

SALT WATER INJECTION WELL AGREEMENT

THIS AGREEMENT, made and entered into this 10th day of August, 1987, by and between MERLAND INC., a New Mexico corporation, P.O. Box 548, Carlsbad, New Mexico, 88220 ("Owner"), and RAY WESTALL, P.O. Box 4, Loco Hills, New Mexico, 88255 ("Operator"),

W I T N E S S E T H:

A. Owner owns the surface and mineral estate of the following described lands in Eddy County, New Mexico:

Township 22 South, Range 26 East, N.M.P.M.

Section 24: SW/4 SE/4

containing 40 acres, more or less,

subject to a certain Oil and Gas Lease dated July 10, 1972, by Owner to D. L. Hannifin, covering SE/4 of said Section 24, and now held by Operator as to horizons from the surface to the base of the Delaware formation;

B. The term "Property" as used hereinafter shall mean the entire SE/4 of Section 24, Township 22 South, Range 26 East, N.M.P.M., Eddy County, New Mexico;

C. The Property has located on it a well known as the Merland No. 1 Well, located 990 feet from the South line and 1,870 feet from the East line of said Section 24, which is not capable of producing oil or gas in commercial quantities, and which the parties agree may be used for the storage, removal,

disposal and transportation of salt water and other produced water, and which is hereinafter referred to as the "Wellsite";

D. Operator desires to utilize the Wellsite for the injection of water as hereinafter provided; and

F. Operator has applied to the New Mexico Oil Conservation Division for an Order authorizing Operator to re-enter and complete the Merland No. 1 Well in such a manner as to permit the injection of salt water for disposal purposes into the Cherry Canyon formation, and Owner has filed with the Division a Response and Objection to Operator's Application.

NOW, THEREFORE, for valuable consideration hereinafter described, the receipt and sufficiency of which are hereby acknowledged, and in consideration of the mutual covenants and agreements to be kept and performed by the parties, the parties agree as follows:

1. Right-of-Way. Owner grants Operator an easement and right-of-way over, through and across the Property along the course of the existing road thereon, for ingress to and egress from the Wellsite. The easement and right-of-way shall include, but not be limited to, the right to construct, maintain and operate a road, powerlines and all other facilities as will promote the use and enjoyment of the Wellsite, including, but not limited to, facilities to transport, inject, store and dispose of salt water and other produced water and to supply electricity and other power to the Wellsite. The right to construct, operate and maintain facilities shall include, but not be limited to, the

right to bury such facilities and powerlines below ground within the easement and right-of-way.

2. Pipeline Right-of-Way. Owner grants to Operator an easement and right-of-way over, through and across the Property for pipelines. This grant includes, but is not limited to, the right to construct, maintain, repair, remove and replace the pipelines, and Operator shall be entitled to use of so much of the surface of the Property as is reasonably required for the exercise of such rights. The pipelines shall be used for the storage, injection, disposal, or transportation of salt water and other produced water.

3. Salt Water Injection Well. Owner grants Operator the exclusive right to construct, maintain and operate facilities on the Wellsite for the perpetual storage, injection and disposal of salt water and other produced water. The facilities, hereinafter referred to as the "Salt Water Injection Well," shall be constructed on the Wellsite in a good and workmanlike manner in accordance with the standards of the industry. Operator shall utilize the existing well location for the Salt Water Injection Well and shall not enlarge the original pad without the written permission of Owner and the settling of surface damages for any such enlargement. The surface facilities for the Salt Water Injection Well shall include two 500-barrel tanks, one 750-gallon barrel and a water disposal pump, which shall be located within the existing fence. Upon written notice to Owner, Operator shall have the right to add additional surface facilities to the Salt

Water Injection Well should Operator deem the construction and maintenance of additional facilities to be necessary or desirable. Operator may repair or replace the fence at the Wellsite should Operator deem the replacement of the fence to be necessary or desirable.

