint Property if such charges are excluded from the overhead  
31 rates. The cost of professional consultant services or contract services of technical personnel not directly engaged on the  
32 Joint Property shall not be charged to the Joint Account unless previously agreed to by the Parties.  
33

34 **8. Equipment and Facilities Furnished By Operator**

- 35  
36 A. Operator shall charge the Joint Account for use of Operator owned equipment and facilities at rates commensurate  
37 with costs of ownership and operation. Such rates shall include costs of maintenance, repairs, other operating  
38 expense, insurance, taxes, depreciation, and interest on gross investment less accumulated depreciation not to  
39 exceed twelve percent ( 12 %) per annum. Such rates shall not exceed average commercial  
40 rates currently prevailing in the immediate area of the Joint Property.  
41  
42 B. In lieu of charges in paragraph 8A above, Operator may elect to use average commercial rates prevailing in the  
43 immediate area of the Joint Property less 20%. For automotive equipment, Operator may elect to use rates  
44 published by the Petroleum Motor Transport Association.  
45

46 **9. Damages and Losses to Joint Property**

47  
48 All costs or expenses necessary for the repair or replacement of Joint Property made necessary because of damages or  
49 losses incurred by fire, flood, storm, theft, accident, or other cause, except those resulting from Operator's gross  
50 negligence or willful misconduct. Operator shall furnish Non-Operator written notice of damages or losses incurred as  
51 soon as practicable after a report thereof has been received by Operator.  
52

53 **10. Legal Expense**

54  
55 Expense of handling, investigating and settling litigation or claims, discharging of liens, payment of judgements and  
56 amounts paid for settlement of claims incurred in or resulting from operations under the agreement or necessary to  
57 protect or recover the Joint Property, except that no charge for services of Operator's legal staff or fees or expense of  
58 outside attorneys shall be made unless previously agreed to by the Parties. All other legal expense is considered to be  
59 covered by the overhead provisions of Section III unless otherwise agreed to by the Parties, except as provided in Section  
60 I, Paragraph 3.  
61

62 **11. Taxes**

63  
64 All taxes of every kind and nature assessed or levied upon or in connection with the Joint Property, the operation thereof,  
65 or the production therefrom, and which taxes have been paid by the Operator for the benefit of the Parties. If the ad  
66 valorem taxes are based in whole or in part upon separate valuations of each party's working interest, then  
67 notwithstanding anything to the contrary herein, charges to the Joint Account shall be made and paid by the Parties  
68 hereto in accordance with the tax value generated by each party's working interest.  
69  
70

1 **12. Insurance**

2  
3 Net premiums paid for insurance required to be carried for the Joint Operations for the protection of the Parties. In the  
4 event Joint Operations are conducted in a state in which Operator may act as self-insurer for Worker's Compensation  
5 and/or Employers Liability under the respective state's laws, Operator may, at its election, include the risk under its self-  
6 insurance program and in that event, Operator shall include a charge at Operator's cost not to exceed manual rates.  
7

8 **13. Abandonment and Reclamation**

9  
10 Costs incurred for abandonment of the Joint Property, including costs required by governmental or other regulatory  
11 authority.  
12

13 **14. Communications**

14  
15 Cost of acquiring, leasing, installing, operating, repairing and maintaining communication systems, including radio and  
16 microwave facilities directly serving the Joint Property. In the event communication facilities/systems serving the Joint  
17 Property are Operator owned, charges to the Joint Account shall be made as provided in Paragraph 8 of this Section II.  
18

19 **15. Other Expenditures**

20  
21 Any other expenditure not covered or dealt with in the foregoing provisions of this Section II, or in Section III and which  
22 is of direct benefit to the Joint Property and is incurred by the Operator in the necessary and proper conduct of the Joint  
23 Operations.  
24

25  
26 **III. OVERHEAD**

27  
28 **1. Overhead - Drilling and Producing Operations**

29  
30 i. As compensation for administrative, supervision, office services and warehousing costs, Operator shall charge  
31 drilling and producing operations on either:

- 32  
33 (XX) Fixed Rate Basis, Paragraph 1A, or  
34 ( ) Percentage Basis, Paragraph 1B  
35

36 Unless otherwise agreed to by the Parties, such charge shall be in lieu of costs and expenses of all offices and  
37 salaries or wages plus applicable burdens and expenses of all personnel, except those directly chargeable under  
38 Paragraph 3A, Section II. The cost and expense of services from outside sources in connection with matters of  
39 taxation, traffic, accounting or matters before or involving governmental agencies shall be considered as included in  
40 the overhead rates provided for in the above selected Paragraph of this Section III unless such cost and expense are  
41 agreed to by the Parties as a direct charge to the Joint Account.  
42

43 ii. The salaries, wages and Personal Expenses of Technical Employees and/or the cost of professional consultant  
44 services and contract services of technical personnel directly employed on the Joint Property:

