



RECEIVED

JUL 25 2000

CAMPBELL, CARR, et. al.

State of New Mexico  
Commissioner of Public Lands

310 OLD SANTA FE TRAIL P.O. BOX 1148

SANTA FE, NEW MEXICO 87504-1148

RAY POWELL, M.S., D.V.M.  
COMMISSIONER

Legal Division  
(505) 827-5713  
Fax (505) 827-4262

July 21, 2000

VIA FAX AND  
U.S. MAIL  
(Fax - 983-6043)

Mr. William Carr  
Attorney at Law  
Campbell, Carr, Berge & Sheridan, P.A.  
P. O. Box 2208  
Santa Fe, New Mexico 87504-2208

RE: State Oil and Gas Lease Nos. VO-5682 & VO-5683; Sections 33 & 34, Township 21  
South, Range 34 East; LG&E Gas Storage Unit

Dear Mr. Carr:

I understand that you represent Nearburg Exploration Company and Yates Petroleum Corporation, BTA, Inc., who have interests in State Oil and Gas Leases Nos. VO-5682 and VO-5683, respectively. The purpose of this letter is to clarify the position of the New Mexico State Land Office ("NMSLO") regarding the gas storage unit that LG&E currently operates in Lea County. The storage unit underlies the west half of state section 34-21S-34E and the east half of section 33-21S-34E, which sections are also partially encumbered by your clients' leases.

Enclosed with this letter is page 3 of the Grama Ridge-Morrow Unit Agreement ("Unit Agreement"), which describes and delineates the "unitized formation" in which LG&E stores its gas. Although your clients are not parties to the Unit Agreement, and their leases are not modified by it, LG&E nonetheless had (and continues to have) valid existing storage rights at the time your clients obtained their leases. Therefore, VO-5682 and VO-5683 are subject to LG&E's existing right to store gas in the unitized formation and to use the surface of Sections 33 and 34 to the extent necessary to inject and withdraw its gas.

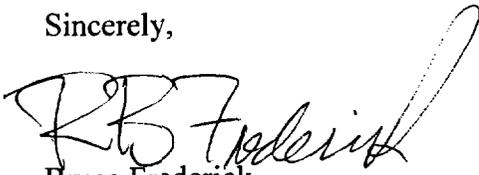
Despite the existence of LG&E's storage rights, your clients have the right under their oil and gas leases to explore for, and produce, native oil and gas on and below the leased premises. However, since they should not exercise their exploration and production rights in a manner that unreasonably interferes with LG&E's existing storage rights, NMSLO advises your clients to cooperate with LG&E and to coordinate their activities with LG&E to the extent possible.

Mr. William Carr  
Attorney at Law  
Campbell, Carr, Berge & Sheridan, P.A.  
July 21, 2000  
Page 2

Please note that the Commissioner regards both LG&E and your clients as valued business partners. With that in mind, NMSLO would be glad to help facilitate an agreement between LG&E and your clients that reasonably accommodates the interests of all parties.

If you have any questions regarding this letter, or would like to propose a resolution to the current situation, please do not hesitate to contact me. My direct line is (505) 827-5756.

Sincerely,

A handwritten signature in black ink, appearing to read "B. Frederick". The signature is fluid and cursive, with a large loop at the end.

Bruce Frederick  
Associate Counsel

pc: J. Scott Hall, Attorney for LG&E  
Dennis Hazlett, Deputy Commissioner, NMSLO  
Larry Kehoe, Assistant Commissioner, NMSLO

2. UNITIZED SUBSTANCES: All oil, gas, natural gasoline and associated fluid hydrocarbons in the unitized formation as hereinafter defined are unitized under the terms of this agreement and herein are called unitized substances.

3. UNITIZED FORMATION: That subsurface portion of the unit area commonly known as the Morrow sands which is the same zone as the top and bottom of which were encountered at log depths of 12,722 feet and 13,208 feet in the Shell Oil Company State GRA Well No. 1 as shown on the Schlumberger Sonic Log - Gamma Ray Log of said well dated July 5, 1965, which said well is located 1980 feet from the North line and 660 feet from the west line of Section 3, Township 22 South, Range 34 East, is unitized under this agreement and is hereinafter referred to as the "unitized formation".

4. UNIT OPERATOR: Llano, Inc. with offices at Hobbs, New Mexico (P.O. Drawer 1320) is hereby designated as unit operator and by signature hereto commits to this agreement all interest in unitized substances vested in it as set forth on Exhibit "B" and agrees and consents to accept the duties and obligations of unit operator for the operation of the Grama Ridge Morrow Unit Area. Whenever reference is made herein to the unit operator, such reference means the unit operator acting in that capacity and not as an owner of interests in unitized substances, and the term "working interest owner" when used herein shall include or refer to unit operator as the owner of a working interest when such interest is owned by it.

5. RESIGNATION OR REMOVAL OF UNIT OPERATOR: Unit operator shall have the right to resign at any time, but such resignation shall not become effective until a successor unit operator has been selected and approved in the manner provided for in Section 6 of this agreement.