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March 6, 2000

HAND DELIVERED

David R. Catanach, Hearing Examiner
Oil Conservation Division
New Mexico Department of Energy,
Minerals and Natural Resources
2040 South Pacheco Street
Santa Fe, New Mexico 87501

***Re: Update on North Square Lake Unit
Eddy County, New Mexico***

Dear Mr. Catanach:

By Order No. R-12113, dated June 17, 1999, the Division granted the application of GP II Energy, Inc. for statutory unitization of the North Square Lake Unit Area for the purpose of implementing a waterflood project in a portion of the Grayburg Jackson Seven Rivers-Queen-Grayburg-San Andres Pool. Ratifications were obtained from the owners of the required percentage of the working interest and royalty interest and the unit became effective on January 1, 2000.

The application for approval of the waterflood project is styled Case No. 12112. Following conversations with the Division and at GP II's request, no order will be entered in that case until an amended application is filed and additional data compiled on the wells in the area affected by this proposed waterflood.

To date GP II Energy, has restored to production 22 wells within the unit boundary and, as indicated on its initial plan of development, GP II has identified the first ten locations for the drilling of new producing wells. GP II has staked these wells and archaeological studies are being conducted this week. GP II will be filing permits to commence drilling operations at these locations in the immediate future. GP II hopes to drill these wells during the first half of 2000.

As you can see from the attached plat and list of wells and locations, these wells are concentrated in two areas within the unit area. The information obtained from these wells will enable GP II to take a concentrated look at these two portions of the reservoir and will assist GP II in the preparation of a revised Form C-108 which will be submitted to the Division with an amended request for approval of waterflood operations in these two initial injection areas. As we have discussed, once waterflood operations are commenced in these areas, GP II will file additional applications for expansion of the waterflood project in phases throughout the unit area. With this approach, GP II will be able to avoid the previous problem we experienced with the acquisition of well data from this very old producing area. We will be able to present the data necessary to satisfy the Division that this project can be implemented with injection confined to the authorized injection interval and without endangering fresh water supplies. Pursuant to Order No. R-11207, injection shall not commence in the Unit Area until the Division has approved the proposed waterflood project and enters an order in Case No. 12112.

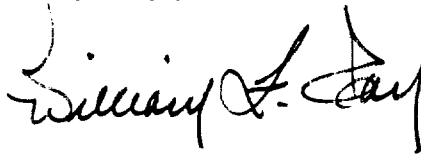
Since our conversations about recent communications to the Division from other operators concerning GP II's operations, GP II has met with representatives of Mack Chase and believes it has worked out with them how they will participate in this unit. We expect to take over operation of their leases in the next few weeks and will advise you when this has been accomplished.

As to the concerns of Staples and Jones, we would point out that they are the owners of non-operating working interest rights under GP II leases. This is an accounting issue which will not impact unit operations. However, with improved oil prices, everyone seems to be getting their business back in order and this problem should soon be resolved.

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We believe that after the trials and tribulations of getting to this point, GP II is now ready to start gathering the data necessary to revise its application for implementation of the waterflood project in the North Square Lake Unit Area. If you would like to meet with representatives of GP II to enable them to review their plans in more detail, I will be happy to arrange a meeting in Santa Fe at your convenience.

Very truly yours,

A handwritten signature in black ink, appearing to read "William F. Carr". The signature is written in a cursive style with a large initial "W" and a stylized "C".

William F. Carr
Attorney for GP II Energy, Inc.

WFC/md

cc: M. A. Sirgo III
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