- 45  
46 (XX) shall be covered by the overhead rates, or  
47 ( ) shall not be covered by the overhead rates.  
48

49 iii. The salaries, wages and Personal Expenses of Technical Employees and/or costs of professional consultant services  
50 and contract services of technical personnel either temporarily or permanently assigned to and directly employed in  
51 the operation of the Joint Property:

- 52  
53 ( ) shall be covered by the overhead rates, or  
54 (XX) shall not be covered by the overhead rates.  
55

56 **A. Overhead - Fixed Rate Basis**

57  
58 (1) Operator shall charge the Joint Account at the following rates per well per month:

59  
60 Drilling Well Rate \$ 3500  
61 (Prorated for less than a full month)

62  
63 Producing Well Rate \$ 350  
64

65 (2) Application of Overhead - Fixed Rate Basis shall be as follows:

66  
67 (a) Drilling Well Rate

68  
69 (1) Charges for drilling wells shall begin on the date the well is spudded and terminate on the date  
70 the drilling rig, completion rig, or other units used in completion of the well is released, whichever

1 is later, except that no charge shall be made during suspension of drilling or completion operations  
2 for fifteen (15) or more consecutive calendar days.

- 3  
4 (2) Charges for wells undergoing any type of workover or recompletion for a period of five (5)  
5 consecutive work days or more shall be made at the drilling well rate. Such charges shall be  
6 applied for the period from date workover operations, with rig or other units used in workover,  
7 commence through date of rig or other unit release, except that no charge shall be made during  
8 suspension of operations for fifteen (15) or more consecutive calendar days.

9  
10 (b) Producing Well Rates

- 11  
12 (1) An active well either produced or injected into for any portion of the month shall be considered as  
13 a one-well charge for the entire month.  
14  
15 (2) Each active completion in a multi-completed well in which production is not commingled down  
16 hole shall be considered as a one-well charge providing each completion is considered a separate  
17 well by the governing regulatory authority.  
18  
19 (3) An inactive gas well shut in because of overproduction or failure of purchaser to take the  
20 production shall be considered as a one-well charge providing the gas well is directly connected to  
21 a permanent sales outlet.  
22  
23 (4) A one-well charge shall be made for the month in which plugging and abandonment operations  
24 are completed on any well. This one-well charge shall be made whether or not the well has  
25 produced except when drilling well rate applies.  
26  
27 (5) All other inactive wells (including but not limited to inactive wells covered by unit allowable, lease  
28 allowable, transferred allowable, etc.) shall not qualify for an overhead charge.  
29  
30 (3) The well rates shall be adjusted as of the first day of April each year following the effective date of the  
31 agreement to which this Accounting Procedure is attached. The adjustment shall be computed by multiplying  
32 the rate currently in use by the percentage increase or decrease in the average weekly earnings of Crude  
33 Petroleum and Gas Production Workers for the last calendar year compared to the calendar year preceding as  
34 shown by the index of average weekly earnings of Crude Petroleum and Gas Production Workers as published  
35 by the United States Department of Labor, Bureau of Labor Statistics, or the equivalent Canadian index as  
36 published by Statistics Canada, as applicable. The adjusted rates shall be the rates currently in use, plus or  
37 minus the computed adjustment.  
38

39 B. Overhead - Percentage Basis

- 40  
41 (1) Operator shall charge the Joint Account at the following rates:  
42  
43 (a) Development  
44  
45 \_\_\_\_\_ Percent ( \_\_\_\_\_ %) of the cost of development of the Joint Property exclusive of costs  
46 provided under Paragraph 10 of Section II and all salvage credits.  
47  
48 (b) Operating  
49  
50 \_\_\_\_\_ Percent ( \_\_\_\_\_ %) of the cost of operating the Joint Property exclusive of costs provided  
51 under Paragraphs 2 and 10 of Section II, all salvage credits, the value of injected substances purchased  
52 for secondary recovery and all taxes and assessments which are levied, assessed and paid upon the  
53 mineral interest in and to the Joint Property.  
54  
55 (2) Application of Overhead - Percentage Basis shall be as follows:

56  
57 For the purpose of determining charges on a percentage basis under Paragraph 1B of this Section III,  
58 development shall include all costs in connection with drilling, redrilling, deepening, or any remedial  
59 operations on any or all wells involving the use of drilling rig and crew capable of drilling to the producing  
60 interval on the Joint Property; also, preliminary expenditures necessary in preparation for drilling and  
61 expenditures incurred in abandoning when the well is not completed as a producer, and original cost of  
62 construction or installation of fixed assets, the expansion of fixed assets and any other project clearly  
63 discernible as a fixed asset, except Major Construction as defined in Paragraph 2 of this Section III. All other  
64 costs shall be considered as operating.  
65

66 2. Overhead - Major Construction

67  
68 To compensate Operator for overhead costs incurred in the construction and installation of fixed assets, the expansion of  
69 fixed assets, and any other project clearly discernible as a fixed asset required for the development and operation of the  
70 Joint Property, Operator shall either negotiate a rate prior to the beginning of construction, or shall charge the Joint

Account for overhead based on the following rates for any Major Construction project in excess of \$ 25,000 :

- A. 3 % of first \$100,000 or total cost if less, plus  
 B. 2 % of costs in excess of \$100,000 but less than \$1,000,000, plus  
 C. 1 % of costs in excess of \$1,000,000.