4. Salt Water Well Payments. Operator shall pay Owner 3/16 of 25¢ (4.6875¢) per barrel of salt water injected by Operator into the Salt Water Injection Well. Payments shall be made by check to Owner monthly, within 30 days following the last day of the month for which payment is being made. Operator shall install a meter on the Salt Water Injection Well for the measurement of salt water and other liquid waste products injected into the well. Upon reasonable notice to Operator, Owner shall have the right to inspect the well meter and any books of account kept concerning the operation of said disposal well during normal business hours. Operator shall have the well meter on the Salt Water Injection Well recalibrated once each year and shall provide the results of such recalibration to Owner upon request.

5. Term. The term of this agreement shall begin as of the date this Agreement is executed by the parties and shall continue thereafter for so long as the Salt Water Injection Well established hereby is used or required for use by Operator. Operator may terminate this agreement at will, and shall thereafter be responsible only for payments then due, for plugging and abandoning the well in accordance with the rules and

regulations of the New Mexico Oil Conservation Division and for restoring the Wellsite in a good and workmanlike manner.

6. Insurance and Indemnification. Operator currently maintains a \$4,000,000 blanket insurance policy insuring against liability for operations within the City of Carlsbad, and during the term of this Agreement shall maintain the same or an equivalent policy. Operator shall save and hold Owner harmless from any and all loss, liability, expense, claim (including any and all costs and fees arising out of the litigation or settlement of any claims), or damages of any nature whatsoever arising, directly or indirectly, out of Operator's activities upon Owner's lands under the terms of this Agreement, including the activities or omissions of Operator's employees, contractors, agents or invitees.

7. Additional Well. Operator represents to Owner that prior to his drilling any new well on any acreage contiguous to the Property which well would be completed in the Cherry Canyon formation, he will drill one additional well in the SE/4 of Section 24 under the terms of the Oil and Gas Lease described in Paragraph A above. Operator shall not be liable to Owner, nor shall the term of the Oil and Gas Lease be affected, by Operator's failure to drill such additional well.

8. Oil Conservation Division Application. Upon execution of this Agreement by Owner and Operator, and prior to the hearing before the Oil Conservation Division, Owner shall withdraw its Response and Objection to Operator's Application to

re-enter and complete the Merland No. 1 Well to permit the injection of salt water for disposal, and in its withdrawal, Owner shall request the Oil Conservation Division to approve the Application.

9. Successors. In the event an assignment, transfer or conveyance of the agreements contained herein or the easements or rights-of-way herein granted to Operator, the heirs, successors and assigns of Operator shall be bound by the terms of this Agreement. This Agreement shall be binding upon, and its benefits and burdens shall inure to, the heirs, successors and assigns of Owner. The agreements herein contained and the easements and rights-of-way herein granted shall run with the Property and are not personal covenants.

10. Purpose. Operator has represented to Owner that the purpose of the disposal well is to dispose of produced water from his wells located on the Property or on lands adjacent to the Property. Should Operator desire to change the operation of the well to a commercial water disposal well disposing of salt water and other produced water from wells operated by others and produced from the same or other formations, Operator and Owner shall negotiate prior to such disposal, the terms concerning the operation of the disposal well and any safeguards necessary to protect the injection formation from permanent damage and the resultant waste of oil and/or gas that may be found therein. However, the payment provided for in Paragraph 4 hereof shall not be the subject of such renegotiation unless agreed to by both

parties. The provisions of this Paragraph 10 shall not apply, however, to the JFG Enterprise Kuklah Baby No. 1 Well, located in SW/4 NE/4 Section 24, and Owner hereby authorizes Operator to dispose of salt water produced from such well by injection into the Salt Water Injection Well.

ATTEST:

MERLAND INC.

James W. Brown
Secretary

By: Mary Frances Merchant
President

"Owner"

Ray Westall
RAY WESTALL

"Operator"

STATE OF NEW MEXICO)
) ss.
COUNTY OF EDDY)

The foregoing instrument was acknowledged before me this 10th day of August, 1987, by Mary Frances Merchant, the _____ President of MERLAND INC., a New Mexico corporation, on behalf of said corporation.

My commission expires:
11-25-89

Charles T. Lee
Notary Public