Total cost shall mean the gross cost of any one project. For the purpose of this paragraph, the component parts of a single project shall not be treated separately and the cost of drilling and workover wells and artificial lift equipment shall be excluded.

### 3. Catastrophe Overhead

To compensate Operator for overhead costs incurred in the event of expenditures resulting from a single occurrence due to oil spill, blowout, explosion, fire, storm, hurricane, or other catastrophes as agreed to by the Parties, which are necessary to restore the Joint Property to the equivalent condition that existed prior to the event causing the expenditures, Operator shall either negotiate a rate prior to charging the Joint Account or shall charge the Joint Account for overhead based on the following rates:

- A. 3 % of total costs through \$100,000; plus  
 B. 2 % of total costs in excess of \$100,000 but less than \$1,000,000; plus  
 C. 1 % of total costs in excess of \$1,000,000.

Expenditures subject to the overheads above will not be reduced by insurance recoveries, and no other overhead provisions of this Section III shall apply.

### 4. Amendment of Rates

The overhead rates provided for in this Section III may be amended from time to time only by mutual agreement between the Parties hereto if, in practice, the rates are found to be insufficient or excessive.

## IV. PRICING OF JOINT ACCOUNT MATERIAL PURCHASES, TRANSFERS AND DISPOSITIONS

Operator is responsible for Joint Account Material and shall make proper and timely charges and credits for all Material movements affecting the Joint Property. Operator shall provide all Material for use on the Joint Property; however, at Operator's option, such Material may be supplied by the Non-Operator. Operator shall make timely disposition of idle and/or surplus Material, such disposal being made either through sale to Operator or Non-Operator, division in kind, or sale to outsiders. Operator may purchase, but shall be under no obligation to purchase, interest of Non-Operators in surplus condition A or B Material. The disposal of surplus Controllable Material not purchased by the Operator shall be agreed to by the Parties.

### 1. Purchases

Material purchased shall be charged at the price paid by Operator after deduction of all discounts received. In case of Material found to be defective or returned to vendor for any other reasons, credit shall be passed to the Joint Account when adjustment has been received by the Operator.

### 2. Transfers and Dispositions

Material furnished to the Joint Property and Material transferred from the Joint Property or disposed of by the Operator, unless otherwise agreed to by the Parties, shall be priced on the following basis exclusive of cash discounts:

#### A. New Material (Condition A)

##### (1) Tubular Goods Other than Line Pipe

- (a) Tubular goods, sized 2 $\frac{3}{8}$  inches OD and larger, except line pipe, shall be priced at Eastern mill published carload base prices effective as of date of movement plus transportation cost using the 80,000 pound carload weight basis to the railway receiving point nearest the Joint Property for which published rail rates for tubular goods exist. If the 80,000 pound rail rate is not offered, the 70,000 pound or 90,000 pound rail rate may be used. Freight charges for tubing will be calculated from Lorain, Ohio and casing from Youngstown, Ohio.
- (b) For grades which are special to one mill only, prices shall be computed at the mill base of that mill plus transportation cost from that mill to the railway receiving point nearest the Joint Property as provided above in Paragraph 2.A.(1)(a). For transportation cost from points other than Eastern mills, the 30,000

1 pound Oil Field Haulers Association interstate truck rate shall be used.

- 2  
3 (c) Special end finish tubular goods shall be priced at the lowest published out-of-stock price, f.o.b. Houston,  
4 Texas, plus transportation cost, using Oil Field Haulers Association interstate 30,000 pound truck rate,  
5 to the railway receiving point nearest the Joint Property.  
6  
7 (d) Macaroni tubing (size less than 2 $\frac{3}{8}$  inch OD) shall be priced at the lowest published out-of-stock prices  
8 f.o.b. the supplier plus transportation costs, using the Oil Field Haulers Association interstate truck rate  
9 per weight of tubing transferred, to the railway receiving point nearest the Joint Property.

10  
11 (2) Line Pipe

- 12  
13 (a) Line pipe movements (except size 24 inch OD and larger with walls  $\frac{3}{4}$  inch and over) 30,000 pounds or  
14 more shall be priced under provisions of tubular goods pricing in Paragraph A.(1)(a) as provided above.  
15 Freight charges shall be calculated from Lorain, Ohio.  
16  
17 (b) Line pipe movements (except size 24 inch OD and larger with walls  $\frac{3}{4}$  inch and over) less than 30,000  
18 pounds shall be priced at Eastern mill published carload base prices effective as of date of shipment,  
19 plus 20 percent, plus transportation costs based on freight rates as set forth under provisions of tubular  
20 goods pricing in Paragraph A.(1)(a) as provided above. Freight charges shall be calculated from Lorain,  
21 Ohio.  
22  
23 (c) Line pipe 24 inch OD and over and  $\frac{3}{4}$  inch wall and larger shall be priced f.o.b. the point of  
24 manufacture at current new published prices plus transportation cost to the railway receiving point  
25 nearest the Joint Property.  
26  
27 (d) Line pipe, including fabricated line pipe, drive pipe and conduit not listed on published price lists shall  
28 be priced at quoted prices plus freight to the railway receiving point nearest the Joint Property or at  
29 prices agreed to by the Parties.  
30  
31 (3) Other Material shall be priced at the current new price, in effect at date of movement, as listed by a reliable  
32 supply store nearest the Joint Property, or point of manufacture, plus transportation costs, if applicable, to the  
33 railway receiving point nearest the Joint Property.  
34  
35 (4) Unused new Material, except tubular goods, moved from the Joint Property shall be priced at the current  
36 new price, in effect on date of movement, as listed by a reliable supply store nearest the Joint Property, or  
37 point of manufacture, plus transportation costs, if applicable, to the railway receiving point nearest the Joint  
38 Property. Unused new tubulars will be priced as provided above in Paragraph 2.A.(1) and (2).

39  
40 B. Good Used Material (Condition B)

41  
42 Material in sound and serviceable condition and suitable for reuse without reconditioning:

43  
44 (1) Material moved to the Joint Property

45  
46 At seventy-five percent (75%) of current new price, as determined by Paragraph A.

47  
48 (2) Material used on and moved from the Joint Property

49  
50 (a) At seventy-five percent (75%) of current new price, as determined by Paragraph A, if Material was  
51 originally charged to the Joint Account as new Material or

52  
53 (b) At sixty-five percent (65%) of current new price, as determined by Paragraph A, if Material was  
54 originally charged to the Joint Account as used Material.

55  
56 (3) Material not used on and moved from the Joint Property

57  
58 At seventy-five percent (75%) of current new price as determined by Paragraph A.

59  
60 The cost of reconditioning, if any, shall be absorbed by the transferring property.

61  
62 C. Other Used Material

63  
64 (1) Condition C

65  
66 Material which is not in sound and serviceable condition and not suitable for its original function until  
67 after reconditioning shall be priced at fifty percent (50%) of current new price as determined by  
68 Paragraph A. The cost of reconditioning shall be charged to the receiving property, provided Condition  
69 C value plus cost of reconditioning does not exceed Condition B value.  
70

1 (2) Condition D

2  
3 Material, excluding junk, no longer suitable for its original purpose, but usable for some other purpose  
4 shall be priced on a basis commensurate with its use. Operator may dispose of Condition D Material  
5 under procedures normally used by Operator without prior approval of Non-Operators.  
6

7 (a) Casing, tubing, or drill pipe used as line pipe shall be priced as Grade A and B seamless line pipe  
8 of comparable size and weight. Used casing, tubing or drill pipe utilized as line pipe shall be  
9 priced at used line pipe prices.  
10

11 (b) Casing, tubing or drill pipe used as higher pressure service lines than standard line pipe, e.g.  
12 power oil lines, shall be priced under normal pricing procedures for casing, tubing, or drill pipe.  
13 Upset tubular goods shall be priced on a non upset basis.  
14

15 (3) Condition E

16  
17 Junk shall be priced at prevailing prices. Operator may dispose of Condition E Material under  
18 procedures normally utilized by Operator without prior approval of Non-Operators.  
19

20 D. Obsolete Material

21  
22 Material which is serviceable and usable for its original function but condition and/or value of such Material  
23 is not equivalent to that which would justify a price as provided above may be specially priced as agreed to by  
24 the Parties. Such price should result in the Joint Account being charged with the value of the service  
25 rendered by such Material.  
26

27 E. Pricing Conditions

28  
29 (1) Loading or unloading costs may be charged to the Joint Account at the rate of twenty-five cents (25¢)  
30 per hundred weight on all tubular goods movements, in lieu of actual loading or unloading costs  
31 sustained at the stocking point. The above rate shall be adjusted as of the first day of April each year  
32 following January 1, 1985 by the same percentage increase or decrease used to adjust overhead rates in  
33 Section III, Paragraph 1.A.(3). Each year, the rate calculated shall be rounded to the nearest cent and  
34 shall be the rate in effect until the first day of April next year. Such rate shall be published each year  
35 by the Council of Petroleum Accountants Societies.  
36

37 (2) Material involving erection costs shall be charged at applicable percentage of the current knocked-down  
38 price of new Material.  
39

40 3. Premium Prices

41  
42 Whenever Material is not readily obtainable at published or listed prices because of national emergencies, strikes or other  
43 unusual causes over which the Operator has no control, the Operator may charge the Joint Account for the required  
44 Material at the Operator's actual cost incurred in providing such Material, in making it suitable for use, and in moving it  
45 to the Joint Property; provided notice in writing is furnished to Non-Operators of the proposed charge prior to billing  
46 Non-Operators for such Material. Each Non-Operator shall have the right, by so electing and notifying Operator within  
47 ten days after receiving notice from Operator, to furnish in kind all or part of his share of such Material suitable for use  
48 and acceptable to Operator.  
49

50 4. Warranty of Material Furnished By Operator

51  
52 Operator does not warrant the Material furnished. In case of defective Material, credit shall not be passed to the Joint  
53 Account until adjustment has been received by Operator from the manufacturers or their agents.  
54

55 V. INVENTORIES

56  
57 The Operator shall maintain detailed records of Controllable Material.  
58

59 1. Periodic Inventories, Notice and Representation

60  
61  
62 At reasonable intervals, inventories shall be taken by Operator of the Joint Account Controllable Material. Written notice  
63 of intention to take inventory shall be given by Operator at least thirty (30) days before any inventory is to begin so that  
64 Non-Operators may be represented when any inventory is taken. Failure of Non-Operators to be represented at an  
65 inventory shall bind Non-Operators to accept the inventory taken by Operator.  
66

67 2. Reconciliation and Adjustment of Inventories

68  
69 Adjustments to the Joint Account resulting from the reconciliation of a physical inventory shall be made within six  
70 months following the taking of the inventory. Inventory adjustments shall be made by Operator to the Joint Account for

1 overages and shortages, but, Operator shall be held accountable only for shortages due to lack of reasonable diligence.  
2

3 **3. Special Inventories**  
4

5 Special inventories may be taken whenever there is any sale, change of interest, or change of Operator in the Joint  
6 Property. It shall be the duty of the party selling to notify all other Parties as quickly as possible after the transfer of  
7 interest takes place. In such cases, both the seller and the purchaser shall be governed by such inventory. In cases  
8 involving a change of Operator, all Parties shall be governed by such inventory.  
9

10 **4. Expense of Conducting Inventories**  
11

12 A. The expense of conducting periodic inventories shall not be charged to the Joint Account unless agreed to by the  
13 Parties.  
14

15 B. The expense of conducting special inventories shall be charged to the Parties requesting such inventories, except  
16 inventories required due to change of Operator shall be charged to the Joint Account.  
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## EXHIBIT "D"

Attached to and made a part of that certain Operating Agreement by and between Merrion Oil & Gas Corporation, as Operator, and Non-Operators.

### INSURANCE

Operator shall at all times during the terms of this Agreement or an extension thereof, and at all times relative thereto, carry insurance to protect the parties hereto as follows:

- (a.) Statutory Workmen's Compensation Insurance as may be required in the state or states where work under this Agreement, or activities relative thereto, will be performed, plus Workmen Compensation Insurance as may be required by Federal Law, if applicable, plus Employers Liability Insurance.
- (b.) Public Liability Insurance with bodily injury limits of not less than \$5,000,000 for death or injury to one person, or not less than \$5,000,000 for death or injury to more than one person in any one accident and property damage liability insurance with a limit of not less than \$5,000,000 for any one accident, for loss of or destruction of or damage to property.
- (c.) Automobile Liability Insurance with bodily injury policy limits of not less than \$5,000,000 for death or injury to one person, or not less than \$5,000,000 for death or injury to more than one person in any one accident and property damage liability insurance with a limit or not less than \$5,000,000 for any one accident, for loss or or destruction of or damage to property.
- (d.) Operator shall require its contractors and subcontractors working or performing services on the contract area covered hereby to carry insurance in the types and amounts as set out in subsections (a), (b), and (c) hereinabove.

Operator agrees to furnish Non-Operator with acceptable certificates from the major drilling contractors, the contract pumper, and from the Operator, showing the effectiveness of the foregoing insurance coverage at least five (5) days before the commencement of actual drilling operations, such to contain a statement that such insurance shall not be materially changed or canceled without at least fifteen (15) days prior written notice to Non-Operator.

## EXHIBIT "E"

Attached to and made a part of that certain Operating Agreement dated  
February 1, 1997, by and between Merrion Oil & Gas Corporation  
as Operator, and Non-Operators.

### GAS BALANCING AGREEMENT

1. The parties to the Operating Agreement dated February 1, 1997, own working interests in the gas rights underlying the lands and leases covered by such agreement ("Contract Area") in accordance with the percentages of participation ("Working Interest") set forth therein.

2. Each party has the right to take, market, or otherwise dispose of its Working Interest share of gas produced from the Contract Area. Each party's Working Interest share shall be calculated on an MMBtu basis as determined at least semiannually by Operator through testing a sample of each gas stream following primary separation at the lease under standard conditions by means of chromatography or another accepted method used in the industry. All references in this agreement to quantity or volume shall be referred to as the number of MMBtu's contained in such volume or quantity of gas. No party shall take or market any gas production from less than the entire Contract Area in any manner that causes the Btu content of its taken or marketed gas production to vary in any material way from the Btu content of then current gas production from the entire Contract Area. In the event any party at any time does not take in kind or market its Working Interest share of gas from a well, or has contracted to sell its Working Interest share of gas to a purchaser which fails to take all or such gas, the other parties shall be entitled, in proportion to their Working Interest, to produce, take and deliver each month up to one hundred percent (100%) of the anticipated allowable gas production to be assigned to such well by the governmental entity having jurisdiction (if applicable). The purpose of this provision is to permit any party not taking or marketing all of its Working Interest share of current gas production to defer its production and permit the other parties to pass clear title to quantities of gas in excess of their Working Interest.

3. Each party which fails to take or market its full Working Interest share of gas from any well at any time shall be credited with gas in an imbalance account for such well equal to that volume of gas taken or marketed by the other parties hereto in excess of their Working Interest share.

4. Each party shall endeavor to take or market its full Working Interest share of gas production from each well. Further, each party shall give Operator reasonable notice and sufficient data either to nominate such party's Working Interest share of gas to the transporting pipeline(s) or, if Operator is not nominating such party's gas, to inform Operator of the manner in which to dispatch such party's gas. Except as and to the extent caused by Operator's gross negligence or willful misconduct, Operator shall not be responsible for any fees and/or penalties associated with imbalances charged by any pipeline to any Non-Operator.

5. To allow for the recovery of gas from an imbalance account and to balance the gas account of the parties, a party which has taken less than its full Working Interest share of gas at any time ("negative balance"), shall be entitled to produce, take and deliver each month upon reasonable notice to the Operator and to the other affected parties, its Working Interest share of the anticipated allowable gas production to be assigned to such well by the governmental entity having jurisdiction (if applicable) plus an amount up to an additional fifty percent (50%) ("Make-up Gas") of the Working Interest share of each party which has taken more

than its full share of gas at such time ("positive balance"). However, a party with a negative balance shall never be allowed to take more than its Working Interest share of such allowable gas (if applicable) during the months of November, December, January and February. If more than one party has a negative balance and elects to take Make-up Gas, they shall divide the Make-up Gas to be taken from any party with a positive balance in proportion to the respective working interest participation of each such party with a negative balance in such well.

6. This Agreement shall apply separately to each well, proration unit, conservation unit, and to each producing formation within such well, proration unit or conservation unit (unless such formation are accounted for all purposes as commingled production), and as to instances where any price controls apply to Make-up Gas, to each regulated price category; all uncontrolled gas is in a single price category for this purpose. The term "well" is used throughout the other paragraphs of this Agreement for convenience only and shall be deemed to include the other delineations herein set forth to the extent relevant. Imbalances in one well, proration unit, conservation unit, producing formation or category shall not be used for balancing any other well, proration unit, conservation unit, producing formation or category, as the case may be.

7. If, at the permanent termination of production of gas from a well, an imbalance exists between the parties, statements or invoices for a monetary settlement of the imbalance between any of the parties relative to such well shall be issued within one hundred eighty (180) days. Operator shall promptly provide all parties with a final cumulative balance for each party upon receipt of all relevant data from all other parties after permanent termination of production from each well. For the purposes hereof, the monetary settlement shall be based on the market value of gas at the time of the permanent termination of production of gas from a well. "Market value" shall be defined as the Inside FERC Index price, (first publication of the month), applicable to the area of production in which the well is located for the month in which the permanent termination of production of gas from the well occurs. If the Inside FERC Index is no longer in existence at the time of the permanent termination of production of gas from a well, then a prevailing, comparable index, mutually acceptable and agreeable by and among the affected parties, shall be the basis for the definition of "market value". "Permanent termination of production of gas" shall be defined as that point in time when a well is permanently plugged and abandoned. The amount of the monetary settlement due each party with a negative balance shall be its pro rata share (the ratio of each party's negative balance volume to the total negative balance volume for all parties) of the product of the market value of gas, as defined above, times the volume of gas which constitutes the positive balance, less production and severance taxes paid on positive balance volumes, and less royalties paid on positive balance volumes if paid on a gas taken basis. Each party with a positive balance shall provide a settlement schedule to each party with a negative balance detailing how its settlement amount was calculated. That portion of the proceeds by each party with a positive balance which is or may be subject to refund or other dispute by order(s) of the FERC, the Minerals Management Service, the courts or other authorities may be withheld by such party until such prices or disputes are fully resolved, unless the relevant parties with a negative balance furnish satisfactory undertakings agreeing to hold the relevant parties with a positive balance harmless from any financial loss due to the orders or disputes. Settlement as provided herein shall also be made by any party with a positive balance prior to any sale, assignment or other disposition of all or any part of its interest in any well in which such party has a positive balance. If the provisions of this Agreement are breached by the transferring party, any party receiving any part of the transferred interest shall be jointly and severally liable for its pro rata share of such positive balance upon the demand of any party with a negative balance.

8. Balancing payments from parties with a positive balance to parties with a negative balance under this Agreement shall be paid not later than sixty (60) days (1) after the amount of the monetary settlement due such party has been determined and a statement or invoice issued, or (2) after the date when the period for calculation of amounts due has passed, whichever is the earlier, pursuant to the provisions of Paragraph 7 above. No interest shall accrue or be due among the parties as to the period prior to this payment date. Interest on late payments (including payments rightfully made on a late basis because amounts are subject to potential refund or other dispute as stated in Paragraph 7 above or which are delayed because computations are not timely completed) shall accrue at the prime rate in effect at Chemical Banking Corp., New York, New York, at noon on the first day of the month in which the payment due date occurs plus two percent (2%) or the maximum contract rate permitted by applicable law, whichever is less. Attorneys' fees, court costs and other reasonable costs of collection of amounts owing due to breach of this Agreement shall also be payable to the affected party(ies).

9. Each party taking gas from a well shall promptly furnish or cause to be furnished to Operator a monthly statement of gas taken. Operator shall furnish to each party a statement of the gas balance among the parties, including the total quantity of gas produced from each well on a quarterly basis, the portion thereof used in operations, vented or lost, and the total quantity delivered for each party's account. Each party shall retain records of volumes of gas taken or marketed from each well and revenues or values accruing thereto for the full term of the Operating Agreement and two (2) years thereafter. Any party with either a positive or negative balance shall have the right during the two (2) years following each statement/invoice due date under Paragraph 7 above to audit the records of the other parties with positive or negative balances as to volumes, revenues, values and other relevant information concerning such well. No party will use any of the information obtained pursuant to the provisions of this paragraph for any other purpose than implementing the terms of this Agreement and enforcing rights thereunder.

10. In addition to any rights granted in the Operating Agreement, if any well produces casinghead gas and any party is not selling all of its Working Interest share, Operator shall have the right but not the obligation to sell the non-selling party's share of casinghead gas for the account of such party.

11. Each Party hereto shall share in and own the condensate recovered from each well by primary separation at the lease in accordance with its Working Interest in such well as provided in the Operating Agreement.

12. Gas used in lease operations, vented or lost shall not be considered taken by any party for purposes of the balancing hereunder. Nothing herein shall change or affect each party's obligation to pay its Working Interest share of all costs and liabilities incurred in accordance with such party's Working Interest.

13. At all times while gas is produced from the Contract Area, unless otherwise required by any laws, rules or regulations, each party shall make appropriate settlement of all royalties, overriding royalties and other payments out of or in lieu of production for which it is responsible ("royalty payments") as if each party were taking or delivering to a purchaser its Working Interest share and its Working Interest share only, of such gas production. Each party hereto agrees to defend, indemnify and hold each other party hereto harmless from all claims from royalty payments asserted by third parties to whom any party hereto is accountable.

14. Each party taking or marketing gas hereunder shall pay, or cause to be

paid, all production and severance taxes due on all volumes of gas actually taken or marketed by such party, unless otherwise required by any laws, rules or regulations.

15. Nothing contained herein shall be construed to deny any party the right, from time to time, to produce and take or deliver to its purchaser the entire well stream, if necessary, to meet such deliverability tests as may be reasonably required by its gas sales contract.

16. The parties shall communicate, as necessary, the contents of this Agreement to any of their respective gas purchasers or transporters and monitor their respective deliveries so as to ensure to the extent reasonably practicable that such third parties do not take gas in excess of the quantities provided herein.

17. This Agreement shall remain in force and effect as long as the Operating Agreement is in effect and thereafter until the gas balance accounts of the parties are settled in full or the audit period provided in Paragraph 9 has expired, whichever shall be longer. The obligations of the parties shall survive the termination of this Agreement.

## EXHIBIT "F"

Attached to and made a part of that certain Operating Agreement  
by and between Merrion Oil & Gas Corporation, as Operator, and Non-Operators.

### NONDISCRIMINATION AND CERTIFICATION OF NON-SEGREGATED FACILITIES

#### EQUAL EMPLOYMENT OPPORTUNITY

During the performance of the contract described above, Contractor agrees to the following additional terms and conditions to the extent they may be applicable to the work to be performed under such contract in accordance with the provisions of the following described Executive orders, Acts and implementing and regulations issued thereunder.

A. E.O. 11246, as amended by E.O. 11375 (Race, Color, Religion, Sex and National Origin)

1. If the contract is in excess of \$10,000, the Contractor agrees to comply with the provisions of Section 202 of such Order (the "Equal Opportunity clause"), which clause is incorporated herein, by reference pursuant to the regulations promulgated under such Order (41 C.F.R., Section 60-1.4(d)).

2. If the contract is in excess of \$10,000, the Contractor certifies that it does not maintain or provide, nor will it maintain or provide for its employees any segregated facilities at any of its establishments, and that it does not permit, nor will it permit its employees to perform their services at any location, under its control, where segregated facilities are maintained.<sup>1</sup> Contractor agrees that a breach of this certification is a violation of the Equal Opportunity clause of Executive Order 11246. Contractor further agrees that (except where it has obtained identical certifications from proposed subcontractors prior to time periods), it will obtain identical certifications from proposed subcontractors prior to the award of subcontractors exceeding \$10,000, which are not exempt from the provisions of the Equal Opportunity clause; that it will retain such certifications in its files; and that it will forward the prescribed notice to such proposed subcontractors (except where the proposed subcontractors have submitted identical certifications for specific time periods).<sup>2</sup>

3. If the contract is in excess of \$50,000 and the Contractor has more than 50 employees, the Contractor agrees (a) to file annually, on or before March 31, of each year, (or within 30 days after the award of such contract, if not filed within 12 months preceding the date of the award), complete and accurate reports on Standard Form 100 (EEO-1) with the appropriate governmental agency, in accordance with the regulations issued by the Secretary of Labor (41 C.F.R., Sec. 60-1.7), and (b) to develop a written affirmative action compliance program for each of its establishments in accordance with the regulations issued by the Secretary of Labor (41 C.F.R. Sec. 60-

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<sup>1</sup> As used in this certification, the term "segregated facilities" shall mean any waiting rooms, work areas, rest rooms and wash rooms, restaurants and other eating area, time clocks, locker rooms and other storage or dressing areas, parking lots, drinking fountains, recreation or entertainment areas, transportation and housing facilities provided for employees which are segregated by explicit directive or are in fact segregated on the basis of race, creed, color, or national origin because of habit, local custom or otherwise.

<sup>2</sup> The form of the prescribed notice is as follows: NOTICE TO PROSPECTIVE SUBCONTRACTORS OF REQUIREMENT FOR CERTIFICATIONS OF NONSEGREGATED FACILITIES. A Certificate of Nonsegregated Facilities, as required by the May 9, 1967 order of Elimination of Segregated Facilities, by the Secretary of Labor (32 Fed. Reg. 7439, May 19, 1967), must be submitted prior to the award of a subcontract exceeding \$10,000, which is not exempt from the provisions of the Equal Opportunity clause. The certification may be submitted either for each subcontract or for all subcontracts during a period (i.e., quarterly, semiannually, or annually). Note: The penalty for making false statements in offers is prescribed in 18 U.S.C. 1001.

1.40).

B. E.O. 11701 (Section 402-Veterans Readjustment Act of 1974)

If the contract is in excess of \$10,00, the Contractor agrees to comply with the affirmative action clause and regulations promulgated under such Order (41 C.F.R. Part 60-250) which clause is incorporated herein by reference pursuant to Section 60-250.22 of such regulations.

C. E.O. 11758 (Section 503-Rehabilitation Act of 1973)

If the contract is in excess of \$10,000, the Contractor agrees to comply with the affirmative action clause and the regulations promulgated under such Order (41 C.F.R. Part 60-741), which clause is incorporated herein by reference pursuant to Section 60-741.22 of such regulations.

D. E.O. 11625 (Minority Business Enterprises)

1. If the contact is in excess of \$10,000, the Contractor agrees to use its best effects to provide minority business enterprises with the maximum practicable opportunity to participate in the performance of such contract to the fullest extent consistent with the efficient performance thereof (41 C.F. R. Sec. 1-1.1310-2(a)).

2. If the contract is in excess of \$500,000, the Contractor agrees to comply with the Minority Business Enterprises Subcontracting Program clause promulgated under such Order (41 C.F.R. Sec. 1-1.1310-2(b)), which clause is incorporated herein by reference.

E. Section 905-Railroad Revitalization and Regulatory Reform Act of 1976

1. The contractor agrees to comply with the requirements of Title 49 C.F.R. 265 Subpart B of the regulations promulgated under such Act regarding "Nondiscrimination in Federally assisted Railroad Programs" and the nondiscrimination clauses therein are incorporated herein by reference.

2. If the contract is for \$50,000 or more, the Contractor agrees to comply with and implement the Affirmative Action Program established pursuant to Section 265.11 of 49 C.F.R.